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EnergyAustralia®

12 February 2010

Dr John Tamblyn
Chairman
Australian Energy Market Commission
Level 5, 201 Elizabeth Street
SYDNEY NSW 2000

By email to: submissions@aemc.gov.au

Dear Dr Tamblyn

EnergyAustralia's submission on ETSA proposed Rule for feed in tariff payments

EnergyAustralia welcomes the opportunity to comment on ETSA's proposed changes to Chapter 6 of the National Electricity Rules (Rules). Our detailed submission is attached to this letter.

EnergyAustralia supports ETSA's proposed Rule, which permits a distributor to adjust annual prices to recover payment obligations pursuant to a feed in tariff scheme or the Climate Change Fund. We consider this mechanism is more appropriate than recovering the costs through the building block determination, for three key reasons:

- The distributor is not financially penalised (rewarded) for a cost that is outside of its control if actual costs are higher (lower) than forecast;
- Forecasting error is minimised under an annual pricing process and any error can be rectified using a straight forward under-over recovery mechanism, as opposed to complex pass through arrangements; and
- There is greater transparency for the customer as to the charges associated with the schemes.

The proposed Rule is particularly important for NSW distributors. The NSW Solar Bonus Scheme commenced on 1 January 2010, and imposes an obligation on NSW distributors to provide a credit against charges to a small retail customer for electricity produced by a generator connected to the distribution network. Our early (and very conservative) estimate is that the costs of bonus payments for EnergyAustralia will be upwards of $100 million over the 2009-14 regulatory period, but this amount could prove to be materially higher if the take up of the scheme is greater than forecast at this time.

Our issue is that neither the Rules nor the AER's regulatory determinations for NSW distributors for 2009-14 have an explicit mechanism to allow us to meet the obligations under the scheme. In the absence of Rules regarding recovery through the annual pricing process, other jurisdictions such as the

ACT, South Australia and Queensland have dealt with the recovery of feed in tariff payments by way of an operating cost allowance and an AER determined pass through arrangement.

However, unlike other jurisdictions, the AER's determination did not provide for a specific pass through event related to feed in tariff schemes for NSW businesses. EnergyAustralia would be required to satisfy the AER that another defined pass through event has occurred and that the materiality threshold has been satisfied. It is also uncertain as to whether the AER's pass through determination would be able to include an over and under recovery adjustment. Without such an adjustment, customers would face a windfall loss or gain from any forecasting error at the time of the pass through application.

The mechanism proposed by ETSA would enable NSW distributors to recover payments made under the NSW Solar Bonus Scheme through the annual pricing approval process. We support this approach. However, ETSA's proposed Rule does not amend the Transitional Rules (Appendix I of Chapter 11 of the Rules), which apply to NSW distributors until the completion of the 2009-14 regulatory period.

Including consequential amendments in the Transitional Rules enables the recovery mechanism, proposed by ETSA, to also apply to NSW distributors in respect of recovering the payments it makes under the NSW Solar Bonus Scheme in the 2009-14 period.

EnergyAustralia notes that the Transitional Rules already have provisions in place which enable NSW distributors to recover payments into the Climate Change Fund as part of the AER's annual price approval process. We consider that consequential amendments to the Transitional Rules would require less drafting complexity than the ETSA Rule change, as it can mirror the existing provisions for the Climate Change Fund, and the provisions relating to the TUOS under and over recovery.

Given the pressing issues faced by NSW distributors, we request that the AEMC expedite ETSA's proposed Rule change and also make consequential amendments to the Transitional Rules. If you have any questions on this matter, please contact Ms Jane Smith on 9269 4171.

Yours sincerely

TREVOR ARMSTRONG
Executive General Manager
System Planning and Regulation

EnergyAustralia's submission on ETSA Rule change Payments under feed in tariff schemes and climate change funds - February 2010

1 Structure of submission

EnergyAustralia's submission is structured as follows:

- We provide background on the feed in tariff scheme and Climate Change Fund currently applying in New South Wales and the types of costs that a NSW distributor incurs under these schemes.
- We explain why the recovery of such payments is best addressed as part of the annual pricing approval process, rather than included in the building block costs of a regulatory determination. In doing so, we address the issues raised by the AEMC in its discussion paper of 14 January 2010.
- We note that the Rule change is a pressing issue for NSW distributors, who have no explicit mechanism in the Rules or in the 2009-14 regulatory determinations to recover payments made under the NSW Solar Bonus Scheme. As such we suggest consequential amendments to the Transitional Rules to provide regulatory certainty to NSW DNSPs that they are able to recover payments made under the scheme.
- We make comments on the drafting of the proposed Rule.

2 Schemes applicable to the NSW jurisdiction

The NSW Solar Bonus Scheme commenced on 1 January 2010. Under the scheme, NSW electricity distributors must provide customer connection services to a small retail customer wishing to connect a generator with a generating capacity of no more than 10 kilowatts to the distribution network. The NSW electricity distributors must record a credit against charges payable at the amount of $0.60 cents per kilowatt hour to the small retail customer for electricity produced by the generator connected to the distribution network.

NSW electricity distributors face 3 obligations under the scheme:

(i) pay the bonus of 60 cents/ kwh to customers who own qualifying generators;

(ii) connect a complying generator; and

(iii) have systems to implement the recording, information keeping and reporting on the scheme.

NSW distributors also have obligations with respect to the NSW Government's Climate Change Fund. Under the scheme, the responsible NSW Minister can direct a distributor to make payments into the Fund. The distributor recovers the costs associated with these payments from customers.

The NSW Solar Bonus Scheme and Climate Change Fund impose two types of costs on the distributor:

- The payments made to eligible customers under the NSW Solar Bonus Scheme and payments made into the Climate Change Fund.
- Other costs resulting from obligations under the schemes. For instance, under the NSW Solar Bonus Scheme, EnergyAustralia incurs capital costs associated with procuring, designing and testing meters. This category of costs would also include the implementation and administration costs of the schemes, such as staff time.

We note that ETSA's Rule change only applies to payments made pursuant to a Feed in Tariff scheme and the Climate Change Fund. EnergyAustralia agrees that other costs associated with the schemes are

relatively within the control of the distributor, and should be recovered through the building block determination or pass through mechanism.

3 Cost recovery mechanisms

The AEMC may only make a rule if it is satisfied that the Rule will or is likely to contribute to the achievement of the National Electricity Objective (NEO) set out in section 7 of the National Electricity Law.

In addition, a clear intent of jurisdictional policy makers is for distributors to recover the costs of the schemes through the prices charged to the broader distribution customer base. As such, the revenue and pricing principles in the National Electricity Law , specifically principles (2) and (3), are relevant

> (2) "A regulated network service provider should be provided with a reasonable opportunity to recover at least the efficient costs the operator incurs in—
>
> (a) providing direct control network services; and
>
> (b) complying with a regulatory obligation or requirement or making a regulatory payment, a regulated network service provider should be provided with a reasonable opportunity to recover at least the efficient costs the operator incurs in complying with a regulatory obligation or requirement making a regulatory payment"[1]
>
> (3) A regulated network service provider should be provided with effective incentive in order to promote economic efficiency with respect to direct control services the operator provides.

The key issue raised by ETSA's proposed Rule is the appropriate mechanism to recover the payments that a distributor incurs under the respective schemes. ETSA notes two potential cost recovery mechanisms. Firstly, the forecast costs for the regulatory period could be included as part of a building block determination for direct control services, with the costs reflected in X-factors. In this case, the risk of forecasting error over the five years could be accommodated through a nominated pass through event, which would effectively operate as an under and over recovery adjustment.

A second mechanism, as proposed by ETSA, is to enable distributors to provide for tariffs to pass on to customers the payments incurred under the schemes. This would be separate to the X-factor constraints. The process would occur as part of the annual pricing proposal. ETSA's proposed mechanism includes an adjustment for over and under recovery of payments from the previous year.

The latter mechanism is not currently permitted by Chapter 6 of the Rules, which only provides for revenue adjustments for TUOS charges. Similar limitations apply to the Transitional Rules, except that NSW distributors can also make revenue adjustments for payments made into the Climate Change Fund.

The limitation in the Rules was raised by the AER in its final determination for ActewAGL when it noted that:

> "Clauses 6.18.7 and 16.18.2b (5A) of the transitional chapter 6 rules state that revenue adjustments can be made for transmission use of system (TUOS) charges and in the case of the NSW DNSPs, the Climate Change Fund. As the transitional chapter 6 rules do not provide a more general exception or an exception specific to the FiT scheme, the AER considers that a pricing proposal cannot be used to adjust revenues in relation to the FiT scheme."[2]

[1] National Electricity (South Australia) Act 1996, Schedule, Part, Section 7A(2)
[2] Australian Energy Regulator, Final decision Australian Capital Territory distribution determination 2009–10 to 2013–14, 28 April 2009, p69.

Which mechanism is more appropriate?

The threshold question for the AEMC is whether the recovery of costs for the schemes are more suited to a revenue adjustment in a pricing proposal or inclusion as a cost in a building block determination. This will in turn inform the AEMC as to whether the proposed Rule will or is likely to contribute to the achievement of the national electricity objective.

This question did not arise in the context of the MCE's review of the general Chapter 6 Rules as, at the time, no jurisdiction was subject to a feed in tariff scheme. In contrast, when the MCE was drafting the Transitional Rules, it was required to consider the recovery arrangements for payments made into the NSW Climate Change Fund. The MCE decided that recovery of Climate Change fund payments was to be separate from the building block determination and was to be recovered through the annual pricing approval process.

There are three policy reasons why EnergyAustralia considers that the mechanism implemented by the MCE for the NSW Climate Change Fund, and that which is now proposed by ETSA for feed in tariff payments, best meets the relevant revenue and pricing principles and will contribute to the achievement of the NEO:

- the payments are outside of the control of the distributor and therefore should not be subject to the incentives under a building block approach.
- customers pay the exact recovery amount under the pricing Rules, without the need for costly and complex administrative arrangements through pass through mechanisms.
- there is more transparency on the charges that customers pay.

(i) Payments are outside the control of the distributor

Distributors are subject to range of costs, some of which can be heavily influenced by the actions of the distributor, and others which are relatively outside the control of the business. The building block framework is designed to provide financial rewards or penalties to incentivise regulated businesses to efficiently reduce their costs and/ or improve service levels. Clearly, these incentives are targeted at the costs which are under the control of the distributor.

We submit that a statutory 'levy type' requirement (where the payment amount varies from year to year) is best recovered through an annual pricing/ revenue adjustment rather than incorporated through X-factor control. The pricing mechanism ensures that the actual costs of the scheme for that year are passed onto customers, and that there is no loss or gain for under or over recovery of payments relative to recovery obligations under the scheme. This is turn will contribute to the achievement of the national electricity objective as it will promote the efficient investment in and efficient operation and use of electricity services for the long term interests of consumers with respect to price, referred to here as the price element of the NEO.

For the same reason the MCE developed general chapter 6 Rules to include TUOS recovery in the pricing provisions. The MCE made a similar policy decision with respect to Climate Change Fund payments when enacting the Transitional Rules.

In the case of feed in tariff and climate change fund payments, the cost cannot be controlled or influenced through more efficient behaviour by the distributor. There is a risk under the building block approach that a distributor will be penalised (rewarded) for payments that exceed (are below) the forecast expenditure allowance, despite this cost being outside of its control. This dilutes the incentive properties in the regulatory framework for distribution networks.

To make this point clear, EnergyAustralia notes that the AER has developed an efficiency benefit sharing scheme that provides financial incentives to efficiently reduce operating costs. The scheme excludes uncontrollable costs. Despite this, there is an inherent incentive in the regulatory framework, which penalises (rewards) a DNSP if it overspends (underspends) its total operating expenditure allowance, irrespective of whether the cost is controllable. The upshot is that there is no mechanism to recoup lost revenue, if uncontrollable costs are higher than forecast.

Assume for example, that distributor forecast that the impact of the scheme will be $150 million, and sought to include the impact through forecast operating expenditure at the time of regulatory proposal or through pass through application. If the actual impact was $170 million, the distributor will incur a revenue penalty of $20 million over the regulatory control period. This is despite having no control over the payments under the scheme. Conversely, customers would bear a $20 million penalty if the costs of the scheme ended up being $130 million. As discussed below, the AER's determination for ActewAGL tried to address the problem of windfall gains or losses by nominating a pass through event to deal with forecasting error.

(ii) Deals better with under/over recovery

We note that a building block approach requires a five year projection of payments, while a pricing proposal is based on a yearly forecast which incorporates latest information on take-up rates and payment levels. There will consequently be less forecasting error under ETSA's proposed Rule. In our responses to the AEMC's questions, set out at Attachment A, we note the multitude of factors affecting take up rates of a feed in tariff scheme.

Further, the mechanism for correcting forecast error is relatively simple under ETSA's proposal. The AER would approve the revenue adjustment if it was satisfied that the forecast, including any under or over recovery from the previous year, was reasonable. It would be uncomplicated for the AER to verify this amount.

The sole mechanism for addressing forecasting error under the building block approach is via an 'unders and overs' pass through event specific to feed in tariffs and Climate Change Fund recovery amounts. The AER's current approach in this respect is summarised in the final determination for Actew AGL:

> "…the AER considers that ActewAGL should not bear the risk of forecasting error, in respect of the direct tariff payments made under the FiT scheme. The AER is of the opinion that differences between actual and forecast direct tariff payments to the retailer should form the basis of a nominated pass through event under the relevant provisions of the transitional chapter 6 rules."[3]

Under this mechanism, distributors such as ActewAGL would need to make a positive or negative change pass through event application, for each year that an under or over recovery has occurred. The AER would assess that application in accordance with the Rule provisions and any materiality threshold that applies. Such an annual process is administratively cumbersome. Further, it is unclear under the Rules whether a distributor would obtain a pass through of costs to correct for under and over recovery of revenue in the last year of a regulatory period.

In our view, a pass through mechanism is a second best solution to recover these type of recovery obligations. The intent of policymakers was for the distributor to recover the only the actual costs of payments made to customers, and it is clear that the pricing mechanism is far more effective at facilitating this objective. Again this will promote the achievement of the price element of the NEO as it will provide more transparency for customers as discussed in (iii) below.

[3] Australian Energy Regulator, Final decision Australian Capital Territory distribution determination 2009–10 to 2013–14, 28 April 2009, p69.

(iii) More transparent for customers

ETSA's proposed Rule change provides more transparency to customers on the cost incurred under the schemes. ETSA's amendments to the billing for distribution services require a distributor to identify the feed in tariff and climate change fund charge for each connection point. In contrast, the building block approach obfuscates the charge paid by the customer as part of total DUOS payments.

AEMC discussion paper

We note that the discussion above addresses many of the issues raised by the AEMC in its discussion paper of 14 January 2010. EnergyAustralia has responded to the specific questions asked by the AEMC at Attachment A.

We consider that while the AEMC has raised relevant issues, it could also investigate the effectiveness of the current arrangements in the transitional Rules for recovery of Climate Change Fund payments. In our view, the current provisions provide a clear and simple mechanism for distributors to pass through the costs of a statutory imposed levy on distributors.

We note that these effective arrangements will expire at the end of EnergyAustralia's 2009-14 regulatory period. In the event that the AEMC do not make ETSA's proposed Rule, we consider the AEMC should, as a minimum, incorporate a provision in the general Chapter 6 Rules to ensure the current arrangements in the Transitional Rules with respect to the NSW Climate Change Fund apply to NSW distributors for future regulatory periods.

4 Amendments to NSW Transitional Rules

We note that ETSA's proposed Rule only applies to the general Chapter 6 Rules and that no consequential amendment has been proposed for the Transitional Rules (Appendix I of Chapter 11 of the Rules) that apply to NSW distributors for the 2009-14 regulatory period.

As noted earlier, the NSW Solar Bonus Scheme commenced on 1 January 2010. Due to the timing of the scheme, the AER's determinations for NSW distributors for the 2009-14 regulatory control period did not allow for the costs associated with meeting the obligations under the scheme. This puts us in a disadvantaged position compared to other jurisdictions such as Actew AGL, which have an allowance for payments incorporated into its X-factors.

Further, there is no specific pass through event in the Rules for a feed in tariff scheme, nor did the AER nominate a pass through event for a feed in tariff as part of the NSW regulatory determinations. EnergyAustralia has the option of applying to the AER for a pass through of costs under the other specific events defined in the Rules, or set out in our regulatory determination.

However, this exposes NSW distributors to considerable regulatory uncertainty, as it must satisfy the AER that a defined or nominated pass through event has occurred, and that a materiality threshold has been satisfied. In this respect we note that the approval of a pass through event is not a simple matter and that the AER's decision needs to accord with the provisions of the Rules. If the materiality threshold is not reached, then a pass through application cannot be made and the distributor would effectively have to absorb the costs of the payments made under the scheme.

If unsuccessful on a pass through application, our early (conservative) estimate is that EnergyAustralia would incur upwards of $100 million in payments under the scheme for a cost that it cannot control or influence. We believe such an outcome would be contrary to the revenue and pricing principles.

It is also uncertain as to whether the AER's pass through determination would be able to include an over and under recovery adjustment. Without such an adjustment, customers would face a windfall loss or gain from any forecasting error at the time of the pass through application.

This is a particularly acute problem for NSW distributors, as the bonus payments are difficult to forecast at the inception of the scheme. This was the experience of other schemes such as the National Solar Homes Scheme where the take up of solar installations rapidly exceeded budgetary expectations. Our response to the AEMC's questions at Attachment A notes the factors that are taken into account when forecasting payments, and notes that forecasting error is more likely to occur in estimating medium to long term projections of payments, rather than as part of an annual process, where the latest information can be taken into account.

Amendment to Transitional Rules

EnergyAustralia considers the Transitional Rules should be amended as part of this proposed Rule to address the uncertainty that NSW distributors face in recovering the bonus payments it is required to make under the NSW Solar Bonus scheme.

We have provided drafting amendments at Attachment B. Similar to the ETSA Rule change, the pricing proposal of NSW distributors would include an estimate of the amount to be recovered from customers for payments made under the feed in tariff scheme for the regulatory year. The amount would include an amount for any over and under recovery of payment from the previous year, and would ensure that there is no windfall gain or loss to customers. We have also included an amendment directed at providing for under and over recovery of climate change payments, as we consider this would ensure that customers do not pay more or less than the cost of the Fund payments.

We consider consequential amendments to the Transitional Rules would require less drafting complexity than the ETSA Rule change, as it can mirror the provisions for the Climate Change Fund, and the TUOS under-over recovery mechanism.

EnergyAustralia notes the desirability of the AEMC acting expeditiously to process this Rule change. Under the current pass through provisions, EnergyAustralia has 90 business days to make a pass through application from the day that the event occurred. There is a risk that the AER will be put in a position of having to assess a pass through application at the same time that the AEMC is making a decision on whether to make consequential amendments to the Transitional Rules. We would like to work with the AEMC in addressing any issues they may have with the suggested amendments to the Transitional Rules.

5 Drafting suggestions to ETSA's proposed Rule

While EnergyAustralia supports the mechanisms and direction of ETSA's Rule change, we consider the drafting could be simplified. We note that the AEMC may wish to consider EnergyAustralia's suggested amendments to the Transitional Rules (Attachment B) as a model for the general Chapter 6 Rules, as this would mirror the MCE's drafting at the time of implementing the Transitional Rules.

Our key concern with ETSA's drafting is the inclusion of consequential amendments to Clause 6.12.1 of the Rules, which we consider are unnecessary. This section of the Rules identifies the AER's constituent decisions upon which a distribution determination is predicated. ETSA has mirrored the existing provisions in the Rules relating to the AER's constituent decision on reporting requirements for TUOS recovery, and has also sought to provide for 'variations' to the determination in the event that a feed in tariff comes into effect after a determination is published.

We consider there is a conceptual difference between TUOS charges and the payments made under the schemes. TUOS charges are costs incurred by a distributor in providing electricity network services and therefore conceptually represent an input into the costs of providing distribution services. This is not the case for payments made into the Climate Change Fund or feed in tariff payments, as this relates to an externally imposed obligation. This is presumably the reason why the MCE's Transitional Rules did not require the AER to make a constituent decision with respect to recovery of payments into the Climate Change Fund.

The key issue in this regard is whether the AER's powers under Clause 6.18.8 are sufficient to ensure that a distributor does not overcharge customers for payments made under the scheme, and that the under and over recovery amount is correct. The AER must approve a pricing proposal if the AER is satisfied that all forecasts associated with the proposal are reasonable. This means that a distributor must demonstrate that forecasts for payments into the Climate Change Fund amount or payments under a Feed in Tariff scheme are reasonable, and that the under and over recovery from the previous year is accurate.

In any case, we do not support the proposed new clause 6.12.1.19(B) and 6.18.2(b)(6B) which effectively provides for a variation to the determination if a feed in tariff scheme or climate change fund commences after a regulatory determination. This is unnecessary and overly complicated as a regulatory determination does not need to transgress into the reporting arrangements for recovery payments. These matters are best addressed in the pricing provisions.

Apart from the exclusion of these provisions, EnergyAustralia supports the drafting of the Rule change. The AEMC may wish to consider:

- Inserting a provision in the Rules which identifies the applicable schemes currently in place in jurisdictions.
- Providing separate provisions for feed in tariff schemes and Climate Change Funds.

Attachment A: EnergyAustralia's response to questions posed by the AEMC in its discussion paper of 14 January 2010

Administrative arrangements	
How, and to what extent, does the current treatment for the recovery of payments under feed-in schemes and climate change funds under the Rules create an administrative burden for DNSPs and/or the AER?	EnergyAustralia has addressed this question within the body of our submission. We note that the current arrangements in the Transitional Rules treat the recovery of payments into the Climate Change Fund as part of the annual pricing process rather than the building block determination. Under this arrangement, a distributor's annual pricing proposal includes the forecast amount be recovered from customers for the regulatory year for payments into the Climate Change. This amount is based on advice from the NSW Government. This arrangement is working effectively for NSW distributors and customers. It ensures that customers pay the 'true' recovery amount for payments made into the Fund. The only issue with the arrangement is that it does not include an over-under recovery adjustment, if the forecast amount varies from actual payments made into the Fund. As noted by ETSA, there is no similar arrangement for Climate Change Funds or feed in tariff schemes in the general Chapter 6 of the Rules. In our view, this is because policymakers were not required to address this issue when drafting Chapter 6 of the Rules as no feed in tariff schemes were in place. NSW was the only jurisdiction with a Climate Change Fund, and our circumstances were accommodated through transitional provisions. Subsequent to the drafting of Chapter 6, jurisdictions have introduced feed in tariffs. Chapter 6 does not provide for recovery of the revenue through the pricing proposal process, and therefore the AER has been limited to treating the recovery of costs as part of a building block determination. In its determination for ActewAGL, the AER noted that this mechanism may result in forecasting error, and has nominated a pass through event to ensure that a DNSP only recovers the 'true' cost of the payments under the scheme. The current arrangements rely on the AER nominating such a pass through event, as there is no defined event in the Rules. The pass through mechanism in the Rules is not suited for this purpose. The term 'event' suggests a one-off incident that occurs in a regulatory period, rather than a series of adjustments for forecasting errors. EnergyAustralia notes the following administrative burdens: ▪ The distributor is required to demonstrate that the relevant materiality threshold has been

	satisfied. This will be at least equal to the cost incurred by the AER in assessing the application. ▪ A distributor's application must specify the 'date on which the positive or negative change event has occurred' (clause 6.6.1(c)(2) and 6.6.1(f)(2). This is not clear cut in the case of forecasting error, where the error occurs throughout the year rather than a particular date. The distributor is therefore reliant on the AER taking a pragmatic view of the term 'event', when such construction was not intended by policymakers. ▪ The AER must demonstrate that it has taken into account the relevant factors listed in 6.6.1(j) of the Rules. This is an unnecessary administrative process, when the under or over recovery amount can be easily verified. In addition to these administrative burdens, our understanding is that the pass through mechanism cannot be used to adjust for over and under recovery in the last year of the relevant regulatory control period. This means that there is no true up of costs for the last year of the period, and the customer faces a windfall loss or gain.
How, and to what extent, would the proposed Rule change amend the administrative processes for these types of costs, from the perspectives of DNSPs, the AER and other stakeholders?	The proposed Rule reduces administrative complexity in 2 ways: ▪ The AER would not be required to make a decision on the efficient and prudent forecast costs of the payments to be made under the scheme. This would avoid the need for the AER to examine the method and data underlying a distributor's 5 year projection of payments. ▪ The AER would not be required to nominate a pass through event or assess pass through applications in respect of feed in tariff and Climate Change Fund payments. Instead, the proposed Rule would require the DNSP to submit the estimated costs of payments made under the scheme for the following regulatory year. In the case of climate change fund payments, this would reflect the most current estimate of payments required by the relevant Minister. In the case of feed in tariff payments, this would incorporate the most current data on take up rates and payments. Therefore the AER has to apply a lower level of scrutiny to establish the reasonableness of forecast payments. Under ETSA's proposed Rule, the AER would also have a more straight-forward process to assess under and over recovery of revenues from the previous year. It would simply verify the actual amount

	paid under the schemes, and compare this to the forecast amount. The AER would not be required to take into account each of the relevant factors in the pass through provisions of the Rules.
Allocation of risks & customer impact	
What factors are taken into account by DNSPs in preparing forecasts of payments under feed-in schemes and climate change funds as a component of operating expenditure?	Under the current arrangements in the Transitional Rules, EnergyAustralia is only required to forecast payments into the Climate Change Fund for the forthcoming regulatory year. To aid this process, we receive an indication from the relevant Minister's department as to the expected level of payment required of EnergyAustralia for the forthcoming year. If climate change fund payments were to be included in a building block approach, EnergyAustralia would be required to rely on budget projections for the Fund (usually 4 years), and extrapolate from the trend line for the remainder of the regulatory control period. This would be highly unreliable. There are many factors that impact the level of payments made under the NSW Solar Bonus Scheme. A distributor's forecast will reflect the most current information. A yearly forecast for the purposes of a pricing proposal will be more accurate than a 5 yearly projection in a building block proposal, as it would incorporate most current data. In the absence of a Rule change, EnergyAustralia would need to make a pass through application to recover its costs for the 2009-14 period, which would require a 5 year projections of costs, with uncertain prospects of adjusting for over and under recovery. EnergyAustralia is currently in the process of estimating the level of payments under the NSW Solar Bonus Scheme. The key variables are the take up rate of the scheme by eligible customers, and the magnitude of payments that accrue to the customer. As part of this exercise, EnergyAustralia will be taking into account: ▪ number of installations to date, ▪ the type of generator (PV, wind etc) ▪ the average capacity of generators ▪ the expected growth rate of the scheme, which takes into account the incentives provided by the scheme and the impact of other schemes. ▪ the expected life of the scheme; including the impact of any reviews. ▪ experience of other jurisdictions subject to a similar scheme.
What considerations or safeguards may be taken into account by DNSPs to minimise any errors in the forecast	As discussed above, the main safeguard for the Climate Change Fund under the current arrangements is that the forecast is made on a yearly basis (rather than a 5 year projection). This ensures the most

values? That is, what actions are taken by DNSPs to minimise any potential risks from forecasting errors?	current projections are used for the purpose of recovering revenue for payments made into the Fund. Similarly, yearly forecasts would assist the accuracy of forecasts for the NSW Solar Bonus Scheme, and this would be achieved by making consequential amendments to the Transitional Rules, to enable the mechanism proposed in ETSA's proposed Rule. There is an inherent risk in forecasting the level of payments for a feed in tariff scheme or Climate Change Fund for a period of five years. A prudent forecasting method will mitigate these risks to a certain extent. In the case of the Climate Change Fund this could be achieved by requesting the Minister to provide a best estimate of payments that will be required by EnergyAustralia for the next 5 years. The forecasting error for estimating payments under the NSW Solar Bonus scheme is impacted by the many and inter-related factors affecting take up of the scheme, Risks can be mitigated to some extent by ensuring that the distributor captures all relevant factors, and uses reliable and current data. The risk can also be mitigated by incorporating the experiences of other jurisdictions in the forecasting approach. Despite these safeguards, we note that the take up of the scheme can exceed expectations. This occurred with the National Solar Homes and Communities program, where the number of solar installations exponentially increased and where it became apparent to the Federal Government that the scheme would rapidly exceed its budgetary limits.
Where the actual operating expenditure differs from the forecast values, what actions would DNSPs take? That is, how would the nominated pass-through provisions function in practice and how are recoveries of payments affected year on-year?	NSW distributors have no allowance in our operating expenditure for the 2009-14 period to recover payments required by the scheme. We would need to rely on the AER approving a pass through application under one of the defined events in the Rules or a nominated pass through event in our determination. There is no certainty that we will be able to recover the amount under this mechanism, and there is further uncertainty as to whether the pass through mechanism could accommodate under and over recovery of revenue in the 2009-14 period.
Savings and transitional requirements	
What factors should be taken into account in developing savings and transitional provisions to enable efficient potential application to all DNSPs recognising that each DNSP is at a different point in the regulatory cycle?	A key issue raised in our submission is that the ETSA Rule change does not involve consequential amendments to the Transitional Rules, and therefore does not enable efficient application to NSW distributor's circumstances in the 2009-14 regulatory period. This is very concerning for NSW distributors. We are in a disadvantaged position relative to ACT

	Queensland and South Australia, as we were not provided with an allowance for the costs of the scheme as part of the building block determination. This was because the NSW Solar Bonus Scheme commenced shortly after the AER published its determination. We request that the AEMC read section 4 of our submission, which explains this issue in more detail. We consider the AEMC should make consequential amendments to the Transitional Rules to ensure that NSW distributors are provided with a cost recovery mechanism, similar to ETSA's proposed Rule, which ensures certainty that the payments made under the scheme can be recovered in the 2009-14 regulatory period. Our proposed drafting is set out at Attachment B
Jurisdictional requirements	
Whether, and if so how, to constrain the potential scope of schemes that may use the proposed cost recovery mechanism?	EnergyAustralia considers that a general definition of a feed in tariff scheme and Climate Change Fund will avoid the need for further Rule changes when jurisdictions introduce these type of schemes. EnergyAustralia understands the issue raised by the AEMC but considers that ETSA's definitions are sufficiently narrow to only include these types of schemes from using this cost recovery mechanism. EnergyAustralia considers the AEMC could include a provision which specifically identifies the relevant schemes at the date when the Rule is made. However, this would not preclude other schemes that meet the general definition.
Should the Rules include a set of criteria that a scheme would need to meet in order to use the proposed cost recovery mechanism? If so, what should be included in the criteria?	EnergyAustralia considers that only feed in tariff and Climate Change Funds should be subject to the cost recovery mechanism in ETSA's Rule change. There may be a basis for including other costs as a pricing adjustment in the future, but this should be subject to a Rule change consultation process. Generic criteria would open up other schemes to the cost recovery mechanism and require the AER to apply the criteria, which may be difficult in practice. .

Attachment B – EnergyAustralia's proposed amendments to Transitional Rules

EnergyAustralia considers that the AEMC should make the following amendments to the Transitional Rules in Appendix 1 of Chapter 11 of the Rules. Please note that blue text indicates new drafting text.

New Definition:
"NSW Solar Bonus Scheme" means obligations imposed upon a Distribution Network Service Provider by the Electricity Supply Amendment (Solar Bonus Scheme) Act 2009.

- Amendment to existing clause 6.18.2(b)
- Delete clause 6.18.2.(b) (5A) and substitute:

(5A) set out the amount required in respect of *other tariff recovery amounts* which include

(a) in the case of a NSW Distribution Network Service Provider – set out the amount required by an order under the Energy and Utilities Administration Act 1987 of New South Wales to be paid, by the provider to the Climate Change Fund in or in respect of the relevant *regulatory year* and reflect that amount in the expected revenue for the relevant *regulatory year*; and

(b) the total amount that is forecast to be credited by the provider pursuant to the *NSW Solar Bonus Scheme* in respect of the relevant regulatory year

(5B) set out how the amounts required in respect of *other tariff recovery amounts* are to be passed on to customers and any adjustments to tariffs resulting from over or under recovery of those charges in the previous *regulatory year*

- Amendment to existing clause 6.18.6(d)(2)

the recovery of revenue to accommodate pass through of charges for transmission use of system service charges and or an amount referred to in clauses 6.18.2(b)(5A) and 6.18.2(b)(5B)(a).

- Delete clause 6.18.7 and substitute:

6.18.7 Recovery of charges for transmission use of system services and *other tariff recovery amounts*

(a) A *pricing proposal* must provide for tariffs designed to pass on to customers the charges to be incurred by the *Distribution Network Service Provider* for:

(i) *transmission use of system services*.

(ii) *other tariff recovery amounts*

(b) The amount to be passed on to customers for a particular *regulatory year* must separately include the estimated amount of the *transmission use of system* charges as well as any *other tariff recovery amount* for the relevant *regulatory year* adjusted for over or under recovery in the previous *regulatory year* for each of the estimated amounts.

(c) The extent of the over or under recovery is the difference between:

(1) the amount actually paid by the *Distribution Network Service Provider* by way of *transmission use of system* charges and/or other tariff recovery amount in the previous *regulatory year*; and

(2) the amount passed on to customers by way of *transmission use of system* charges and/or other tariff recovery amount by the *Distribution Network Service Provider* in the previous *regulatory year*.