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Dr Patrick Walsh
Utilities Commissioner
Utilities Commission
GPO Box 915
Darwin NT 0801

Dear Pat

Re: 2014-2019 Networks Price Determination: Framework and Approach Consultation Paper

Thank you for the opportunity to comment on the Utilities Commission's Framework and Approach Consultation Paper for the 2014 Network Price Determination.

Power and Water's response to the Commission's Consultation Paper is attached.

It is Power and Water's objective throughout the 2014 Network Price Determination process to raise all concerns regarding the Commission's interpretation, determination, and application of the regulatory framework for the fourth regulatory period to ensure the best outcome for network users, the shareholder, and Power Networks.

Overall, Power and Water agrees with the Commission's preliminary position to adopt, where possible, the approach used by the Australian Energy Regulator (AER) and to apply those parts of Chapter 6 of the National Electricity Rules (NER) that are consistent with the NT Electricity Networks (Third Party Access) Code (the NT Access Code).

Power and Water agrees with the Commission that full adoption of Chapter 6 of the NER and the AER processes may not be possible and variations or a transitional approach may be required, for the following reasons:

- The small size of the market and high scale costs in the NT as compared to other systems in the National Electricity Market (NEM) means that some aspects of the NER and AER's approach may not be cost effective in the NT at this time;
- Increased documentation, data provision and reporting requirements, and limited resources available (internally and externally) to Power and Water and the Commission could mean that some aspects of the NER and AER's approach will be difficult to be provided and reviewed within the required timeframes; and
- The differences in the market structure and regulatory environment in the NT compared to the NEM means that some aspects of the NER and AER's approach may need to be modified for the NT's circumstances.

Power and Water requests that the Commission be continually mindful of this as it develops its models and data requirements.

Power and Water considers that the Commission should focus on priority areas for this 2014 Networks Price Determination, such as:

- Prudency and efficiency reviews of the capital and operational expenditure forecasts;
- Regulatory asset values; and
- Networks pricing principles and tariff structures,

with further transition to Chapter 6 of the NER and the AER approach to be achieved as part of the following Networks Price Determination for the fifth regulatory control period. This is consistent with the arrangements in the NEM, as the NER provide for jurisdictional derogations and transitional arrangements for each participating jurisdiction.

Power and Water has identified the following key issues with the Commission's proposed framework and approach. These issues are expanded on in the attached response to the Commission's Consultation Paper:

- <u>Post-tax approach</u>

  Power and Water's preference is to adopt a pre-tax approach for the 2014 Network Price Determination, and to transition to the AER's post-tax approach for the next Network Price Determination for the fifth regulatory control period. Power Networks is not a tax entity, and the tax liability is calculated at the Corporation level. Converting 10 years of Power Networks' financial data from a pre-tax to a post-tax basis will only add to the already considerable increase in reporting requirements, for no obvious benefit other than interstate comparability.

- <u>Regulatory Asset Base</u>

  If Power and Water can demonstrate in its regulatory proposal that basing the required revenue calculation on the initial value of $350 million as at 1 July 2002 is not sufficient to ensure Power Networks' capability to deliver the required level of network performance and services in the long term and its ongoing commercial viability then Power and Water believes that the Commission should reconsider its decision not to re-open the regulatory asset base. The on-going commercial viability of the network provider is a requirement of the NT Access Code.

- <u>Reconciliation of actual expenditure incurred during the third regulatory control period</u>

  The Commission did not utilise a forward-looking building blocks approach for the 2009 Network Price Determination. As such, Power and Water has essentially only received a return on and return of capital for 2008-09, and not on its forecast rolled forward RAB, for this current regulatory control period.

  Power and Water strongly supports the Commission's position that a reconciliation of the actual expenditure incurred by Power Networks during the third regulatory control period should be undertaken as part of the 2014 Network Price Determination process, as it impacts significantly on Power Networks on-going commercial viability. However, Power and Water requests that further consideration be given to how this will be achieved. The required revenue calculation under a forward building blocks approach will not provide

for the return of and return on assets that have been foregone during the current regulatory control period.

- Networks Pricing Proposals and tariff structures

  Power and Water would like to highlight to the Commission that it intends to undertake a major review of its tariff structures as part of the 2014 Network Price Determination process. However, Power and Water's ability to meet all of the NER's Pricing Proposal requirements in the timeframes will be on a best endeavours basis, as the requirements are much more onerous in the NER than in the NT Access Code.

- Cost Allocation Method

  Due to timing issues, Power and Water will submit its current UC-approved Accounting and Cost Allocation Procedures that will be used in the development of its capital and operational expenditure forecasts. During the fourth regulatory control period, Power and Water will develop a Cost Allocation Method consistent with the AER Cost Allocation Guidelines, for submission to the Commission as part of the Networks Price Determination process for the fifth regulatory control period.

- Regulatory Investment Test (RIT)

  This will be a new requirement for Power Networks. Some aspects of the RIT will need to be modified for the NT's circumstances.

- Regulatory Information Notice (RIN) Template

  The data and supporting documentation that the Commission requires under its RIN is unknown at this stage. Power and Water requests that the Commission issue its RIN as soon as practicable, so that Power and Water can assess it's capability to provide the data.

Power and Water appreciates the opportunity to work with the Commission to determine the extent to which information provision can be best matched to that required under the NER and the AER processes, and looks forward to working constructively with the Commission throughout the 2014 Network Price Determination process.

Please contact Ms Djuna Pollard, Manager Regulation, Pricing and Economic Analysis, on (08) 8985 8431 or by email at djuna.pollard@powerwater.com.au if you wish to clarify any matter in this response.

Yours sincerely

Andrew Macrides
Managing Director

August 2012

2014-2019 NETWORK PRICE DETERMINATION - FRAMEWORK AND APPROACH CONSULTATION PAPER

SUBMISSION BY POWER AND WATER CORPORATION

AUGUST 2012

This report contains 21 pages

Response to Issues Raised in the 2014 Network Price Determination Framework and Approach Consultation Paper

The following table provides a summary of Power and Water's comments on the 2014 Network Price Determination Framework and Approach Consultation Paper. Please note that the order in which the comments are presented is based on the sequence of contents of the Consultation Paper, and not in order of priority.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
General Framework and Approach			
1.13 1.14 1.16 1.17	The Commission's preliminary position is to adopt, where possible, the approach used by the AER and on the application of those parts of Chapter 6 of the NER in relation to electricity network businesses in the NEM that are consistent with the NT Access Code. The Commission considers that this framework represents generally accepted regulatory practice at this time. The Commission acknowledges that resourcing constraints and economies of scale mean that full adoption of an approach consistent with the AER processes may not be practical. The Commission's proposed approach is, in consultation with PWC Networks, for each aspect of the 2014 Network Price Determination: a) if a component of the approach used by the AER is not inconsistent with the requirements of the NT Access Code, to consider whether the requirements for that component can currently be met by PWC Networks and if so, then apply it; b) if a component of the approach used by the AER cannot currently be met by PWC Networks, to make the minimum modifications necessary such that the modified requirements can be met by PWC Networks and apply the modified requirements; and c) where a component of the approach used by the AER has	Agree	• PWC supports the UC's proposed approach, and its interpretation of generally accepted regulatory practice. However, PWC notes that the AER has proposed changes to Chapter 6 of the Rules, which are still the subject of consultation by the AEMC. • The UC's acknowledgment that the full adoption of the AER's processes isn't practical due to resourcing constraints and economies of scale is important. The small size of the market, differences in the market structure and regulatory environment, limited available resources (internally and externally), and high scale costs in the NT mean that the regulatory cost/benefit trade-off is more significant here than in other systems in the NEM. • Additionally, PWC notes that the NER and AER's processes are more onerous than the requirements under the NT Electricity Networks Access Code (the NT Access Code). The increased reporting requirements, and limited available resources to both PWC and the UC could mean that some aspects of the NER and AER's approach will be difficult to be provided by PWC and reviewed by the UC within the required timeframes. Where this is the case, PWC proposes a transitional approach to the adoption of the NER and AER requirements. • PWC notes that that the Distribution Network Service Providers (DNSPs) operating in the NEM have taken some time to establish the systems and processes required to meet the NER and AER's reporting requirements, and that the NER also allows for jurisdictional derogations and transitional arrangements.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
	been modified, document the reasons for departing from the NER and outline a framework and timeframe for putting in place capabilities to meet the requirement in future.		• At this time, the most significant aspect of the NER/AER's approach that cannot currently be met by Power Networks without introducing unwarranted complexity is the adoption of a post-tax approach. PWC proposes that the UC modify its approach to a pre-tax approach for the 2014 Network Price Determination. This is discussed further in the 'Application of the Post-Tax Revenue Model' section of this response. • Other aspects that are likely to be difficult for PWC to fully comply with or are inappropriate in an NT context and could therefore require modifications to the NER and AER's approach, include: – RAB roll forward asset reporting categories – Networks Pricing Proposals tariff structure justification – Cost Allocation Method – Regulatory Investment Test provisions and consultation process – Regulatory Information Notice Template data provision • PWC appreciates the opportunity to work with the UC to determine the extent to which information provision can be best matched to that required under the NER and the AER processes.
Scope of the Network Price Determination ***- Transmission Network versus Distribution Network Services***			
3.44	The Commission's preliminary position is that the 2014 Network Price Determination will comprise a single building block of cost of service covering all network services (both transmission and distribution) provided by PWC Networks, applying where appropriate the provisions of Chapter 6 of the NER.	Agree	• PWC supports the regulation of PWC's networks in the NT as Distribution Networks. The separate regulation of transmission (even if these assets were treated as dual function assets) would add a level of complexity that is not warranted for the scale of PWC's network. Additionally, the required asset specific information for transmission regulation and pricing is not readily available.
Scope of the Network Price Determination ***- Regional Determinations versus a Single NT Wide Determination***			
3.45	A single cost of service determination will be made for all regulated networks, rather than separate determinations for	Agree	• PWC supports a single determination for all regulated networks, rather than separate determinations for each network.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
	each network.		• PWC agrees with the UC that the emphasis should be on cost effective regulation, and the scope for giving increased weight to regulatory stability and predictability, given the cost and complexity of a small enterprise in a small market. PWC considers that separate determinations would introduce unwarranted complexity and would not be cost effective. • PWC understands that the UC has specific concerns with PWC's current pricing structure, specifically in regards to locational pricing signals. PWC agrees with the UC that its concerns should be addressed through an examination of the structure of Power Networks' proposed tariffs, as opposed to a separate distribution determination for each network. PWC also points out that the revised Capital Contributions approach that it has submitted for the approval of the UC is intended to supplement network prices by providing more cost reflective locational price signals.
PWC capabilities to deliver information (Regulatory Information Notice)			
3.51 3.52	While further development is required, the Commission's preliminary view is that sufficient progress has been made to apply a firm-specific building block approach for the 2014 Network Price Determination. In line with this, the Commission proposes to issue a request for information under section 25 of the *Utilities Commission Act* that will be largely modeled on the RIN issued by the AER to DNSPs in the NEM.	Agree	• PWC supports the application of a firm-specific building block approach. • The data and supporting documentation that the UC requires under its Regulatory Information Notice (RIN) is unknown at this stage. PWC requests that the UC issue its RIN as soon as practicable, so that PWC can assess it's capability to provide the data and commence discussions with the UC regarding the extent to which information provision can be best matched to that required under the AER processes and any required modifications to the RIN request.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Classification of services			
4.33	For excluded services, the Commission proposes to continue with the 2009 service classification of alternative control services, but the Commission does not propose to apply any price control mechanism for these services. The Commission will provide guidance on whether or not a control mechanism submitted by PWC in its pricing proposal is consistent with the principles set out in the NT Access Code.	Agree subject to clarification	• PWC considers that the UC's interpretation and proposed treatment of Alternative Control Services (ACS) is consistent with the NT Access Code. • PWC seeks clarification from the UC as to whether it will have an approval role in the escalation arrangements to apply to ACS charges during the fourth regulatory control period. If the UC has an approval role, the UC's Draft and Final Determinations should outline the arrangements associated with the escalation of existing ACS charges, amendments to existing ACS charges, and the introduction of new ACS charges. • PWC proposes to continue to annually escalate existing ACS charges by CPI-X. PWC intends to review its existing ACS charges as part of its review of the regulated networks tariff structures.
4.35	The Commission proposes to continue with the service classifications that it adopted in the previous regulatory control period, while further clarifying the service descriptions.	Agree subject to clarification	• PWC supports the UC's proposal to continue with the services classification in the current regulatory period. • PWC seeks further explanation as to what the UC means by *"further clarifying the service descriptions"*.
Form of Control Mechanism			
1.27 1.28 1.30	The basis of the control mechanism will be of the prospective CPI minus X form. However, rather than the Total Factor Productivity (TFP)-based approach applied for the 2009 Network Price Determination, the Commission proposes to determine the X-factor in accordance with a building block approach. The Commission's preliminary view is that the most practical course is to adopt a forward-looking building block approach using similar processes and practices as applied by the AER, but noting that full adoption of the AER processes may not be possible and variations may be required. The Commission is	Agree	• PWC supports the continued use of CPI minus X as the basis of the control mechanism and a weighted average price cap as the form of price control. • PWC agrees with the UC that there is sufficient justification to depart from the TFP-based approach to determine the X-factor, and to instead adopt a forward-looking building block approach. PWC agrees that the TFP approach cannot be considered to represent generally accepted regulatory practice in Australia at this time. The use of a forward-looking building blocks approach has extensive precedent, and is in line with the UC's general approach to align its framework and approach with the NEM arrangements.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
	mindful that, in a small jurisdiction, the Commission and PWC have limited resources available (both internally and externally) to undertake a building block approach form of price control. The Commission intends to seek advice from the AER on how similar processes and practices can be applied to the Territory's context.		• PWC acknowledges that there are currently a number of initiatives underway that will affect its capabilities to deliver information suitable to be applied to an approach consistent with the NER methodology. As identified by the UC in its Framework and Approach Consultation Paper, these initiatives include: – full implementation of the Asset Management Capability Project; – further development of network asset management plans; – implementation of recommendations resulting from the various reviews undertaken in the NT Government's priority work program; and – implementation of initiatives to further align PWC's processes and practices with good industry practice. However, PWC considers that sufficiently reliable financial and other supporting data can be provided to the UC in order for efficient and reliable X factors to be determined for the next regulatory period.
1.31	The Commission will work with PWC Networks to determine the extent to which information provision can be best matched to that required under the AER processes.		
1.32	The Commission does not propose to apply any price control mechanism for services other than standard control services.		
Application of the Post-Tax Revenue Model			
6.4	The Commission's preliminary position is that a post-tax revenue model (PTRM), largely modeled on the AER's published PTRM and its accompanying handbook, be adopted for use by the network service provider in the 2014 Network Price Determination.	Agree subject to proposed transitional arrangements	• PWC proposes that the UC modify its proposed position from a post-tax to a pre-tax approach and revenue model for the 2014 Network Price Determination. However, PWC agrees that a post-tax approach and revenue model should be used as part of the Networks Price Determination process for the fifth regulatory control period (the 2019 Network Price Determination). • PWC considers that this aspect of the NER/AER's approach cannot currently be met by Power Networks without introducing unwarranted complexity, for the following reasons: – Power Networks is not a tax entity and PWC's tax liability is calculated at the Corporation level. This is a key distinction between Power Networks and DNSPs operating in the NEM. – Converting 10 years of Power Networks' actual and forecast financial data (2009 to 2019) from a pre-tax to a post-tax basis is a labour intensive task.
6.5	Any modifications of the AER's PTRM will be based on PWC Networks' capacity to provide information equivalent to that required under the NER. The Commission proposes to make only the minimum modifications necessary such that the modified requirements can be met by PWC Networks.		

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
			– There is currently no networks tax asset base and one would need to be calculated. – A pre-tax framework is less information intensive. Given the tight timeframe for the Reset, a post-tax framework will only add to the already considerable increase in reporting requirements, for no obvious benefit other than interstate comparability. • A pre-tax framework has been adopted in each of the previous regulatory control periods for these reasons, and PWC does not consider that there is sufficient justification to depart from this approach until the 2019 Network Price Determination. This will enable Power Networks sufficient time to develop its actual and forecast information on a post-tax basis.
Regulatory Asset Base			
6.9	Consistent with the approach applied for the 2009 Network Price Determination, the Commission does not intend to reconsider the opening regulatory asset base, set at $350 million (excluding gifted assets) as at 1 July 2002 (in July 2002 dollars).	Disagree	• PWC's major concern with using the regulatory asset base set at $350 million as at 1 July 2002 is that there is insufficient provision for expenditure necessary to replace its pre-1 July 2002 assets. • If PWC can demonstrate in its Initial Regulatory Proposal that basing the required revenue calculation on the initial value of $350 million as at 1 July 2002 is not sufficient to ensure PWC Networks' ongoing commercial viability then the UC should reconsider its decision not to re-open the regulatory asset base. • PWC defines commercial viability to be the ability to maintain its financial and infrastructure capital over the long-term. This is consistent with the requirements of the NT Access Code: – clause 63 "Price regulation under this Part must be administered to achieve the following outcomes: (aa) expected revenue for a regulated service or services that is at least sufficient to meet the efficient long-run costs of providing that regulated service or services, and includes a return on investment commensurate with the commercial and regulatory risks involved"; and

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			– clause 68 "In setting a revenue or price cap, the regulator must take into account the revenue requirements of the network provider during the relevant financial year or years having regard to: (e) the provision of a return on efficient capital investment undertaken by the network provider in order to maintain or extend network capacity that is commensurate with the commercial and regulatory risks involved; … and (j) the on-going commercial viability of the network provider".
Recognition of capital expenditure incurred in the current regulatory control period			
6.18	The Commission's preliminary position is that, consistent with the Commission's Off-ramp Decision in 2005 and the NER as they stand at this time (and which the Commission has accepted as representing generally accepted regulatory practice), the Commission will roll the full amount of capital expenditure incurred in the third regulatory control period into the opening RAB for the fourth regulatory control period.	Agree	• PWC agrees with the UC's preliminary position to roll the full amount of capital expenditure into the asset base to determine the opening RAB for the fourth regulatory control period. This approach provides certainty that investments made in the network may be recovered and thus provides some incentive for investment and reduces the risk to investors.
6.19 6.20	However, the Commission intends to subject this capital expenditure to detailed scrutiny, with a reconciliation of the actual capital expenditure that PWC Networks has incurred during the third regulatory control period forming part of the Commission's assessment of required revenue for the 2014 Network Price Determination. If unacceptably high levels of inefficiency are revealed in assessing PWC Networks' regulatory proposal, the Commission may propose some optimisation of the RAB in its draft determination.	Disagree	• PWC does not agree to the UC undertaking an ex-post optimisation of actual capital expenditure. • For capital investment during the 2009-14 regulatory control period above the permitted capital forecast, PWC has already forgone the return on, and of, assets. The UC's calculation of PWC's 2009-10 opening tariffs for the 2009 Network Price Determination only considered PWC's capital expenditure requirements for 2008-09 and not its future capital expenditure requirements. Therefore, PWC's opening tariffs only allowed it to recover its recalculated 2008-09 costs, which were adjusted annually for each remaining year of the regulatory period by a productivity measure. As such, PWC has essentially only received a return on, and of, capital for 2008-09 expenditure (and the RAB at the start of the regulatory control period), not on its forecast rolled forward RAB, for this current regulatory control period.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
			• In addition, the ex-post optimisation of actual capital expenditure is not consistent with the incentive regulation approach adopted under the NER. It introduces a potentially significant regulatory risk on network investments.
Rolling forward of the RAB			
6.21 6.22 6.23 6.24	The Commission's preliminary position is that a roll forward model (RFM) largely modeled on the AER's published RFM and its accompanying handbook be adopted for use by PWC Networks in the 2014 Network Determination to roll forward the RAB. As with the AER's PTRM, modifications to the RFM will be based on PWC Networks' capacity to provide information. The RFM is used by the AER to determine the closing RAB for each DNSP for each regulatory control period. This closing RAB value (broken into asset classes) becomes the opening RAB to be used for the purposes of making a distribution determination for the next regulatory control period. The RAB values from the RFM form inputs into the PTRM, where they are rolled forward from year to year using forecast data. The RFM performs calculations predominantly using actual data.	Agree subject to proposed amendments	• PWC supports the use of the AER's RFM with modifications made as required based on PWC's capacity to provide information. For example, the provision of data in the required asset categories is likely to be difficult to provide as it will require manual manipulation of PWC's regulatory asset book. • However, the AER's RFM will also need to be modified because it is premised on the use of a forward-looking building blocks approach in the current regulatory control period, as opposed to the Total Factor Productivity (TFP) approach that was adopted by the UC. • Under the TFP approach, PWC has essentially only received a return on and return of capital for 2008-09, and not on its forecast rolled forward RAB, for this current regulatory control period. To ensure its on-going commercial viability, PWC should receive a return on and a return of its capital expenditure during the current regulatory control period. • To this end, PWC proposes that the UC modifies the AER's RFM so that its capital expenditure in the current regulatory control period is not depreciated, and the undepreciated value is therefore incorporated in the opening RAB used in the PTRM. This will enable PWC to receive the full return of depreciation on its capital investment from 2009-10 to 2013-14.
Forecast capital expenditure			
6.28	The Commission's preliminary position is that PWC Networks' regulatory proposal should include total forecast capital expenditure which complies to the maximum extent possible with the requirements of clause 6.5.7 of the NER.	Agree	• PWC supports the UC's preliminary position with regards to forecast capital expenditure.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Regulatory Investment Test (RIT)			
6.31 6.35	As indicated in its review of Electricity System Planning, Monitoring and Reporting, the Commission supports the introduction and use of a regulatory investment test (RIT) as part of the network planning process to ensure that network developments are subject to a cost-effectiveness evaluation. While transmission and distribution are separated in the NER in Chapter 6A and Chapter 6 respectively, the Commission's preliminary position is that a combined regulatory investment test (that is the AER's regulatory test version 3) for the transmission and distribution network be applied by PWC Networks to the determination of efficient capital expenditure for the purpose of the 2014 Network Price Determination.	Agree subject to proposed amendments	• PWC agrees in principle with the application of the AER's RIT version 3 for PWC's network investments to all network investments with a capital expenditure of greater than $10 million.[1] However, some aspects of the RIT should be modified for NT circumstances. • The RIT has two limbs: – **Reliability**: where the investment minimises the cost of an option "necessitated principally to meet service standards linked to the technical requirements of schedule 5.1 of the Rules or in applicable regulatory instruments" [jurisdictional reliability or other legal requirements], and – **Market benefits**: where an option maximises the "expected net economic benefit to all those who produce, consume and transport electricity in the national electricity market". • The RIT specifies the range of market benefits that must be included in the NPV analysis, including "competition benefits", net changes in market benefit arising from the impact of the option on participant bidding behaviour. This latter provision would not apply in the NT situation. • The RIT also requires the publication of: – a "Request for information" for each investment, seeking information as to the identity and detail of alternative options to the potential or proposed new investment; – an "Application notice", followed by a consultation period for public submissions. • PWC requests that the provisions in the RIT be varied to suit the NT and PWC's circumstances. Specifically the terminology "market benefits" and the approach to their analysis are specific to the NEM. In addition, the extensive consultation approach needs adaption for the circumstances in the NT. PWC would be happy to work with the Commission to make suitable amendments to the RIT.

[1] AER, *Final Decision Regulatory Test version 3 & Application Guidelines*, November 2007.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Weighted Average Cost of Capital (WACC)			
6.44 6.45	The Commission considers the approach in the NER to be appropriate for the 2014 Network Price Determination, as it is well defined and sufficiently flexible to enable formulation of a forward-looking WACC that reflects prevailing market conditions. The Commission's preliminary position is that it will adopt a post-tax nominal WACC, consistent with the AER methodology.	Agree subject to clarification and subject to proposed transitional arrangements	**WACC Parameters** • PWC supports the use of the NER's WACC methodology and approach in principle. • WACC parameters are reviewed by the AER every 5 years and were last reviewed in May 2009. It is noted that the determination of WACC parameters, in particular the Market Risk Premium, has been the source of debate, disagreement and appeal in the NEM. Notably, the Australian Competition Tribunal has varied AER decisions on the averaging period to determine the risk free rate, the value assigned to tax imputation credits and the debt risk premium. • As network businesses are capital intensive, the determination of WACC is one of the most significant decisions that will affect revenues in a network determination. The AER's next review of WACC parameters around May 2014 is unlikely to be incorporated in the UC's 2014 Final Determination. The AER's review is expected to more closely specify the approach by which WACC parameters are determined, to reduce the likelihood of successful appeals. • PWC requests that the UC make clear what its approach will be to the determination of WACC parameters in its Final Framework and Approach Paper. **Use of a Post-tax WACC** • PWC does not agree to the use of a post-tax WACC. The use of a post-tax or pre-tax nominal WACC should reflect the UC's decision regarding the use a post-tax or a pre-tax approach. As previously stated, PWC is proposing that the UC modify its proposed position from a post-tax to a pre-tax approach and revenue model. • PWC requests that the UC adopt a pre-tax nominal WACC, consistent with the use of a Pre-tax Revenue Model for the 2014 Network Price Determination.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Treatment of corporate tax			
6.50	The Commission's preliminary position is that for the 2014 Network Price Determination a post-tax approach should be adopted, consistent with the AER methodology. The Commission recognises that this may create difficulties for PWC as PWC Networks is not a tax entity and PWC's tax liability is calculated at the Corporation level. This may require further consideration.	Agree subject to proposed transitional arrangements	• PWC proposes that the UC modify its proposed position from a post-tax to a pre-tax approach for the 2014 Network Price Determination. However, PWC agrees that it should transition to a post-tax approach for the 2019 Network Price Determination. • PWC considers that this aspect of the NER/AER's approach cannot currently be met by Power Networks without introducing unwarranted complexity, as Power Networks is not a tax entity and PWC's tax liability is calculated at the Corporation level. This is a key distinction between Power Networks and the DNSPs operating in the NEM. • A pre-tax framework is also considered to be less information intensive. Given the tight timeframe for the Reset, a post-tax framework will only add to the already considerable increase in reporting requirements, for no obvious benefit other than interstate comparability. • A pre-tax WACC has been adopted in each of the previous regulatory control periods for these reasons, and PWC does not consider that there is sufficient justification to depart from this approach until the 2019 Network Price Determination. This will enable Power Networks sufficient time to develop its actual and forecast information on a post-tax basis.
Depreciation			
6.53	The Commission's preliminary position is that PWC Networks' regulatory proposal should calculate depreciation for each regulatory year consistent with the requirements of the NER.	Agree subject to proposed alternative approach	• PWC supports the UC's preliminary position with regards to the depreciation calculation for each year of the fourth regulatory control period in the PTRM. • However, PWC is proposing an alternative approach to the calculation of depreciation in the RFM that is used to determine the closing RAB value for the current regulatory control period, and the opening RAB value for the fourth regulatory control period.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Forecast Operating Expenditure			
6.58	The Commission considers the approach specified in the NER for determining forecast operating expenditure to be appropriate for the 2014 Network Price Determination, and that it should provide PWC Networks with an incentive to undertake a robust assessment of its network expenditure requirements.	Agree	• PWC supports the UC's preliminary position with regards to forecast operating expenditure.
Cost allocation			
6.62 6.63 6.64 6.65 6.66	While the NT Access Code does not explicitly require the network service provider to submit a cost allocation methodology to the Commission, the network service provider is implicitly required to allocate costs between different categories of distribution services. The Commission approved the initial cost allocation procedures in November 2001 under the Ring-fencing Code. The Commission is of the view that, as they stand, the Cost Allocation Procedures developed under the Ring-fencing Code are too broad to provide guidance to PWC Networks in the development of consistent internal policies to be used as part of the 2014 Network Price Determination. The Commission's preliminary view is that the Cost Allocation Procedures require review, and that the NER cost allocation principles and the AER Cost Allocation Guidelines would be appropriate indicators of generally accepted regulatory practice. In line with this, PWC Networks will be required to submit a Cost Allocation Method, setting out the detailed principles and policies used by PWC Networks to allocate costs between different categories of distribution services, consistent with the AER Cost Allocation Guidelines, prior to finalising its regulatory proposal.	Agree subject to proposed transitional arrangements	• PWC supports the submission of a Power Networks' Cost Allocation Method to the UC as part of the Network Price Determination process and prior to finalising its regulatory proposal. However to meet this requirement for the 2014 Network Price Determination, the Cost Allocation Method will by necessity be the current UC-approved Accounting and Cost Allocation Procedures. • PWC has an existing obligation to submit its cost allocation procedures under the Northern Territory Electricity Ring-fencing Code, and the UC approved the Accounting and Cost Allocation Procedures submitted by PWC in November 2001. In May 2006, the UC extended indefinitely its approval of PWC's Accounting, Cost Allocation and Information Procedures under the Ring-fencing Code. • PWC will not have sufficient time to prepare its capital and operational expenditure forecasts on an alternative cost allocation basis. Power Networks will have finalised its financial budgets for its Business Plan and for input into the 2013-14 SCI prior to the UC's approval of its Cost Allocation Procedures, and it will therefore be too late to amend the capital and operational forecasts in the SCI. • During the fourth regulatory control period, PWC will develop a Cost Allocation Method consistent with the AER Cost Allocation Guidelines for submission to the UC as part of the 2019 Network Price Determination process.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Driving improvements in reliability (Service Target Performance Incentive Scheme)			
6.77	GSL schemes in place elsewhere in Australia are generally funded as an operating cost of the DNSP. This is done for NEM jurisdictions through an ex ante assessment of likely costs by the AER when setting the revenue or price cap. Accordingly, the Commission will consider if an allowance for GSL payments should be made when assessing the regulated revenue requirement of PWC Networks for the 2014 Network Price Determination.	Agree	• PWC considers that the GSL scheme should be funded through the Network Price Determination, consistent with how GSL schemes are funded in the NEM.
6.79	The Commission's preliminary view is that it would be premature for the 2014 Network Price Determination to include STPIS arrangements in the price control mechanism, since PWC Networks will have had only limited exposure to the new service standards. Rather, the Commission will rely on the GSL Code to drive reliability improvements in poorly performing areas of the network and on the targets and reporting framework to be established under the Standards of Service Code to encourage reliability improvements across the network as a whole. The Commission may consider including incentive scheme arrangements based on the STPIS for future regulatory periods.	Agree	• PWC supports the UC's preliminary view that it would be premature for the 2014 Network Price Determination to include STPIS arrangements in the price control mechanism.
Providing incentives for demand management (Demand Management Incentive Scheme)			
6.84 6.85	The Commission is aware that both the Territory Government and PWC have implemented demand management initiatives and the Commission will consider if an allowance should be made for any associated costs when assessing the regulated revenue requirement of PWC Networks for the 2014 Network Price Determination. However, the Commission's preliminary view is that it may be premature to adopt a formal DMIS for the 2014 Network Price Determination, particularly given the limited experience of such arrangements in NEM jurisdictions at the present time.	Agree	• PWC agrees with the UC's preliminary view that it is probably premature to adopt a formal DMIS for the 2014 Network Price Determination. It is noted that in its most recent Framework and Approach Paper for the NSW and ACT distributors, the AER has proposed extending the scheme to include embedded generator connections, as the DMEGCIS.

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
	The Commission may consider demand management incentives for future regulatory periods.		
Sharing the benefits of efficiency gains (Efficiency Benefits Sharing Scheme)			
6.92	The Commission's preliminary position is that, at the end of the fourth regulatory control period, any efficiency gains or losses achieved during the period will be dealt with consistent with the requirements of the AER's EBSS or with a Territory-specific EBSS if one is in force at that time.	Disagree	• PWC does not support the implementation of an EBSS at the end of the fourth regulatory period. • As the 2014-2019 performance against the regulatory operating cost allowance will form the basis for this carry-over incentive scheme in the subsequent regulatory control period, it is incumbent upon the UC to specify the operation of an EBSS scheme at least 5 years in advance of its implementation, including specifying how network operating expenditure on demand management and network support will be treated, and for PWC to have the opportunity to put forward exclusions or variations.
Pass-through cost arrangements			
6.100	In the 2009 Determination, the Commission decided that it would only consider cost pass through applications if they are the consequence of: • change in tax or insurance events; • force majeure events; • regulatory compliance events; • service standard events; or • such other events that satisfy the following requirements: – the occurrence was not anticipated at the time of the preceding determination or was, while allowable, explicitly excluded from affecting the outcome of that determination on the grounds that the likely impact on PWC Networks was unknown or too difficult to quantify at the time, or – the occurrence is not a result of actions of PWC's board or	Agree subject to proposed amendments	• The UC proposes to apply the same pass through arrangements as it did in 2009, including the application of a materiality threshold of 1% of annual revenue, regardless of whether the events had been nominated beforehand or were captured by its general provisions. • PWC considers that the UC should apply the AER's materiality provision. In AER consultation on the pass through materiality threshold, it adopted the position that an event is material if: "1. the revenue impact in any one year exceeds 1 per cent of the respective DNSP's revenue for the first year of the regulatory period; or 2. the proposed capex exceeds 5 per cent of the AARR in the first year of the regulatory period".[2] • There are a number of additional foreseeable events that could make material changes to PWC's cost structures:

[2] AER, *Preliminary Positions - Matters relevant to distribution determinations for ACT and NSW DNSPs for 2009-2014 - Demand management incentive scheme, Control mechanisms for alternative control services, Approach to determining materiality for possible pass through events*, December 2007.

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	management or of decisions of the Government in its capacity as owner or shareholder or guarantor of PWC.		– A **structural separation event**, if more complete disaggregation of PWC's System Operation function or other functions leads to increases in network costs; – A **new technology event**, if a mandated roll out of smart meters or smart grid technology; – An **emissions trading scheme event**, if costs are impacted by emissions trading arrangements; and – A **network losses event**, if the regulations under the Energy Efficiency Opportunities Act are extended to capture PWC and result in increasing administrative, compliance or capital costs.
6.101	The Commission also applied a materiality test, requiring that a cost pass-application must at least satisfy a materiality threshold of 1 per cent of the annual revenue from standard control services in the financial year in which the event occurs.		
6.102	The Commission's preliminary view is that it will adopt the same list of allowable pass through events as that applied to the 2009 Network Price Determination but will follow the processes and have regard to the factors set out in clause 6.6.1 of the NER when determining whether a particular cost pass through event has occurred.		
Networks Pricing Principles Statement (NPPS) and Networks Pricing Proposal			
7.26	In previous network price determinations, the Commission has focused on establishing an efficient opening level for required revenue (determining Po) and setting an efficient price path (determining the X factor), leaving limited time and resources to give detailed scrutiny to PWC Networks' NPPS and the structure of tariffs.	Agree subject to clarification	**Initial Pricing Proposal** • The UC is proposing that PWC should prepare a Networks Pricing Proposal for the first year of the regulatory control period to be included in its regulatory proposal, in a similar manner to the documents required to be published by NEM DNSPs. This document would demonstrate compliance with the provisions of clauses 74 and 63 of the NT Access Code and consistent with the requirements of clause 6.18.2(b) of the NER. • PWC agrees in principle, but notes that its ability to meet all of the NER requirements in the required timeframes will be on a best endeavours basis, as the requirements in the NER are much more onerous than in the NT Access Code. • PWC understands the UC's motivation behind its intention to increase its scrutiny of PWC's tariffs and tariffs structures. PWC is continually mindful of the need for access prices to send appropriate signals to network users, and to ensure that cross subsidisation is kept to a minimum.
7.32	The Commission's preliminary position is that PWC Networks' regulatory proposal should include: • a draft NPPS to apply to the setting of individual prices; and • for the regulatory year commencing 1 July 2014, an indicative Network Pricing Proposal and Tariff Schedules consistent with all other elements of the regulatory proposal.		
7. 34	It should define the tariff classes into which network users are divided and provide modelling, where appropriate, and qualitative analysis to support the constitution of those tariff classes. This should include discussion of the options considered and reasons for the choices made in relation to differentiating tariffs because of:		

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
	• the user's geographical and electrical location; • the quantities in which the relevant network access service is to be supplied or is supplied; • the pattern of network usage; • the technical characteristics or requirements of the user's load or generation; • the nature of the plant or equipment required to provide the network access service; and • the periods for which the network access service is expected to be supplied.		• As part of the 2014 Network Price Determination process, PWC intends to undertake a major review of its pricing structures, particularly in relation to the declining block tariff arrangements and the 750MWh per annum threshold for the application of demand charges. The review will also canvass more cost reflective locational price signals, and standby and embedded generation charges. **Annual Pricing Proposals** • PWC seeks clarification from the UC as to what the annual pricing proposal approval process will be for the second and each subsequent regulatory year of the regulatory control period.
7.36	The indicative Network Pricing Proposal and tariff schedules for the year commencing 1 July 2014 should be consistent with the requirements of clause 6.18.2(b) of the NER.		• In consideration of the approval process, PWC requests that the UC be mindful of the requirements and timeframes of section 78 of the NT Access Code.
Capital Contributions Principles and Methods Statement			
7.46	The Commission's preliminary position is that PWC Networks should include in its regulatory proposal a draft Capital Contributions Principles and Methods Statement to apply to the setting of capital contributions towards works that would not be commercially viable without that capital contribution.	Agree	• PWC has submitted a revised Networks Capital Contributions Policy for consideration by the UC and commencement in the current regulatory control period. Unless significant issues arise with the proposed revised arrangements, this will form the basis of what PWC will submit as part of its regulatory proposal for the 2014 Network Price Determination.
7.47	The Commission expects that the draft Capital Contributions Principles and Methods Statement submitted as part of PWC Networks regulatory proposal for the 2014 Network Price Determination will be substantially the same as the final version of the revised NCCP currently under consideration.		
7.48	As such, any issues will be dealt with as part of this consultation process and should not need to be revisited.		

PARA REF.	COMMISSION'S PRELIMINARY POSITION	PWC POSITION	PWC'S COMMENTS AND PROPOSED AMENDMENTS
Other issues - Reconciliation of actual expenditure incurred during the third regulatory control period			
5.60 5.61 5.62	In its Final Methodology Decision for the 2009 Network Price Determination, the Commission foreshadowed that, before the end of the third regulatory control period, it would undertake a further assessment of actual operating and capital costs incurred by PWC Networks in supplying standard control services and a comparison of those costs with the relevant revenues received in that same period (or part thereof) in order to assess whether a further adjustment was required. A reconciliation of the actual expenditure that PWC Networks has incurred during in the third regulatory control period will form part of the Commission's assessment of required revenue for the 2014 Network Price Determination. The adoption of a forward building block approach removes the need to apply a 'base year' adjustment (Po) of the weighted average of network access tariffs at the end of the third regulatory control period. Rather, a different initial year X-factor in the fourth regulatory control period, if necessary, will serve to equalise (in terms of net present value) the network revenue to be earned by PWC Networks from the provision of standard control services over the regulatory control period with the total revenue requirement for the regulatory control period, with the use of the forward building block approach taking account of projected future costs in subsequent years.	Agree	• The UC did not utilise a forward-looking building blocks approach for the 2009 Network Price Determination. As such, PWC has essentially only received a return on and return of capital for 2008-09, and not on its forecast rolled forward RAB, for this current regulatory control period. • PWC strongly supports the UC's position that a reconciliation of the actual expenditure incurred by Power Networks during the third regulatory control period should be undertaken as part of the 2014 Network Price Determination process. • However, PWC requests that further consideration be given to how this will be achieved. The required revenue calculation under a forward building blocks approach will not provide for the return of and return on assets foregone during the current regulatory control period. • To ensure its ongoing commercial viability, PWC should receive a rate of return on its capital expenditure during the current regulatory control period, and the undepreciated value of its capital expenditure should be included in the RAB at the start of the new regulatory control period.