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Mr Philippe Laspeyres
Senior Regulatory Analyst
NT Utilities Commission
Sent by email

Dear Philippe

Re: 2014-2019 Regulatory Determination

Thank you for your invitation to Qenergy Limited (QEnergy) to provide a submission in relation to the Commission's *Framework and Approach Consultation Paper*.

QEnergy supports the adoption of Chapter 6 of the National Electricity Rules as the basis for network regulation in the Northern Territory. This is a well-known and well-regarded arrangement for regulating third party access and sends a strong and positive signal to potential new market entrants about the robustness of the Northern Territory regime.

QEnergy notes however that this regime is currently under review as a consequence of the Rule change applications that have been made by the Australian Energy Regulator (AER) and the Energy Users Association of Australia. These applications raise quite serious and well-considered concerns about the discretion provided to regulators under Chapter 6, and the interaction between network price rises and Government ownership of network companies.

We believe that the eventual outcome of these applications should, even if adapted by the Commission, be included within the Northern Territory regime if the final form of Chapter 6 remains under development. In particular, this means providing the Commission with adequate power and resourcing to critically review and assess the operating and capital expenditure forecasts, in particular the level of overheads being applied by the Northern Territory Power and Water Commission (PAWC) to standard and alternative control services. The Commission's intended move to a forward-looking building block assessment away from Total Factor Productivity will in all likelihood result in a large step increase in network prices unless it is countered with a very careful review of the efficiency of PAWC's overall operations.

QEnergy supports the use of a single determination for transmission and distribution networks. While there would clearly be some benefits to the Commission and market participants in understanding the true network cost for the Darwin / Katherine transmission line, a decision to separately price the Darwin and Katherine systems can be accomplished through the pricing arrangements and need not involve two separate revenue determinations.

QEnergy also supports the decision taken that the classification of services should remain consistent between this and the upcoming regulatory control period unless a compelling rationale can be found otherwise. QEnergy has some concerns relating to the definition of some services – in particular whether PAWC should legitimately be allowed to charge customers for providing them with their own (standard) metering information – however, changes to these prices can be accomplished without altering the service classification.

As a related matter, the Commission should also note that PAWC has, it appears, erred on the side of creating quoted fee arrangements for some services where a fixed fee arrangement could be sought. QEnergy will prepare submissions on these at the appropriate part of the process.

QEnergy does not support the continuation of the Weighted Average Price Cap Control (WAPC) mechanism in the Northern Territory. A WAPC, through its use as a pricing mechanism as much as a revenue control mechanism, allows PAWC to rebalance its prices away from competitive markets to non-competitive markets, thus driving up the Community Service Obligation and inhibiting the extent of competition. It is a reality that some parts of the Northern Territory are open to competition, and some parts are not.

The incentive mechanism created by the WAPC, which in completely open markets simply incentivises the network owner to rebalance its prices in a way that maximises its revenue, is no longer appropriate in the Northern Territory now that two new retailers have entered the market. QEnergy strongly encourages the Commission to assess whether the use of the WAPC in a competitive context meets the objectives of the Network Access Code. QEnergy does not consider that a compelling case can be made for its retention.

QEnergy does however support the use of a building block method for establishing forward-looking costs – this is a fair and reasonable method of determining revenue. It will be for the Commission to deal with the potentially large P_o adjustments which will be consequent to this decision. As noted further below, principles of prudency and efficiency will need to be rigorously applied if price increases are to be avoided.

QEnergy supports the use of the AER's PTRM and RFM models. QEnergy would caution the Commission away from simply accepting the actual capital expenditure in the previous period and allowing this to roll in automatically into the opening Regulatory Asset Base (RAB). There are significant issues associated with transitioning from a TFP approach to a building block approach, and a large RAB (and tax RAB) is probably the most significant of them. It is possible that this issue alone could drive a substantial price rise in 2014/15.

QEnergy supports the use of the relevant provisions of the NER for the establishment of forward operating and capital expenditure by networks. As noted above and below, efficiency will be a particularly important factor for the Commission in interpreting and applying the NER to Power and Water.

QEnergy generally supports the use of the AER's Cost Allocation Methodology (CAM) principles for the establishment of the appropriate proportions of overheads to the regulated business, and then to service classes. It will however be necessary for the CAM to be extremely broad in its scope in order to correctly place overheads and costs from the entire operations of Power and Water to the regulated portions and then to standard control services.

In this context, QEnergy considers that the Commission must acknowledge that the entire operations of Power and Water, and their efficiency, have an impact on competition in the retail market. As a vertically integrated, Government-owned generation, network and retail entity, there is a clear incentive for PAWC to direct its overheads towards networks and generation, and away from its retail functions. A decision by the Commission to cut overheads in networks, without scope to see where they are going after this decision, may in fact lead to higher wholesale costs for all customers.

QEnergy supports the adoption of an Efficiency Benefit Sharing Scheme although we doubt whether this would simply result in costs being allocated elsewhere by PAWC in the event that penalties were likely to be triggered. It is questionable whether the incentive powers inherent in the Scheme, which was designed to be applied to single purpose network companies, would create incentives within a vertically integrated monopoly that were ultimately unhelpful in the context of the Code objective.

Finally, QEnergy is comfortable with the indicative timetable laid out by the Commission. However, we are concerned to ensure that sufficient time is allocated to PAWC justifying its current allocation of revenue recovery, through principles of cost reflective pricing, between the various centres of Darwin / Katherine, Tennant Creek and Alice Springs, having particular regard to the incentives within the current system for PAWC to unduly inflate its network prices in competitive market areas such as Darwin / Katherine. The implication of this would be to ensure that smaller consumption customers – where there are regulated price impediments to competition – are more fully protected to PAWC and less open to competitive forces.

In QEnergy's view, a full assessment of the cost basis for prices, including a building block assessment, should be conducted to assess whether regional network tariffs are indeed cost reflective.

I would be pleased to discuss these issues, and this submission, in greater detail should you wish.

Yours sincerely

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