RULE CHANGE

Australian Energy Market Commission

CONSULTATION PAPER

National Electricity Amendment (Changes to cost allocation method) Rule 2013

Rule Proponent(s)

Trans Tasman Energy Group

14 February 2013

For and on behalf of the Australian Energy Market Commission

Inquiries

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

E: aemc@aemc.gov.au
T: (02) 8296 7800
F: (02) 8296 7899

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About the AEMC

The Council of Australian Governments (COAG), through its then Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005. In June 2011, COAG established the Standing Council on Energy and Resources (SCER) to replace the MCE. The AEMC has two main functions. We make and amend the national electricity, gas and energy retail rules, and we conduct independent reviews of the energy markets for the SCER.

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1 Introduction

On 7 December 2012, Trans Tasman Energy Group (the proponent) submitted a rule change request to the Australian Energy Market Commission (AEMC or Commission). This rule change request proposes amendments to the distribution rules (Chapter 6), so that a Distribution Network Service Provider (DNSP)'s cost allocation method:

- is included in the distribution consultation procedures (Part G); and
- contains numeric values against the cost allocators.

The proponent considers that giving stakeholders the opportunity to review the cost allocation method, and increasing the transparency of the cost allocation process, would improve the capacity of customers to effectively negotiate access to distribution services. It also proposes to amend the negotiated distribution principles to provide for minimum pricing requirements for negotiated prices.

This Consultation Paper has been prepared by the staff of the AEMC to facilitate public consultation on the Rule change proposal and does not necessarily represent the views of the AEMC of any individual Commissioner of the AEMC.

This paper:

- sets out a summary of, and a background to, the rule change request;
- identifies a number of questions and issues to facilitate the consultation on this Rule change request; and
- outlines the process for making submissions.

Submissions

Submissions are to be received by 14 March 2013. Additional details on lodging a submission are included in Chapter 6 of this paper.

Timetable

The draft rule determination (and draft rule if applicable) is required to be published by 23 May 2013.

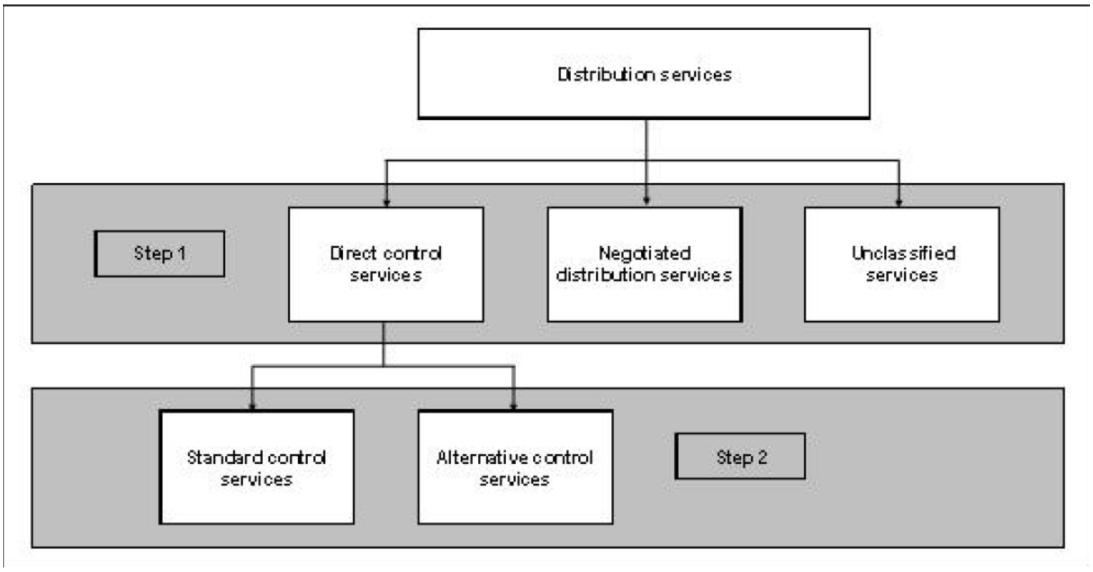
2 Background

This rule change request relates to two specific areas of Chapter 6 of the National Electricity Rules (NER): negotiated distribution services, contained in Part D; and cost allocation method, contained in Part F. An overview of each of these parts is provided below.

2.1 Negotiated distribution services

Negotiated distribution services area category of services for which the parties can negotiate the terms and conditions for services, including price. This is in contrast to direct control services for which the Australian Energy Regulator (AER) determines the maximum price that a DNSP can charge for a particular service.[1] Services that are not classified by the AER are not regulated under the rules. Direct control services must be further classified as either standard control or alternative control. This process is illustrated in Figure 2.1 below.

Figure 2.1 Distribution service classification process



In making its decision on service classification for direct control services, the AER is to have regard to a number of factors specified in the rules, which include:

- the potential for competition;
- the impact on administrative costs;
- the desirability for a consistent regulatory approach to similar services; and

1 Note in practice the AER may approve a maximum price change for a basket of services or the total revenue that a DNSP may recover from certain activities. For ease of reference, we refer to the AER's role in standard and alternative control as price setting, given the level of regulatory oversight.

- the extent to which costs are directly attributable to the customer to whom the service is provided.[2]

Once the AER classifies a service, there is no scope under the rules for the AER to change its classification of services or to classify new services within a regulatory control period.[3]

Direct control services are characteristically services where it is considered necessary to regulate the revenue earned by DNSPs through the AER making a distribution determination. Direct control services have price setting requirements for the AER under the rules. Pricing for negotiated services are determined by the negotiating parties; however, the process is bound by the requirements in the rules. This includes:

- the DNSP's negotiating framework; and

- the DNSP's negotiated distribution service criteria.

The negotiating framework forms part of a distribution determination. Therefore it is approved by the AER. It sets out the requirements that a DNSP is to comply with in respect of the preparation, replacement, application or operation of its negotiating framework. There are minimum requirements for the framework set out in the rules, including the kind of information the DNSP is required to provide to an applicant.

The determination also sets out the negotiated service criteria. The criteria are to be applied by the DNSP, in negotiating terms and conditions of access, and the AER in resolving an access dispute about terms and conditions of access. Terms and conditions of access include the price for a service. The price for a service differs from the cost of service. The cost relates to what the provider incurs in order to deliver the service and will likely differ from the price. However, the price for a negotiated service must be consistent with the cost allocation method. That is, the costs that are attributed to that category of services.

The negotiated distribution service criteria must give effect to and be consistent with the negotiated distribution principles. These principles are set out at clause 6.7.1 of the NER and generally relate to the relationship between the cost and price of a negotiated service. For example, the price for a negotiated distribution service should be based on the costs incurred in providing that service.

2.2 Cost allocation method

The cost allocation method is a document published by a DNSP which sets out how it will allocate costs between the different classes of services that it provides. Essentially it is a set of instructions to convert the statutory accounts (corporate reporting) into the regulatory accounts (for compliance with the economic regulatory framework). DNSPs are required to publish cost allocation methods under the rules. Its principal aim is to

2 NER, clause 6.2.2(c).

3 NER, clause 6.2.3.

ensure that an appropriate amount of costs are allocated to the activities that drive the relevant costs, and in particular between regulated and unregulated services. This is so customers of the relevant category of services are paying prices that reflect the cost of delivering those services. If a higher proportion of costs were allocated to one service (for example, standard control) relative to the costs of providing it, customers of that service would end up cross-subsidising other customers.

An important consideration for any cost allocation method is the distinction between direct and indirect costs. Direct costs are those that are incurred as a result of carrying out a specific activity and so can be easily attributed to it. For example, the labour and vehicle costs to fix a fault in the distribution network are directly related to providing standard control (or regulated) services. In contrast, indirect costs are those that relate to a broader range of activities and cannot be easily attributed to one and so are usually referred to as 'shared costs'. For example, overhead costs, such as the Chief Executive Officer's salary and the costs of the head office's premise, relate to providing all the services that the distribution business provides, including those that are unregulated.

Under the rules, the AER is required to develop cost allocation guidelines. DNSPs cost allocation methods are to be developed in accordance with the AER's guidelines. The guidelines are required to give effect to the cost allocation principles in the rules. There are seven cost allocation principles, which are:

“1. the detailed principles and polices used by a *Distribution Network Service Provider* to allocate costs between different categories of *distribution services* must be described in sufficient detail to enable the *AER* to replicate reported outcomes through the application of those principles and policies;

2. the allocation of costs must be determined according to the substance of a transaction or event rather than its legal form;

3. only the following costs may be allocated to a particular category of *distribution services*:

(i) costs which are directly attributable to the provision of those services;

(ii) costs which are not directly attributable to the provision of those services but which are incurred in providing those services, in which case such costs must be allocated to the provision of those services using an appropriate allocator which should:

(A) except to the extent the cost is immaterial or a causal based method of allocation cannot be established without undue cost and effort, be causation based; and

(B) to the extent the cost is immaterial or a causal based method of allocation cannot be established without undue cost and effort, be an allocator that accords with a well accepted cost allocation method;

4. any cost allocation method which is used, the reasons for using that method and the numeric quantity (if any) of the chosen allocator must be clearly described;

5. the same costs must not be allocated more than once;

6. the principles, policies and approach used to allocate costs must be consistent with the *Distribution Ring-Fencing Guidelines*;

7. costs which have been allocated to a particular service cannot be reallocated to another service during the course of a *regulatory control period*.[4]"

The regulatory determination process is highly dependent on the cost allocation method. This is because the revenues for direct control services are related to the costs that are attributed to providing those services. For this reason, it is important for the cost allocation method to be in place prior to a distribution determination and for it to remain stable, at least through the regulatory control period as the revenues have been determined using that particular method. Substantial changes in approaches even between periods will affect the comparability of costs between past and future periods.

The AER published its cost allocation guidelines in June 2008.[5] It was also required to publish a separate set of guidelines to apply to the Victorian DNSPs.[6] This set of guidelines was to be consistent with the Essential Services Commission's approach to enable consistency between future regulatory periods and historic periods.[7] The distribution consultation procedures apply to the development of and any amendment to the cost allocation guidelines.[8]

The initial cost allocation method was required to be submitted within twelve months of the commencement of the rules (which occurred on 1 January 2008) or accompanying the next regulatory proposal for the Victorian DNSPs.[9] The AER has six months to approve or refuse to approve a cost allocation method.[10] As part of giving approval, the AER may consult with the DNSP regarding amendments it views as necessary to gain approval.[11] Once the AER approves a DNSP's cost allocation method, DNSPs are required to comply with the approved cost allocation method and

4 NER, clause 6.15.2

5 AER, Electricity distribution network service providers, Cost allocation guidelines, June 2008.

6 These are included as Appendix A to the guidelines noted above.

7 NER, clause 11.17.4.

8 NER, clause 6.15.3(a) and (d).

9 NER, clause 6.15.4(a); NER, clause 11.17.5(a).

10 NER, clause 6.15.4(d).

11 NER, clause 6.15.4(e).

maintain a copy on its website.[12]The AER has approved a cost allocation method for each DNSP.[13]

However, under the transitional arrangements the DNSPs in New South Wales (NSW) and the Australian Capital Territory (ACT) were subject to separate arrangements for the regulatory period that followed the introduction of the NER (2009-2014). Under these arrangements, the cost allocation method which was approved was to be consistent with the method previously submitted to the relevant jurisdictional regulator[14] and submitted within one month of the NER commencing.[15]Following the 2009-2014 regulatory period, the NSW and ACT DNSPs will fall under the general provisions of the NER and will be subject to the AER's cost allocation guidelines.[16]

The AER has approved three amendments to cost allocation methods since the introduction of Chapter 6 of the NER.[17] DNSPs are also required to amend their cost allocation methods if required by the AER to take into account any change to the AER's cost allocation guidelines.[18] Similar provisions for cost allocation are also in place for transmission network service providers under Chapter 6A of the NER.[19]

2.3 Other relevant work

In November 2012 the AEMC released its final determination on the economic regulation of network service providers.[20] As part of the changes made, the NER now include a requirement for the AER to publish an annual benchmarking report setting out the relative efficiencies of network businesses.[21] Benchmarking analysis is also the focus of a current Productivity Commission Review.[22]

The cost allocation method is an important consideration in benchmarking analysis. This is because it determines how costs are recovered by different service categories. If DNSPs allocate costs between categories in materially different ways, it would be

12 NER, clause 66.154(h)

13 See the AER website, Determinations & Access Arrangements, Cost allocation method.

14 For the NSW DNSPs this was the Independent Pricing and Regulatory Tribunal (IPART) and for ActewAGL (of the ACT) it was the Independent Competition and Regulatory Commission (ICRC).

15 NER, chapter 11 appendix 1, 6.15.6-8.

16 However, following the AEMC's Economic Regulation of Network Service Providers final rule determination (see http://www.aemc.gov.au/Electricity/Rule-changes/Completed/economic-regulation-of-network-service-providers-.html) the NSW and ACT DNSPs are subject to a new set of transitional arrangements which affects the timing of their reviews.

17 See the AER website, Determinations & Access Arrangements, Cost allocation method.

18 NER, clause 6.15.4(g).

19 NER, Chapter 6A, part G.

20 AEMC, Economic Regulation of Network Service Providers, and Price and Revenue Regulation of Gas Services, Rule Determination, 29 November 2012.

21 NER, clauses 6.27 and 6A.31

22 Public Inquiry - Terms of Reference, received 9 January 2012 by the Productivity Commission (see http://www.pc.gov.au/projects/inquiry/electricity)

difficult to compare the costs of one DNSP to another for a particular sub-set of service costs. The AER has acknowledged this link with the development of its expenditure forecast assessment guidelines. In it, it states that "different approaches to cost allocation used by NSPs [network service providers] may be a potentially major source of incomparability in benchmarks."[23]

23 AER, Better Regulation: Expenditure forecast assessment guidelines for electricity distribution and transmission, Issues Paper, December 2012, p.141.

3 Details of the rule change request

There are three problems which the proponent is seeking to address with this rule change request:

- absence of consultation on cost allocation method;
- lack of transparency of the cost allocation method; and
- the binding nature of the principles to establish negotiated prices.

Each of these is discussed below.

3.1 Consultation on cost allocation method

The proponent states that the cost allocation method is a primary input to establishing prices for negotiated distribution services. As such, it argues that as an important part of the negotiation process, the cost allocation method should be open to review so customers can assess the appropriateness of any changes to DNSPs' cost allocation methods. It also notes that as a 'method', it should fall under the general categories subject to the distribution consultation procedures.[24] It therefore proposes to require the AER to comply with the distribution consultation procedures when accepting or amending a cost allocation method.[25]

The requirement is proposed to be included in the NER as a new clause inserted into clause 6.15.4:

> "The *AER* may, from time to time and in accordance with the *distribution consultation procedures*, amend or replace the *Distribution network Service Provider's Cost Allocation Method*.[26]"

In practice, this would require the AER to publish the relevant cost allocation method (or amendments) and invite written submissions from interested parties. It would then be required to publish a final decision on the cost allocation method, including its reasons and taking into account any public submission. This differs from the current process whereby the approval of cost allocation methods, and any subsequent amendments, are not subject to public consultation. Rather it is a document produced by the DNSP and submitted to the AER for approval. The AER has six months to make a decision. The AER may make amendments in consultation with the DNSP but there is no requirement to consult with any other parties. However, the AER's guidelines, of which the cost allocation methods need to comply, are subject to the distribution consultation procedures.

24 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, pp.3-4.

25 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.5.

26 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.7.

The proponent acknowledges that the introduction of consultation requirements is likely to impose costs on the AER. It does not expect that a requirement for DNSPs to publish additional information will impose significant costs as they will have already established such information in preparing their regulatory proposal.

3.2 Transparency of cost allocation method

The proponent is concerned that the current requirements for the cost allocation method in the NER are not sufficiently transparent to enable effective negotiation of prices under Part D of the NER. The cost allocation method under the NER is based on the cost allocation principles and the cost allocation guidelines, developed by the AER.

The proponent is specifically interested in the value of allocators. An allocator is the method by which a cost is allocated across different categories. For example, senior management salaries could be allocated based on the previous year's total revenue in each service. The value of that allocator will differ each year depending on the total revenue and the shares generated by each category.

The principles in the NER do not require the value of allocators to be published. However, the AER's guidelines require the value of an allocator to be published if it is to remain unchanged over the regulatory control period.[27] The proponent states that a requirement to publish the value of allocators would enable participants to identify and inform the reasonable costs of providing the service. Without access to such information, the proponent states that customers cannot establish for themselves whether the price offer is compliant with the NER including whether the same cost was allocated more than once.[28]

To give effect to the requirement for cost allocators, the proponent proposes amending the cost allocation principles (clause 6.15.2(4)) as follows:

> "any cost allocation method which is used, the reasons for using that method and the numeric quantity ~~(if any)~~ of the chosen allocator must be clearly described;[29]"

3.3 Principles to establish negotiated prices

The proponent also considers that the principles which underpin how negotiated prices are established should be binding. Specifically, that the first principle for determining a negotiated price should be based on the cost of providing it, determined in accordance with the cost allocation method.

It has proposed amending clause 6.7.1(1) as follows:

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27 AER, Electricity distribution network service providers: Cost allocation guidelines, June 2008, p.5.

28 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.7.

29 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.7.

> "the price for a *negotiated distribution service* ~~should~~ must be based on the costs incurred in providing that service, determined in accordance with the principles and policies set out in the *Cost Allocation Method* for the relevant *Distribution Network Service Provider*;[30]"

The proponent argues that a default position for how prices must be established is appropriate given the significant imbalance of market power that exists between the DNSP and negotiating party. It also states that although negotiating parties are free to determine how they establish prices it is relevant to have a required method if ever there is a case where the AER needs to set prices to resolve a dispute. The proponent also states that such a requirement will provide a clear direction as to how prices should be determined, and combined with the additional information provided under the changes proposed above, would better equip the negotiating parties.[31]

30 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.7.

31 Trans Tasman Energy Group, rule change request, 7 December 2012, p.7.

4 Assessment Framework

The Commission's assessment of this Rule change request must consider whether the proposed Rule promotes the National Electricity Objective (NEO) as set out under section 7 of the National Electricity Law (NEL). The NEO states:

> "The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to -
>
> (a) price, quality, safety, reliability, and security of supply of electricity; and
>
> (b) the reliability, safety and security of the national electricity system."

In assessing the rule change request against the NEO, the AEMC will consider the likely long term costs and benefits of adopting the rule change request compared to the counterfactual of not making the proposed change to the NER. It will also consider whether the proposed rule satisfies the rule making test in that it will, or is likely to, contribute to the achievement of the NEO.

In assessing the rule change request against the NEO, the Commission shall examine whether the proposed changes will lead to:

- regarding the cost allocation method:
  - improved transparency;
  - increased stakeholder engagement regarding amendments;
  - increased regulatory burden;
- regarding the negotiated services:
  - more efficient prices for network services.

The key aspect of this rule change is to improve the information available to participants negotiating services and to set specific requirements regarding the principles for negotiated prices. Such changes will contribute towards the achievement of the NEO if they can improve the efficiency of prices.

The assessment framework will be reviewed following the receipt of submissions and the AEMC's own analysis.

Question 1	**Is the assessment framework presented in this consultation paper appropriate for assessing this rule change request?**

5 Issues for Consultation

We have identified a number of issues for consultation that appear to be relevant to this rule change request. These issues outlined below are provided for guidance. Stakeholders are encouraged to comment on these issues as well as any other aspect of the rule change request or this paper including the proposed framework.

5.1 Significance and scope of the problem

The proponent has raised stakeholder consultation as an important forum for stakeholders to contribute to the development of a robust cost allocation method.

Consultation is a key tool in promoting transparency and efficiency in the market. However, in some instances, the costs of consultation may outweigh the benefits to the broader market. Therefore it is important to understand the extent to which changes to cost allocation method may impact different parties and the market more broadly, as this will assist in determining the scope of the identified problem and whether changes to the NER are required.

To gauge the scope of the problem that has been identified by the proponent, we propose to consider how often the cost allocation method is likely to be changed. How often the cost allocation method has changed and how frequently it may change in the future are important factors in understanding whether such changes are common or are limited to specific circumstances. This will help inform whether the costs of consultation will be outweighed by the benefits. For instance, if changes to cost allocation method occur frequently, it would need to be considered whether consultation requirements could become too onerous on DNSPs and market participants relative to the impacts on participants.

Question 2	How often is the cost allocation method likely to change? What are the costs for stakeholders, including the AER, of public consultation for a change in the cost allocation method?

The proponent has also proposed a change to the cost allocation principles, which would require DNSPs to include more information in their content requirements of a cost allocation method. The cost allocation principles are implemented through the AER's guidelines, which are subject to consultation requirements. The proponent states that the information it has proposed to be included in the principles will enable it to verify compliance and more effectively negotiate prices under the negotiated distribution services framework.

To better understand the scope of the problem identified by the proponent, we propose to consider how the contents of the cost allocation method are determined, its relationship with the AER cost allocation guidelines and how the cost allocation method is currently used by DNSPs. We will also examine where the cost allocation method fits in the broader revenue setting framework. In this context we note that in developing its expenditure forecast assessment guideline, the AER has raised the cost allocation method as a barrier to suitable comparability between network service providers:

> "The different approaches to cost allocation used by NSPs [network service providers] may be a potentially major source of incomparability in benchmarks...given the importance of benchmarking analysis we may consider mandating particular approaches to capitalisation and cost allocation across NSPs [network service providers] for the purposes of regulatory reporting, and seek views on alternative methods to overcome problems of incomparability in reporting.[32]"

Question 3	**What information is included in the cost allocation method in practice? How does this differ between DNSPs? Is comparability of cost allocation methods between DNSPs relevant to the negotiation framework? What is the cost of providing more detailed information of allocators?**

This rule change request focuses on the transparency of the cost allocation method and its role in the negotiated distribution principles. The specific clauses referred to in the rule change request were in Chapter 6, the distribution rules. However, the same rules are in Chapter 6A, which apply to transmission. There may possibly be a benefit from consistency between the two chapters. We are therefore interested in stakeholders' views as to whether the scope of the problems identified extend to transmission services as well.

Question 4	**Are the problems that the proponent identified also present in the transmission frameworks for cost allocation method and negotiated services?**

5.2 Assessment of proposed solutions

Consultation on cost allocation method

The proponent has proposed that any change to a cost allocation method be subject to the distribution consultation procedures under Part G of the rules. These provisions set out the requirements for the AER in conducting a public consultation where required under the rules "in making, developing or amending any guidelines, models or schemes, or in reviewing any values or methods".[33] Specifically, it sets out:

- publishing requirements, including explanatory statements (clause 6.16(b)(2));

32 AER, Better Regulation: Expenditure forecast assessment guidelines for electricity distribution and transmission, Issues Paper, December 2012, p.141

33 NER, clause 6.16(b)

- consultation periods, including the minimum number of business days for stakeholders to prepare written submissions (clause 6.16(c));
- limitations on time, including when the AER is required to publish its final decision (clause 6.16(e));
- requirements to consider all submissions received, including summarising and responding to each issue (clause 6.16(f)); and
- circumstances where the AER can extend the time required to publish its final decision (clause 6.16(g)).

These provisions currently apply to the AER's development and amendment of the cost allocation guidelines. It is therefore relevant to consider whether for each cost allocation method the same consultation procedures are appropriate, given the relationship between a cost allocation method and the AER's cost allocation guidelines. Particularly if the changes to a cost allocation method are the result of a change to the guidelines. We also note that the cost allocation method provisions require the AER to assess an amendment within six months.[34]

Question 5	**Is additional consultation required? Are the Distribution Consultation Procedures an appropriate framework for consultation in this context? Will the AER have sufficient time to adequately consider stakeholder views with the consultation procedures? Will consultation delay changes to a cost allocation method?**

Transparency of cost allocation method

The proponent has proposed amending the cost allocation principles in order to require numeric quantities of allocators to be included in a cost allocation method. The AER's cost allocation guidelines recognise that cost allocators can be stable (remain unchanged over time) or unstable (change over time).[35] This is because the allocator may be based on an item which changes from year to year, such as total revenue. A requirement to include the value of all allocators in a cost allocation method will therefore have implications for how often it will require revision, which would in turn increase consultation requirements if combined with the other changes proposed. It may be relevant to consider alternative approaches to achieve increased transparency of the value of allocators, such as by publishing a separate schedule.

Further, the proponent has stated that by including cost allocators it will enable stakeholders to verify compliance and in turn, encourage more effective negotiation.[36]

34 NER, clause 6.15.4(c).

35 AER, Electricity distribution network service providers: Cost allocation guidelines, June 2008, p.5.

36 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.4.

However, there are a limited suite of cost allocation groups[37] and far more prices for which those costs are divided.[38] It may therefore be difficult from the cost allocation method alone to ascertain the likely costs incurred to deliver a particular service.

Question 6	**Will the inclusion of numeric quantities require more frequent updating of cost allocation methods? Does the proposed solution to include numeric quantities achieve the aim of including sufficient information to replicate costs to be recovered?**

Principles to establish negotiated prices

The proponent has proposed amending the principles relating to access to negotiated distribution services so that costs are more clearly identifiable for negotiated distribution services. The principles are enabled through their influence on the negotiation criteria, which are approved by the AER as part of the revenue determination process. To examine the proposed solution, it is relevant to consider how the principles for negotiated access influence the criteria in practice. For example, the proponent has stated that ultimately the principles are included as negotiated distribution service criteria in the DNSP's negotiating framework. Further, that the AER has already recognised the benefit of the proponent's approach by including the same wording in the negotiated distribution services criteria in the South Australian distribution determination.[39]

It is also relevant to consider whether the principles (or criteria) alone can achieve the aims of the proponent's request. That is, whether making the amendment will lead to more effective negotiation and in turn, more efficient pricing. The proponent has claimed that DNSPs have significant market power, which if present, would affect the conduct and outcome of the negotiation process. The explicit aim is to have a fall back position for the AER in overseeing negotiations (or arbitrating disputes).[40] It is therefore relevant to consider whether the stated issue may be reflective of the nature of particular services in the negotiation category or a shortcoming of the rules. That is, whether the balance of regulatory oversight and market forces is appropriate in the negotiated services framework.

Question 7	**To what extent do the existing principles influence the**

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37 For example, SA Power Networks allocates costs between standard control, alternative control, negotiated distribution and unregulated (Cost allocation method September 2012, 3 September 2012).

38 For example, SA Power networks has twelve current network tariffs, each containing at least a couple components (such as a supply charge and different block usage rates) as well as other parameters such as time of use and locational prices (SA Power Networks, Tariffs 1 July 2012, available from its website (http://www.sapowernetworks.com.au/centric/industry/our_network/network_tariffs.jsp)). It also publishes a number of metering and connection related prices (SA Power Networks, Network tariff & negotiated services Manual No. 18, 3 September 2012).

39 Trans Tasman Energy Group, Proposed Rule Change Request, 7 December 2012, pp. 3 and 6.

40 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.5.

negotiation criteria? Is imposing a pricing requirement consistent with the level of regulation appropriate for negotiated services?

5.3 Implementation requirements

Assuming that there is a problem that requires a rule change to be made to the NER, the solution needs to be practical and the drafting of the rule needs to reflect the intended solution. Further, the proponent has recognised that should the cost allocation principles be amended, the cost allocation guidelines may also require amendment by the AER.[41] A significant change in the cost allocation guideline may require amendments to cost allocation methods.[42] Moreover, a change to require consultation on any change to a cost allocation method will add further consultation time and effort. Therefore, the implementation of any changes will need to consider the timing and resource commitments of stakeholders.

The implementation of such changes may also interact with existing regulatory determination reviews. For example, the NSW DNSPs are required to submit their next full regulatory proposals on 31 May 2014 and the framework and approach stage has already commenced.[43] For any changes to the relevant cost allocation method to be applied by the AER in its final decision, the changes should be made prior to submission of the regulatory proposal. This is because the cost allocation method is an integral component for the determination process. It affects how forecast operating and capital expenditure are calculated as well as the regulated asset base.[44] It is also relevant for dual function assets and shared assets.[45]

Changes to the cost allocation method during a regulatory control period therefore will not have an effect on revenues since "costs which have been allocated to a particular service cannot be reallocated to another service during the course of a regulatory control period."[46] Accordingly any change would only take effect for the subsequent regulatory control period unless transitional arrangements are put in place.

Question 8 **If the cost allocation principles are amended are the existing arrangements sufficient to enable compliance? Should transitional arrangements be considered to allow any rule changes to have effect as soon as possible?**

41 Trans Tasman Energy Group, Proposed Rule Change, 7 December 2012, p.4.

42 NER, clause 6.15.4(g).

43 AEMC, Economic Regulation of Network Service Providers, and Price and Revenue Regulation of Gas Services, Rule Determination, 29 November 2012, p.265.

44 See NER clauses 6.5.6-7, S6.2.

45 See NER clauses 6.26 and 6.4.4.

46 NER clause 6.15.2(7).

6 Lodging a Submission

The Commission has published a notice under section 95 of the NEL for this Rule change proposal inviting written submission. Submissions are to be lodged online or by mail by **14 March 2013** in accordance with the following requirements.

Where practicable, submissions should be prepared in accordance with the Commission's guidelines for making written submissions on Rule change proposals.[47] The Commission publishes all submissions on its website subject to a claim of confidentiality.

All enquiries on this project should be addressed to Tara D'Souza on (02) 8296 7800.

6.1 Lodging a submission electronically

Electronic submissions must be lodged online via the Commission's website, www.aemc.gov.au, using the "lodge a submission" function and selecting the project reference code "ERC0150". The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated.

Upon receipt of the electronic submission, the Commission will issue a confirmation email. If this confirmation email is not received within 3 business days, it is the submitter's responsibility to ensure the submission has been delivered successfully.

6.2 Lodging a submission by mail

The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated. The submission should be sent by mail to:

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Or by Fax to (02) 8296 7899.

The envelope must be clearly marked with the project reference code: ERC0150.

Except in circumstances where the submission has been received electronically, upon receipt of the hardcopy submission the Commission will issue a confirmation letter.

If this confirmation letter is not received within 3 business days, it is the submitter's responsibility to ensure successful delivery of the submission has occurred.

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47 This guideline is available on the Commission's website.

Abbreviations

ACT	Australian Capital Territory
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Commission	See AEMC
DNSP	Distribution Network Service Provider
ICRC	Independent Competition and Regulatory Commission
IPART	Independent Pricing and Regulatory Tribunal
NEL	National Electricity Law
NEO	National Electricity Objective
NER	National Electricity Rules
NSW	New South Wales
proponent	Trans Tasman Energy Group