



Australian Inland Energy and Water

**SUBMISSION TO IPART
RE
FORM OF ECONOMIC REGULATION
OF DNSP's COMMENCING JULY 2004**

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Australian Inland Energy and Water welcomes the opportunity to make a submission to the Independent Pricing and Regulatory Tribunal (IPART) regarding the form of economic regulation to apply to distribution network service providers (DNSPs) for the regulatory period commencing 1 July 2004.

Form of economic regulation

Section 2.2 of the Draft notice states that the proposed weighted average price cap will vary for each year by an X factor, and possibly other certain factors including service quality incentive mechanisms, a correction factor to transition factors from the current regulatory period to be carried forward, and a benefit sharing mechanism to account for significant differences between forecast and actual throughput.

Considering the variable load growth throughout the AIEW network affected by factors outlined below, there is a greater risk to revenue recovery with a weighted average price cap than with a traditional revenue cap. A correction mechanism should be included to allow for significant differences between forecast and actual throughput, as outlined in the draft notice, particularly for the AIEW circumstances where there is minimal annual load growth and significant throughput variability year to year due to climatic and general economic factors.

Volume forecasts

AIEW agrees that inaccurate forecasts of throughput and customer numbers can substantially impact on the profitability, particularly under a weighted average price cap.

AIEW does not enjoy consistent growth in terms of customer numbers that occurs within other distribution networks, therefore forecasting customer numbers for each year within the regulatory period should be reasonably accurate.

However, the kWh throughput and network maximum demand are greatly influenced by high summer temperatures, annual rainfall across agricultural areas serviced by the network, general economic prosperity, and commercial developments that often have short planning horizons (from the customer's perspective) and represent significant spot loads to be connected to the distribution network, rather than consistent load growth.

Reference to a mechanistic approach based on historical growth rates or load profiles is likely to produce estimates with a larger error than those based on forecasts prepared by AIEW, although the accuracy of these is eroded by application of the above externalities.

Some correction mechanism must be provided to allow for variation in energy throughput and maximum demand from one year to another, that effects not only the revenue that can be recovered from customers, but also TUOS estimates, that now have a greater alignment to monthly energy and demand.

Other regulatory arrangements

Consistent with section 6.10.5(c) of the Code, the regulatory control period will be a minimum of 3 years, and the Tribunal may impose a longer regulatory period.

The regulatory period should be of sufficient duration to provide regulatory consistency and certainty, with clearly defined principles relating to treatment of capital expenditure and re-valuation of the regulatory asset base between determinations.

At the February public forum, AIEW expressed the view that transition from the existing determination to the new determination, considering side-constraints on annual price increases, will be its main issue. Existing under-recovery of network revenue, increasing operating costs, significant increases in TUOS, and the negligible load growth, apart from some specific mining projects, are the main factors to be considered in any transitional arrangements.

Indicative timetable for 2004 review

The indicative timetable for the 2004 review process in the Draft Notice issued on 6 May appears fairly optimistic in terms of DNSP's submitting their first written submissions and initial pricing proposals in October 2002, including customer willingness to pay evidence.

NSW Treasury is currently coordinating a Willingness to Pay consultancy on behalf of the four DNSP's, and this is not due to be completed until December 2002.

Treasury is also coordinating an asset valuation consultancy, that will be an input to both the building block revenue calculation and the roll forward of the asset base.

Considering the annual compliance and regulatory reporting required to be completed in the July – August period, including Network Management reports to the MoEU, Australian Inland Energy and Water considers that the indicative timetable is particularly onerous. Accordingly, AIEW requests that the first submissions and initial pricing proposals be deferred until April 2003, the due date for the second public submissions, with the indicative timetable adjusted to achieve the release of the final report on 30 March 2004.

Considering the timetable discussed at the Network Service Standards Consultative Group meeting on 23 May for service standards and reliability reporting under the National Regulatory Reporting Requirements, it appears that the indicative timetable has already been revised to accommodate this aspect.

Conclusion

Australian Inland Energy and Water requests that IPART include a correction mechanism in the weighted average price cap to allow for significant differences between forecast and actual throughput, as outlined in the draft notice, particularly for the AIEW circumstances where there is minimal annual load growth and significant throughput variability year to year due to climatic and general economic factors.

Further, AIEW requests that IPART revise the indicative timetable for the 2004 review, to defer the requirement for first written submission from DNSPs to at least April 2003, being the nominated time for the second submissions. In particular this will allow completion of the willingness to pay study and better integration of the results within the pricing proposals, as well as more detailed analysis on a number of other important matters, such as service standards and asset valuations.

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