



ENERGY POLICY DIVISION

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**Natural Resources
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Letter follows.

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20 July 2001

Mr Mike Rawstron
General Manager
Electricity Group
Australian Competition and Consumer Commission
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Dear Mike

Victorian Derogations Pre-Determination Conference

I refer to Australian Energy Services' submission to the Commission calling a pre-determination conference relating to the Victorian derogations granted interim authorisation by the Commission earlier this month.

Louis Tirpou of your office has invited EPD to provide a preliminary written response in relation to the issue raised by AES regarding the exclusivity proposed to be granted to Local Network Service Providers (*LNSPs*) to act as the Responsible Person for type 5 metering installations.

We are aware that AES made a general submission, opposing the derogations, as part of the Commission's consultation process in relation to the interim authorisation and draft determination of the derogations. AES' current submission relates specifically to type 5 metering installations, and argues that the exclusivity proposed to be granted to LNSPs should not apply in respect of this type of metering installations. While the submission is not entirely clear, it appears that AES' arguments are limited to the category of customers consuming between 40MWh and 160MWh per annum, suggesting that the exclusivity would remain in place in respect of type 5 metering installations for customers having an annual consumption of less than 40MWh. AES' arguments proceed on the basis that a type 5 metering installation is almost the same as a type 4 metering installation (since both involve the use of interval meters) and that the contestable market has been effective for type 4 metering installations.

We understand that AES has installed a number of type 4 metering installations for customers on the basis that, once type 5 metering installations are able to be used, it will remove the communications equipment and convert the type 4 metering installation into a type 5 metering installation. We understand AES maintains that this will result in cost savings for the customer, however, we are uncertain as to the nature and timing of type 5 metering installation services that AES would be in a position to offer its customers.

EPD would be opposed to amending the derogations as proposed in AES' submission.

Meter Reading

AES' submission does not recognise the fundamental difference between type 4 metering installations and type 5 metering installations, which is that type 4 metering installations have remotely read meters and type 5 metering installations have manually read meters.

Whereas type 4 metering installations are read remotely on a daily basis by MDAs acting on behalf of NEMMCO, the Responsible Person for a type 5 metering installation is responsible for manual meter reading and for the associated data flows and processes that are set out in the metrology procedure that has been prepared for type 5 metering installations pursuant to the National Electricity Code.

We query AES' assertion that no new processes are required for type 5 metering installations and that the NEMMCO accredited MDAs are capable of providing all of the services required for type 5 metering installations. The wholesale market settlement process currently does not involve manually read meters. Accordingly, the introduction of this type of metering installation necessarily involves new systems and processes. As far as we are aware, the MDAs do not currently undertake manual meter reading or prepare the regular estimated data that will be required under the metrology procedure to facilitate wholesale market settlement on the basis of manually read meters.

In this regard, a type 5 metering installation is much more analogous to a type 6 or 7 metering installation in respect of which, as AES recognises in paragraph 8 of its letter, the LNSPs are currently best placed to provide the relevant services.

Meter Provision

In respect of meter provision, we note the views expressed by the Commission in the draft determination of the FRC related amendments to chapter 7 of the Code and the draft condition requiring the jurisdictional regulators to review this issue in 2003. In particular, the Commission noted that the cost savings derived from lower electricity prices in the below 160MWh per annum market are unlikely to be outweighed by the cost of a meter, and that it was unlikely retailers would bear the cost of meters where there was a risk of customers switching. It remains EPD's view that this issue needs to be addressed by the jurisdictions in light of market developments over the next few years, rather than lock in particular meter ownership positions at this stage.

The ORG has also expressed the view that providing for contestable meter provision in the type 5 category could have adverse implications for the roll out of interval meters. In particular, the ORG has noted that the proposal would mean a meter installed pursuant to a new and replacement policy could be subject to churn when the customer changes retailer. The ORG has suggested that it may be more difficult to obtain the cooperation of the businesses in the implementation of such a policy where different rules apply for first and second tier customers.

Cost Savings

AES argues that it has achieved better cost outcomes in respect of type 4 metering installations, using a competitive tender process, from a commercially driven metering provider than it was able to obtain from the LNSPs. We also understand AES maintains that converting type 4 metering installations into type 5 metering installations will result in further cost savings for its customers.

However, the LNSPs are not regulated in respect of the provision of type 4 metering installations, because this is not an exclusive service. The prices offered by LNSPs in respect of type 4 metering installations are indicative of the fact that LNSPs do not generally provide these services as part of their business, and do not enjoy economies of scale in this context.

The granting of exclusivity necessarily involves regulatory protection, as reflected in the draft derogations, which require the LNSPs to provide the relevant services on a fair and reasonable basis

and provide for price regulation through Victorian regulatory instruments. The Office of the Regulator-General is in the process of approving the excluded service charges that will apply in respect of type 5 metering installations.

It can be expected that the excluded service charges will be set on a basis that assumes the LNSPs have obtained any services to be provided to them on a competitive basis. The charges will also reflect the fact that, in respect of manual meter reading, the LNSPs do enjoy the benefits of significant economies of scale. Given these economies of scale, we query the extent to which cost savings in manual meter reading could be achieved through contestability in the early stages of FRC. We note that this position was also taken by the ORG in its recent price determination.

It is also worth noting in this respect that, in the absence of exclusivity, the regulatory protections that have been built into the derogations would not apply. Even if AES is in a position to offer competitive prices to its customers, this may not necessarily be the case for other independent retailers seeking to enter the market.

Other Issues

An amendment to the derogations that differentiated between classes of customer within the same type of metering installation would introduce an additional element of complexity in the metering arrangements for full retail competition. As you know, one of the main reasons for seeking the exclusivity derogations was to remove the layer of complexity resulting from contestable metering arrangements to assist in the smooth introduction of FRC. We consider having different arrangements apply for customers with the same type of metering installation could create the potential confusion and complication that we are seeking to avoid.

While we are sympathetic to AES' possible contractual position, it could be argued that there was a risk involved in offering such arrangements to customers while the regulatory instruments for FRC were still under development. It also seems to us the number of customers affected by this issue would be relatively small. NEMMCO's website indicates that, since 1 January 2001 (when customers consuming below 160MWh per annum became contestable), approximately 1,200 customers have switched retailer. Assuming the pre 1 January 2001 average rate of switching for customers consuming greater than 160MWh per annum, only around 800 of these customers would have a consumption level below 160MWh per annum and, accordingly, be entitled to move to a type 5 metering installation.

We suggest that it may be possible to find a more specific solution in relation to AES' position with its current type 4 customers consuming between 40MWh and 160MWh per annum, rather than seeking to address the issue through the regulatory framework for the entire FRC market.

I would be pleased to discuss any of the issues raised above, and would welcome the opportunity to provide a further submission following the pre-determination conference.

Yours sincerely



Peter Clements
Acting Executive Director
Energy Policy Division