AUSTRALIAN COMPETITION TRIBUNAL

Application by ActewAGL Distribution [2016] ACompT 4

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| Citation: | Application by ActewAGL Distribution [2016] ACompT 4 |
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| Review from: | Australian Energy Regulator |
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| Applicant: | **ACTEWAGL DISTRIBUTION** |
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| File number: | ACT 5 of 2015 |
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| Tribunal: | **MANSFIELD J (PRESIDENT)**  **MR R DAVEY (member)**  **DR D ABRAHAM (member)** |
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| Interveners: | AusNet Services (Distribution) Pty Ltd  AusNet Services (Transmission) Ltd  Australian Gas Networks Ltd  Citipower Pty Ltd  Powercor Australia Ltd  SA Power Networks  United Energy Distribution Pty Ltd  Ergon Energy Corporation Ltd  Minister for Resources, Energy and Northern Australia |
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| Date of Determination: | 26 February 2016 |
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| Catchwords: | **ENERGY AND RESOURCES** – application under s 71B of the *National Electricity Law* (NEL) for review of a distribution determination by the AER – topics for review – operating expenditure (opex) – service target performance incentive scheme (STPIS) – return on equity – return on debt – gamma – metering services opex – metering classification  **ENERGY AND RESOURCES** – service target performance incentive scheme (STPIS) – service standards factor adjustment to the annual revenue allowance – reliability of supply – maintenance of historical standards of service performance – where opex allowance is a significant reduction from historical opex allowance -where there is no dispute about the allowance for capex |
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| Legislation: | *National Electricity Law*  *National Electricity Rules*  *National Gas Law*  *National Gas Rules* |
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| Cases cited: | *Applications by Public Interest Advocacy Centre Ltd and Ausgrid* [2016] ACompT 1 |
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| Dates of hearing: | 21-25 September 2015; 28-30 September 2015;  1-2 October 2015, 6-9 October 2015 |
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| Place: | Darwin (via video link to Sydney, Melbourne, Brisbane and Adelaide) |
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| Category: | Catchwords |
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| Number of paragraphs: | 87 |
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| IN THE australian competition tribunal |  |
|  | ACT 5 of 2015 |

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| re: | **APPLICATION UNDER SECTION 71B OF THE NATIONAL ELECTRICITY LAW FOR A REVIEW OF DISTRIBUTION DETERMINATION MADE BY THE AUSTRALIAN ENERGY REGULATOR IN RELATION TO ACTEWAGL DISTRIBUTION, PURSUANT TO RULE 6.11.1 OF CHAPTER 6 OF THE NATIONAL ELECTRICITY RULES** |
| by: | ACTEWAGL DISTRIBUTION  Applicant |

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| TRIBUNAL: | MANSFIELD J (PRESIDENT)  MR R DAVEY (MEMBER)  DR D ABRAHAM (MEMBER) |
| DATE OF DETERMINATION: | 26 FEBRUARY 2016 |
| WHERE MADE: | DARWIN (via video link to SYDNEY, MELBOURNE, BRISBANE AND ADELAIDE) |

THE TRIBUNAL DETERMINES THAT:

1. Pursuant to s 71P(2)(c) of the *National Electricity Law*, the *Final Decision ActewAGL distribution determination 2015-16 to 2018-19*, April 2015, including attachments (the Final Decision) is set aside and remitted to the Australian Energy Regulator (AER) to make the decision again in accordance with the following directions:

* 1. the AER is to make the constituent decision on opex under r 6.12.1(4) of the *National Electricity Rules* in accordance with these reasons for decision including assessing whether the forecast opex proposed by the applicant reasonably reflects each of the operating expenditure criteria in r 6.5.6(c) of the *National Electricity Rules* including using a broader range of modelling, and benchmarking against Australian businesses, and including a “bottom up” review of ActewAGL’s forecast operating expenditure;
  2. the AER is to make the constituent decision on the service target performance incentive scheme in the light of such variations as are made to the Final Decision by reason of (a) hereof;
  3. the AER is to make the constituent decision on return on debt in relation to the introduction of the trailing average approach in accordance with these reasons for decision;
  4. the AER is to make the constituent decision on estimated cost of corporate income tax (gamma) in accordance with these reasons for decision, including by reference to an estimated cost of corporate income tax based on a gamma of 0.25; and
  5. the AER is to consider, and to the extent to which it considers appropriate to vary the Final Decision in such other respects as the AER considers appropriate having regard to s 16(1)(d) of the *National Electricity Law* in the light of such variations as are made to the Final Decision by reason of (a)-(d) hereof.

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| IN THE AUSTRALIAN COMPETITION TRIBUNAL |  |
|  | ACT 5 of 2015 |

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| Re: | **APPLICATION UNDER SECTION 71B OF THE NATIONAL ELECTRICITY LAW FOR A REVIEW OF DISTRIBUTION DETERMINATION MADE BY THE AUSTRALIAN ENERGY REGULATOR IN RELATION TO ACTEWAGL DISTRIBUTION, PURSUANT TO RULE 6.11.1 OF CHAPTER 6 OF THE NATIONAL ELECTRICITY RULES** |
| BY: | aCTEWagl distribution |

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| TRIBUNAL: | MANSFIELD j (president)  MR R DAVEY (member)  DR D ABRAHAM (member) |
| DATE: | 26 FEBRUARY 2016 |
| PLACE: | darwin (via video link to sydney and melbourne) |

**REASONS FOR DETERMINATION**

# INTRODUCTION

1. This application by ActewAGL Distribution (ActewAGL) is one of eight applications heard together, by the agreement of all parties, because of their substantially common issues.
2. ActewAGL is the owner and operator of an electricity distribution network located in the Australian Capital Territory (the ACT). It is registered as a distribution network service provider (DNSP) under s 12(1) of the *National Electricity Law* (NEL) and r 2.5.1 of the *National Electricity Rules* (NER). It provides distribution services to retailers through its network.
3. On 30 April 2015, the Australian Energy Regulator (AER) published its Final Decision *ActewAGL Distribution Determination 2015-16 to 2018-19* (Final Decision). It is that determination which gave rise to the present application.
4. The Tribunal has, at the same time as delivering these reasons, delivered its reasons in applications ACT 1 and 4 of 2015, *Applications by Public Interest Advocacy Centre Ltd* *and* *Ausgrid* [2016] ACompT 1 (Applications 1 and 4 of 2015) (the *PIAC-Ausgrid Decision*). The *PIAC-Ausgrid Decision* is the “lead” decision in respect of the issues common to this and other applications made at or about the same time to review decisions of the AER under the NEL and in one instance under the *National Gas Law* (NGL). The Tribunal adopts, where appropriate, the definitions and abbreviations used in the *PIAC-Ausgrid Decision* without repeating them.
5. In addition to the two applications giving rise to the *PIAC-Ausgrid Decision*, there were two further separate applications by PIAC to review related Final Decisions of the AER also made on 30 April 2015 under the NEL in respect of Endeavour Energy (Endeavour) and Essential Energy (Essential), as well as applications by Endeavour and Essential themselves to review those Final Decisions: ACT 2 of 2015 and ACT 3 of 2015 by PIAC and ACT 6 of 2015 and ACT 7 of 2015 by Endeavour and Essential. In addition to the ActewAGL application, the AER made a decision on 3 June 2015 under the National Gas Law (NGL) in respect of Jemena Gas Networks (NSW) Ltd (JGN) in respect of its New South Wales (NSW) gas distribution network. JGN duly applied to review that decision. Its application was heard with the other applications.
6. Each of Ausgrid, Endeavour and Essential are DNSPs owned by the State of New South Wales, and each provided electricity network distribution services (and in the case of Ausgrid transmission services) within that State. They are collectively called Networks NSW.
7. There were a number of issues or topics common to this application, the applications by Networks NSW and the application by JGN. Those five applications and the three PIAC applications were heard together. The five regulated suppliers (Ausgrid, Endeavour, Essential, ActewAGL and JGN) are conveniently called the Network Applicants.
8. That course of action was adopted with the support of the several parties, and the AER. It was agreed that there were significant issues in common (as well as some issues specific to a particular network applicant). It was also agreed that it was the more efficient way to proceed. In the conduct of the applications, leave to intervene in each application was given to AusNet Services (Distribution) Pty Ltd, AusNet Services (Transmission) Ltd, Australian Gas Networks Ltd, CitiPower Pty Ltd, Powercor Australia Ltd, SA Power Networks and United Energy Distribution Pty Ltd (Vic/SA Network Interveners) and Ergon Energy Corporation Ltd (Ergon). Leave to intervene in all applications was also given to the Commonwealth Minister for Energy and Science. On 21 September 2015, the title of the Commonwealth Minister with responsibility for energy matters changed from the Minister for Industry and Science to the Minister for Resources, Energy and Northern Australia. For consistency, hereafter he is referred to as the Minister.
9. The relevant background to the applications collectively, and the relevant legislative and regulatory structure within which the AER Final Decisions were made, and within which the Tribunal’s reviews are to be conducted, is discussed at length in the *PIAC-Ausgrid Decision*. It is not necessary to repeat it.
10. It is important, however, to note that this decision, and the other relevant decisions, of the AER were made in the phase of the second regulatory decision-making process under the NEL and the NGL. The first regulatory period in respect of which the AER generally made those decisions was the period 2008-09 to 2013-14. Following that first phase, both the NEL and the NGL, and the complementary NER and *National Gas Rules* (NGR) respectively, were quite extensively changed. The 2013 Legislative Amendments, and the 2012 Rule Amendments, imposed on the AER (and the Tribunal) are significantly different legislative and regulatory structures for the making of their respective decisions. The nature and significance of those changes is addressed generally in the *PIAC-Ausgrid Decision*. So, too, is the description and outcome of the Tribunal’s consultative process. Those matters are directly relevant to, but not repeated, in these reasons for decision.
11. It is the combination of those eight applications which was heard together for the reasons given.

# BACKGROUND TO THE ACTEWAGL APPLICATION

1. As in the case of each of the applications, ActewAGL’s application is a result of reviewable regulatory decisions made by the AER following the introduction of the 2012 Rule Amendments by the AEMC.
2. Because of the timing of the 2012 Rule Amendments, the AEMC deferred the full regulatory determination process for the ACT and NSW DNSPs for the 2014-15 to 2018-19 regulatory control period. To allow for a transition to the regime under the 2012 Rule Amendments, the Savings and Transitional Rules in Div 2 of Pt ZW of Ch 11 of the NER provided for a two stage process for the regulation of ACT and NSW DNSPs over the five year period commencing on 1 July 2014 (the 2014-19 period), comprising:
3. the transitional regulatory control period from 1 July 2014 and ending on 30 June 2015 (transitional regulatory control period); and
4. the subsequent regulatory control period from 1 July 2015 and ending on 30 June 2019 (subsequent regulatory control period).

Under the transitional arrangements, the AER was required to make placeholder distribution determinations for those DNSPs for the initial transitional one year period. It was then required to carry out a full regulatory determination process and make distribution determinations for those DNSPs for the balance of that period.

1. In accordance with the prescribed process, following the transitional determination made by the AER in respect of ActewAGL on 16 April 2014, ActewAGL submitted its Regulatory Proposal on 10 July 2014. The AER published a Draft Decision in respect of that proposal on 27 November 2014 for the balance of the regulatory control period. ActewAGL in turn, on 20 January 2015, submitted its Revised Regulatory Proposal, and subsequently on 13 February 2015 made its submissions on the Draft Decision and in support of its Revised Regulatory Proposal.
2. That led to the AER Final Decision concerning ActewAGL (and coincided with separate Final Decisions for each of the three Networks NSW entities) on 30 April 2015.
3. On 17 July 2015, the Tribunal gave ActewAGL leave to apply to review the AER Final Decision concerning it in respect of the following topics which are encompassed in the building blocks prescribed by rr 6.3 and 6.4.3 of the NER:
4. allowance for operating expenses (opex);
5. service target performance incentive scheme (STPIS);
6. return on equity;
7. return on debt;
8. value of imputation credits (gamma);
9. alternate control metering services annual charges (metering services opex); and
10. classification of metering services.
11. ActewAGL adopted a common position with Networks NSW in relation to opex, return on equity and gamma (as did JGN), and a position substantially similar to Networks NSW on return on debt.
12. In those circumstances, it is not necessary to repeat much of what is in the *PIAC-Ausgrid Decision* regarding the relevant provisions, the character of the common issues, the AER’s processes for its decision-making in relation to those common issues, and the Tribunal’s decision in relation to each issue and its reasons for that decision.
13. The *PIAC-Ausgrid Decision* should be taken to be part of the Tribunal’s reasons for its decision on this application on such issues. To the extent necessary, the Tribunal will address each of the issues in respect of which leave to apply to review was given, but in the common issues it will be able to do so in relatively brief terms.
14. Nor is it necessary to repeat what is said generally in the *PIAC/Ausgrid Decision* regarding those grounds of review, the role of the Tribunal, and what amounts to a “materially preferable NEO decision”.
15. The topics of STPIS, metering services opex and classification of metering services will, of course, have to be separately considered in a little length and the topic of return on debt will also require a little further consideration because of ActewAGL’s particular position.
16. The particular decisions of the AER about which ActewAGL complains involve very substantial sums. Those decisions are:
17. the AER’s decision to reject ActewAGL’s proposed opex allowance of $371.2m ($2013-14) for the 2014-19 period (excluding debt raising costs and Demand Management Incentive Allowances) in its Revised Regulatory Proposal, and to determine that ActewAGL’s opex allowance ought to be $240.6m ($2013-14), and to otherwise not make any provision for ActewAGL transitioning to that level of opex by way of a “glide path” in the control mechanism or otherwise;
18. the AER’s decision to apply its STPIS to ActewAGL for the current regulatory control period without modification to the performance targets applicable to ActewAGL;
19. the AER’s decision to reject ActewAGL’s proposed opex for metering services of $15.7m ($2013-14) (excluding debt raising costs), and to determine an alternative opex allowance for those metering services of $10.8m ($2013-14) (excluding debt raising costs);
20. an error by the AER in the classification of metering services pursuant to cl 6.12.1(1) of the NEL;
21. the AER’s decision to reject ActewAGL’s proposed return on equity methodology (that resulted in a proposed final annual return on equity of 10.71 percent) for use in the determination of the allowed rate of return for the 2014-19 period, and to instead adopt an annual return on equity for that period of 7.1 percent;
22. the AER’s decision to reject ActewAGL’s proposed trailing average approach (without transition) in estimating the return on debt for use in the determination of the allowed rate of return for the 2014-19 period, and to instead adopt an approach that involves a form of transition from the previous “on the day” approach to the trailing average approach; and
23. the AER’s decision to reject ActewAGL’s proposed value of imputation credits of 0.25 for use in the estimation of the cost of corporate income tax for the 2014-19 period, and to determine that the value of imputation credits ought to be 0.4.
24. The issues relating to opex, return on equity, return on debt, and value of imputation credits (gamma) can be addressed quite shortly. The ActewAGL submissions on those topics were made in conjunction with those of Networks NSW, and therefore can be determined by reference to the Tribunal’s decisions on those topics and its reasons for those decisions in the *PIAC-Ausgrid Decision*.
25. It is, or course, not necessary to refer to the PIAC submissions, as PIAC confined its applications to, and its submissions as an intervener to, the Final Decisions concerning Networks NSW.

# OPEX ALLOWANCE

1. Although ActewAGL made separate submissions on this topic, its submissions largely took the same position as Networks NSW. Indeed, the Tribunal in the *PIAC-Ausgrid Decision* includes extensive references to the ActewAGL contentions on this topic.
2. The starting point for ActewAGL’s attack on the AER’s Final Decision on opex was to contend that the AER had failed to comply with r 6.5.6(c) and (d) of the NER by failing to separate its consideration:
   1. of whether it was satisfied that the total forecast opex in the Revised Regulatory Proposal reasonably reflected each of the criteria (as specified in r 6.5.6(c)(1)-(3), having regard to the operating expenditure factors in r 6.5.6(e) of the NER); and
   2. of the required opex pursuant to r 6.12.1(4)(ii) of the NER.
3. ActewAGL said that the AER had not taken the first step by first addressing ActewAGL’s forecast opex carefully to decide whether or not it was satisfied of its reasonableness. Instead, it says, the AER started by itself determining what was the appropriate forecast opex for ActewAGL by reference to its own analysis and modelling, and then – because the forecast opex by ActewAGL was higher than the AER assessment – took the joint or rolled up decision on the reasonableness of ActewAGL’s forecast opex and the appropriate forecast opex in one step.
4. That matter was raised also by Networks NSW. In the *PIAC-Ausgrid Decision*, the Tribunal has not accepted that the AER fell into that error. It is not necessary to repeat those reasons on this topic. In the ActewAGL Final Decision, the AER appears to have taken the step of considering critically its opex forecast: see eg ActewAGL Final Decision, Attachment 7, Appendix D at pp 7-34 to 7-35.
5. In any event, unless it could be shown that a more complete and sophisticated analysis of the ActewAGL opex forecast in its Revised Regulatory Proposal would have led to the AER being satisfied that it did reasonably reflect each of the opex criteria, the contention (even if made out) would not of itself pass the obstacle to setting aside the opex decision of the AER on that ground, having regard to s 71P(2a) and (2b) of the NEL. The Tribunal has not taken the step of concluding that a different or more complete and sophisticated analysis of the ActewAGL opex forecast would have led the AER to that satisfaction.
6. The Tribunal has decided, as recorded in the *PIAC-Ausgrid Decision*, that the criticisms of the AER’s Final Decisions in relation to its benchmarking methodology expose that the asserted grounds of review by Networks NSW are made out. As ActewAGL’s contentions in large measure follow Networks NSW’s contentions, it is not necessary to do more than observe that the particular elements or features of ActewAGL’s network fortify those conclusions.
7. The report by Advisian: *Opex cost drivers: ActewAGL Distribution electricity (ACT)*, January 2015 at pp 47-48 provides a convenient reference for those physical features of the ActewAGL’s distribution network which the AER’s modelling, in the view of the Tribunal, did not take properly into account.
8. As noted in the *PIAC-Ausgrid Decision*, the AER acknowledged as much by providing an input margin of 23 percent to ActewAGL to accommodate those differences. Such an adjustment by reason of the particular operating environment factors (OEFs) is really indicative of the potential inadequacy of the AER’s preferred model.
9. The Tribunal also does not need to repeat what it said in the *PIAC-Ausgrid Decision* regarding the individually immaterial OEF factors, and its treatment of them by the AER.
10. In view of its conclusion on those matters, the Tribunal does not need to determine specifically whether – in relation to ActewAGL’s labour costs, it was appropriate for the AER to apply the metric cost per average staffing level per customer (as it did) rather than a comparison of its labour costs against average staffing levels of other network providers, on what (ActewAGL said) should be by a peer review with other network providers and which should take account of the particular network characteristics. Nor does it need to address ActewAGL’s criticisms of the *EMCa: Review of ActewAGL Distribution Labour Resourcing and Vegetation Management Practices at 2012-13*, April 2015. It notes that the EMCa report took as part of its foundation the *Marchant Hill Consulting Report* (MHC Report)*: Organisational Review ActewAGL Energy Networks*, and a Sinclair Knight Merz (SKM) report: *Resource Planning* *to deliver ActewAGL’s Program of Work for the FY 2012/13, Final Report*, 27 March 2012 (the SKM Report), even though MHC by letter of 4 March 2015 said that its findings in its report were not directly indicative of material labour cost inefficiencies on the part of ActewAGL, and even though the thrust of the SKM Report was that ActewAGL did not have sufficient workforce to deliver its proposed program of works.
11. It is also not necessary to determine specifically the correctness of the AER’s assessment that ActewAGL’s vegetation management costs are inefficient.
12. Finally, the Tribunal notes the contention of ActewAGL that the AER was required to consider the endogenous (as distinct from the exogenous) considerations which ActewAGL said were relevant to its position. The AER took a different view: Attachment 7 to the ActewAGL Final Decision at pp 7-61 to 7-62. The question whether “efficient costs” for the opex allowance should be determined having regard to the legacy issue (ie the endogenous factors concerning a particular DNSP) has been discussed in the *PIAC/Ausgrid Decision*.
13. The Tribunal proposes to set aside the ActewAGL Final Decision of the AER in relation to its opex allowance for in essence the same reasons as apply to Networks NSW. In that circumstance, it is not necessary to deal with those matters in detail. The further reasons for doing so equate to those in the Conclusions section of the *PIAC-Ausgrid Decision* as noted later in these reasons.
14. Each of those matters will have to be revisited by the AER when considering the opex allowance for ActewAGL. The Tribunal has left to the AER, subject to correcting the matters which give rise to the grounds of review having regard to the Tribunal’s reasons in the *PIAC/Ausgrid Decision*, the process including the modelling steps which it takes to do so. To specifically address those individual matters, as elements or steps in the revised modelling and benchmarking of the AER for the purposes of that review, is not necessary, and the Tribunal’s reasons provide only a different broad framework for the AER to undertake that task.
15. Indeed, depending on the options considered by the AER, there may be two or more alternative decisions which may contribute to the achievement of the NEO and the AER may, on an appropriate assessment of those alternatives, arrive at different preferable reviewable regulatory decisions: s 16(1)(d) of the NEL.

# SERVICE TARGET PERFORMANCE INCENTIVE SCHEME

1. Rule 6.6.2(a) requires the AER to publish a service target performance incentive scheme (STPIS) to provide incentives, which may include targets, for DNSPs to maintain and improve performance.
2. Not surprisingly, there is considerable accord between ActewAGL and the AER about the relevant provisions concerning a STPIS and about how it is to work.
3. The applicable STPIS required by r 6.2.2 of the NER was duly published by the AER in November 2009. It is referred to in the ActewAGL Final Decision by the AER as “the national STPIS”. It defines the performance incentive scheme parameters that measure the service performance of a particular DNSP, and sets out the requirements with which the values to be attributed to the parameters must comply. It also states that the incentive rates so calculated will be used to decide the service standards financial reward or penalty component of a distribution determination. The rewards and penalties are based on the value of customer reliability so as to align the distributor’s incentives with the long term interests of consumers, consistently with the NEO.
4. It is not necessary to refer in detail to how the STPIS operates. One of its mechanisms is a service standards factor (s-factor) adjustment to the annual revenue allowance, which rewards or penalises the particular DNSP for improved or diminished service compared to pre-determined targets. The s-factor mechanism adjusts the revenue that a DNSP earns depending on a reliability of supply component and a customer service component. The reliability of supply component, which is identified by ActewAGL as the component of the STPIS presently in issue, contains parameters to apply during a regulatory control period by reference to, amongst other things, unplanned System Average Interruption Duration Index as defined, and unplanned System Average Interruption Frequency Index as defined. It also prescribes that the performance targets to apply for the reliability of supply component during a regulatory control period must not deteriorate across regulatory years and must be based on average performance over the previous five regulatory years (subject to particular modification).
5. Hence, the performance targets for the reliability of supply component are determined by reference to whether historical standards of service performance are to be maintained.
6. The STPIS also provided that the maximum revenue increment of decrement under the s-factor adjustment for each regulatory year within the regulatory control period would be 5 percent.
7. Following the AER’s ActewAGL Draft Decision, ActewAGL’s Revised Regulatory Proposal maintained or enhanced the modifications to the STPIS which it proposed for the purposes of AER’s Final Decision. One matter of concern then raised was that the opex allowed to ActewAGL, or proposed to be allowed to ActewAGL, would not be sufficient to maintain its historical standards of service performance.
8. The AER did not accept that proposed variation to the performance target. It maintained the setting of targets based on ActewAGL’s average performance over the past five regulatory years for the reliability of supply components. It accepted certain other modifications to the STPIS proposed by ActewAGL, including accepting the proposal to lower share of revenue at risk under the STPIS from 5 percent to 2.5 percent. Relevantly, therefore, it considered that the allowed opex in its Final Decision provided a sufficient amount to enable ActewAGL, acting prudently and efficiently, to maintain reliability at the current level.
9. ActewAGL contends that the decision of the AER to apply its then existing STPIS to ActewAGL for the subsequent regulatory control period without modifying the applicable performance targets for the reliability of supply element of that STPIS was in error. It contends that a modification of the performance target was necessary because the opex allowed to ActewAGL in the Final Decision was insufficient to enable it to maintain the historical reliability outcomes by reference to which those performance targets had been set. That is because, as has been discussed in the previous section of these reasons for decision, the opex allowance was a significant reduction from the levels of opex previously allowed to ActewAGL when it achieved those historical reliability outcomes, and was determined on the basis of benchmarking of ActewAGL’s opex against that incurred by other DNSPs who did not achieve those reliability outcomes at the time those other DNSPs incurred that level of opex.
10. It is perhaps a little simplistic, but not unfair, to note that the AER’s decision is justified firstly on the basis that its decision as to STPIS must be referenced to its consideration of expenditure as a whole, including capex. As it says, capex for replacing assets is an important factor in maintaining and improving reliability. ActewAGL does not complain about the allowance for capex in the Final Decision of the AER, which represent about 90% of the capex proposed in the Revised Regulatory Proposal. The second matter which the AER points to particularly is that ActewAGL, together with another DNSP, CitiPower, have a significantly higher level of underground cabling than other DNSPs, and so they are less prone to damage by climactic events or to other breakdowns. That is, the reliability performance of a particular DNSP is influenced by the configuration and condition of its network assets, and underground cabling should substantially discount the significance of uncontrollable external impacts such as weather variations which affect reliability performance.
11. Both those observations by the AER appear to the Tribunal to be sensible ones. ActewAGL said, nevertheless, that the AER’s conclusion was erroneous for several reasons.
12. While ActewAGL submitted the two points may support the AER’s conclusion that its application of the STPIS was correct, it went on to submit that ActewAGL has network structural differences which may justify a conclusion different from the AER’s based on its benchmarking. ActewAGL then argued that the starting assumption about its efficient opex allowance – as fixed by the AER – was shown (by the contentions of ActewAGL and Networks NSW) to be erroneous, so the starting assumption should not be treated as a valid one. It also argued, as is self-evident and as was accepted by the AER, that the opex allowance has an impact on the STPIS selected and the outcomes generated, but it also said the AER had proceeded to fix the STPIS for ActewAGL without regard to its opex. The Tribunal does not accept that the AER proceeded in that way, that is without regarding the opex allowance as relevant to the capacity of the particular network provider to provide service to consumers. The AER reasons did not make that error. The point is really that the AER did not do so adequately. Finally, ActewAGL said the AER decision as to the form of opex was counterintuitive, given the significant reduction in opex and having regard to the comparators to which the AER referred.
13. By way of a general proposition, it was argued that the AER had not really sought to clearly identify with any precision the extent to which the undergrounding of the ActewAGL network in fact would lead to a lower opex requirement to provide the level of service it had historically achieved, so as to assess whether that level of service could be maintained with the significantly reduced opex allowance.
14. The Tribunal does not need to address those individual contentions. It notes that the AER rejected each of those criticisms. However, as the Tribunal has concluded that the opex fixed by the AER exposes the grounds of review referred to above, one of the foundations or reference points from which the AER based its decision on STPIS is flawed.
15. In that circumstance, the Tribunal considers that the STPIS determination by the AER is also flawed. As the Tribunal has also decided that it should remit the ActewAGL Final Decision to the AER (see below) for the same general reasons as expressed in the *PIAC-Ausgrid Decision*, it is appropriate that this element of the ActewAGL Final Decision should also be set aside.
16. There is an interrelatedness between opex and the form of the STPIS, although not a directly linear one. However, it is sufficiently direct to require the STPIS element of the ActewAGL Final Decision to be set aside and reconsidered at the same time as the AER reconsiders and potentially resets the opex allowance for ActewAGL.
17. The AER, for its part and depending upon its revised conclusions on opex, may choose to select a different service standard for STPIS or may choose to restore the ±5 percent exposure level which it generally imposes.

# METERING SERVICES OPEX

1. This topic concerns the AER’s rejection in the ActewAGL Final Decision of the claim in the Revised Regulatory Proposal for $15.7m ($2013-14) as the appropriate allowance of metering services (excluding debt raising costs). Instead, the AER set the opex allowance at $10.8m ($2013-14).
2. It is helpful to explain the nature of the topic itself, before addressing the asserted grounds of review.
3. In the Final Decision, the AER classified various network services, namely the design, planning, operation, maintenance of the network, connection services to premises (including extensions and augmentations), and emergency response and administrative services, as standard control services. It categorised other services, relevantly Types 5 and 6 meter provisioning, installation and commissioning, and reading, maintenance and data services as alternative control services.
4. It is the control mechanism over those alternative control services imposed by the Final Decision which is the subject of contentions. The AER imposed control mechanisms on the provision of three services by caps on the prices of individual services, namely:
5. an upfront capital charge for all new and upgraded meters installed from 1 July 2015; and
6. an annual charge comprising:
   * 1. capital – metering asset base (MAB) recovery; and
     2. non-capital – opex and tax.
7. The AER addressed metering capital costs for regulated meters installed before and after 1 July 2015 separately. The former involved the amortising of the capital cost, and progressive payment of the MAB recovery as part of the annual metering charge. The latter, installations after 1 July 2015, involved the upfront payment of the MAB, and only the non-capital charge would be the subject of the ongoing annual metering charge.
8. The AER also accepted ActewAGL’s proposed price caps for new or upgraded connections. It also broadly accepted ActewAGL’s approach to the annual metering charges, including for installations prior to 1 July 2015 and the opening MAB as at 1 July 2014.
9. ActewAGL’s Revised Regulatory Proposal sought an accelerated depreciation of those assets over a nine year period. The Final Decision of the AER was to maintain the standard asset life of 15 years, with forecast depreciation on that basis. It also, as noted, adopted a forecast of $10.8m (exclusive of debt costs) for the metering opex (operation, maintenance and other non-capital costs in providing material services) rather than accepting ActewAGL’s proposed allowance of $15.7m ($2013-14).
10. The AER’s forecast of metering opex is said by ActewAGL to be erroneous. It is clear that the AER’s estimation was based on an average of five years of historical opex, and that it derived an efficient opex by benchmarking against other network service providers. The data source was the economic benchmarking RIN. As the AER did not conclude, adversely to ActewAGL, that its historical opex was inefficient, the steps criticised by ActewAGL are more subtle.
11. ActewAGL says that the AER erred in determining the base annual metering opex amount. The error, it is said, is to have assumed – incorrectly – the historical metering opex, based upon ActewAGL’s response of 2 June 2014 to the RIN issued to ActewAGL on 7 March 2014 included certain categories of capex, and so were wrongly deducted. Consequently, the base annual metering opex used by the AER was too low.
12. It is common ground that the AER used a base-step approach in its metering opex forecast.
13. The AER adopted its approach, and made the adjustments to the base as presented by ActewAGL, because (it says) that conformed to the Basis of Preparation instructions that accompanied the economic benchmarking RIN, which included a definition of “Metering Services”. That included annual metering services and ancillary metering services. The network providers, including ActewAGL, were required to explain their methodology applied in providing the required information, and to identify any assumptions applied. It says that ActewAGL did not comply with that requirement so as to make clear, as ActewAGL now asserts, that its reported historical opex did not include the perceived capex elements now identified by ActewAGL.
14. The AER observed that ActewAGL’s historical data did not show any steady increase in metering opex per customer, and the industry average was stable, so it applied zero real price growth and productivity growth on the forward trend analysis, based on average data for the five year historical figure.
15. The AER’s response to ActewAGL then is that it reasonably proceeded on the basis that the historical metering opex figures included the costs that it deducted, because there was no information to point it to a different conclusion. The historical metering opex costs (which the AER now accepts did not include ancillary metering costs) were in fact required by the AER in a form which did not require the disaggregation of opex and capex, but that the same costs should not be allocated twice. The economic benchmarking RIN made that clear.
16. The AER said, in any event, that the amount in issue – assuming that the factual basis it proceeded on in its assessment of ActewAGL’s data is incorrect – means that the asserted error is not a material one, and its correction would not lead to a materially preferable NEO decision.
17. The Tribunal does not consider it necessary to resolve the question whether, in the circumstances, a ground of review has been made out. That is because, for other reasons, the Tribunal considers that it should set aside the ActewAGL Final Decision. If that is done, metering service opex may well be a matter to which the AER may have regard because of the potential interrelationship of this opex element with other opex elements or more generally because of its functions under s 16(1)(d) of the NEL. That also obviates the necessity of what may have been a difficult question as to whether the ground of review asserted is in reality error of fact in a material issue of fact or an error in the exercise of a discretion. It also then, if the error was one of fact, obviates the necessity of considering whether the asserted error of fact can be established when, as the AER said, it appears to have proceeded on a reasonable understanding of the complex data presented by ActewAGL. The different understanding of the AER and of ActewAGL as to what the RIN data included became apparent to ActewAGL only after the time of the Final Decision by reference to the metering model provided by the AER. Such issues are not likely to recur.

# CLASSIFICATION OF METERING SERVICES

1. It is necessary to address this topic only briefly.
2. ActewAGL has pointed out an error in the ActewAGL Final Decision. Appendix A to the Overview for the Final Decision includes a table of constituent decisions upon which it is predicated. The table reads as if Type 5 and Type 6 unrecovered metering costs are defined as standard control services, when the substantive comment in the Final Decision Attachments 13 and 16 make it clear that standard control services do not include Type 5 and Type 6 unrecovered metering costs.
3. At the time the application for leave to apply to review the ActewAGL Final Decision was made, the AER pointed out that it had acknowledged the error and had undertaken to correct it, by adopting ActewAGL’s proposed formulation. It was conscious that, to correct the error, it would have required revocation of the ActewAGL Final Decision, and consequently the foundation for the review application itself. But for that consideration, it would in any event have taken corrective action under r 6.13 of the NER.
4. The dispute is whether it is appropriate for the Tribunal to proceed to determine the error exists, as acknowledged by the AER, or whether (as the AER says) because the decision has no real revenue impact, and would not, or would not be likely to, result in a materially preferable NEO decision when corrected, it is not appropriate to determine that a ground of review is made out, and the AER should simply be left to take corrective action under r 6.13 of the NER.
5. The Tribunal does not need to further address that issue because, in any event, for reasons unrelated to this issue, it proposes to set aside the ActewAGL Final Decision as discussed more generally in these reasons for decision.
6. In that circumstance, the error which is acknowledged can be corrected by the AER when making its revised determination in any event.

# RETURN ON EQUITY

# RETURN ON DEBT

# VALUE OF IMPUTATION CREDITS (GAMMA)

1. As noted above, ActewAGL made submissions on each of these three topics jointly with Networks NSW and JGN (Return on Equity and Gamma) and jointly with Networks NSW (Return on Debt).
2. The *PIAC-Ausgrid Decision* therefore records sufficiently those contentions, and the Tribunal’s conclusions with respect to them. They should be taken as being incorporated into these reasons for decision on those topics.
3. The result is that the Tribunal considers that grounds of review have been made out with respect to the topics of Return on Debt and Gamma, and were not made out in respect of the topic of Return on Equity.

# CONCLUSIONS

1. In the *PIAC-Ausgrid Decision*, the Tribunal addressed the way in which it approached its task under s 71P(2a) and (2b) in deciding whether to set aside or vary or leave standing the AER’s Final Decisions.
2. What is said in those reasons is equally applicable to AER’s ActewAGL Final Decision. The Tribunal for those same reasons, is satisfied that making a determination that the ActewAGL Final Decision should be set aside or varied is a materially preferable NEO decision, and that it should not vary the Final Decision itself.
3. Consequently, as in the cases of Networks NSW, the Tribunal sets aside the AER’s ActewAGL Final Decision and remits it to the AER for reconsideration, by having regard to and giving effect to the reasons of the Tribunal on the particular elements of the ActewAGL Final Decision where grounds of review have been established. Having regard to its consideration of interrelatedness of the elements of some building blocks, and of some building blocks themselves, the Tribunal also determines that the whole of the Final Decision should be set aside. That is so the AER, in its reconsideration, can properly give effect to its obligations under s 16(1)(c) and (d) of the NEL when conducting the reconsideration.
4. ActewAGL made the point in the course of its submissions that the opex allowed in the AER Final Decision concerning it was last achieved by ActewAGL some 15 years ago when it was serving 40% fewer customers and maintaining an asset base that had a value some 40% lower than that which it presently maintained: see its Revised Regulatory Proposal at p (ii). Consequently, ActewAGL asserted, and provided some evidence to the AER to the effect that a reduction in opex of that degree may have a serious and adverse effect on the ability of ActewAGL to deliver safe reliable and secure supplies of electricity.
5. The Tribunal notes that the AER’s Final Decision with respect to ActewAGL was to reject its proposed opex allowance of $371.2 million ($2013-14) for the 2014-19 period (excluding debt raising cost and Demand Management Incentive Allowances in its Revised Regulatory Proposal) and determine an opex allowance of $240.6 million ($2013-14), and to make otherwise no provision for ActewAGL transitioning to that level of opex by way of a glide path in the control mechanism. Whether such transitioning is appropriate in the light of the reconsidered decision is a matter for the AER.
6. In its background discussion in the Introduction and Framework section of the *PIAC-Ausgrid Decision*, the Tribunal has referred to s 16(1)(d) of the NEL and has also addressed the Tribunal’s responsibilities under s 71P(2a) and (2b) of the NEL. In the concluding part of its reasons in the *PIAC-Ausgrid Decision* those matters are further explored. As there noted, it is a fair observation of the AER Final Decisions regarding the service providers generally that its focus was, understandably, largely upon the price of the supply of electricity to consumers both in the short and immediate and longer terms. There is no particular discussion by the AER in those Final Decisions in which there is a quantitative assessment of the impact or likely impact of its determinations upon the quality, safety, reliability and security of supply of electricity or of the reliability, safety and security of the national electricity system. That is not said by way of a criticism for the reasons which are discussed in the concluding section of the *PIAC-Ausgrid Decision*. However, given the confronting assertion made by ActewAGL referred to above, and the submissions made by the Minister in the course of the hearing, it is obvious that some degree of balancing is necessary. The consultation process exposed that there is a very serious concern on the part of consumers of electricity about the price of its supply. There is also, as noted, and for identifiable reasons, concern about ensuring the quality, safety, reliability and security of supply of electricity and of the national electricity system itself. Where there is a compromise to be made between those two broad factors, or indeed some elements of the safety, reliability and security factors, it is presently unclear how the AER would see the appropriate compromise to be set.
7. As the matter is to be remitted to the AER, the Tribunal does not consider it appropriate to determine in the first place how that balancing exercise should be performed in the light of appropriate factual findings, including of course because (as it discusses in the concluding section of the *PIAC-Ausgrid Decision*) it is of the view that it should not vary the AER’s relevant reviewable regulatory decisions because, to do so, would require the Tribunal to undertake an assessment of such complexity that the preferable course is to remit the matter to the AER.

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| I certify that the preceding eighty-seven (87) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Mansfield, Mr R Davey and Dr D Abraham. |

Associate:

Dated: 26 February 2016