NSWIC
NEW SOUTH WALES IRRIGATORS' COUNCIL

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Draft Submission

Essential Energy

Draft 2019 – 2024 Regulatory Proposal

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Introduction

The NSW Irrigators' Council (NSWIC) is the peak body representing irrigators and the irrigation industry in NSW. NSW irrigators hold water access licences to access regulated, unregulated and groundwater systems. Our Members include valley water user associations, food and fibre groups, irrigation corporations and community groups from the rice, cotton, dairy and horticultural industries.

NSWIC engages in advocacy and policy development on behalf of the irrigation sector. As an apolitical entity, the Council provides advice to all stakeholders and decision makers.

This submission represents the views of the Members of NSWIC with respect to Essential Energy's draft 2019-2024 regulatory proposal. However, each member reserves the right to independent policy on issues that directly relate to their areas of operation, expertise or any other issues that they may deem relevant.

Executive Summary

The NSW Irrigators' Council would like to provide the following summary recommendations to Essential Energy about the Draft Regulatory Proposal (2019-2024):

Affordability

- Affordability of future network distribution charges must remain the priority of Essential Energy in its development of the final regulatory proposal. The proposed average annual price increase of 1.63 per cent (real, 2017/18) is not acceptable for NSW irrigators as the current level of network distribution charges is already at a level that is unsustainable for the irrigation industry. As highlighted across the customer engagement workshops conducted by *Woolcott Research*, affordability was ranked higher in importance than reliability when customers were asked to compare and trade-off between the two issues.

Distributional Impacts

- The distributional impacts of the 1.63 per cent (real, 2017/18) average annual price increase is not clear from the Draft Regulatory proposal. NSWIC would like to see further detailed information from Essential Energy on how this average annual price increase is intended to be distributed amongst different tariff classes. Also, NSWIC would like to understand whether large customers - including irrigators – are likely to bear a disproportional burden of the price increase.

Cost Drivers

- The proposed average annual price increase of 1.63 per cent (real, 2017/18) highlights that the current regulatory system governing the revenue allowances for the Distribution Network Service Providers is broken. Despite best efforts and proposed reductions in both Operating and Capital expenditures by Essential Energy, current network distribution charges are scheduled to rise over the course of the next regulatory determination (and potentially beyond). NSWIC seeks a more detailed explanation from Essential Energy on how much of this price increase is due to the current regulatory requirements, including the calculations of the Weighted Average Cost of Capital, the derivation of the Regulated Asset Base and the current reliability standards, or is due to consumer demand.

Tariff Change Project

- The impact of the tariff change project needs to be clearly understood by those who are impacted by the change. As raised in previous consultation sessions with Essential Energy on the tariff change project, primary producers and irrigators who had previously operated under one of the now obsolete network distribution tariffs (and often do not have an interval meter), would have little understanding about their current electricity use, their demand profile or the implications of the change-over to the new (demand-driven) tariff classes. While NSWIC understands that Essential Energy had previously proposed, and the Australian Energy Regulator had accepted, a gradual phase-in of the new tariff provisions, further education and information need to be provided to customers about what the change may mean to affected customers financially. In addition, NSWIC calls on Essential Energy to work with these customers to potentially find alternative options to mitigate potential future cost increases.

Despite the concerns outlined above, NSWIC appreciates that Essential Energy is genuine about a long-term future reduction in the business' operating and capital expenditure. We also acknowledged that Essential Energy is considering more innovative and technology driven solutions to building a smarter grid. We welcome these developments and encourage Essential Energy to build its partnerships to address the ongoing changes in the National Electricity Market. There are many unknowns around the future development of the national grid and these uncertainties are likely to grow as consumers are provided with even more choices around installing their own energy generation and storage systems at home and on business premises. Further work and effort must be put into Essential Energy's demand management incentive and innovation allowance schemes to assess future cost-effective ways to deliver electricity to consumers in NSW.

Comments

The NSW Irrigators' Council welcomes the opportunity to provide comments to Essential Energy on the draft regulatory proposal 2019 – 2024. Since the last regulatory determination in 2014, NSWIC has noticed that Essential Energy's consultation and engagement has improved significantly. We have broadly welcomed this extended engagement and would like to encourage Essential Energy to build on this effort throughout this regulatory determination process and beyond. The National Energy Market and the structure and responsibilities of the businesses that operate within it are very complex and stakeholders will require ongoing information and consultation to meaningfully respond to both Essential Energy and the regulator on matters that concerns their electricity use and costs.

While we support the additional engagement and consultation by Essential Energy, we would like to raise the issue of balancing the need to make the information (i.e. regulatory proposals and Tariff Structure Statements) accessible whilst providing sufficient information for stakeholders interested in more in-depth data and information. NSWIC believes there is room for improvement, particularly around the drivers of the 1.63 per cent average annual cost increase, the tariff change project, the distributional impact of the average price increase and replacement capital expenditure.

In relation to the drivers of the cost increase, NSWIC would like to better understand how much of this proposed average annual price increase is driven by the current regulatory framework (i.e. the calculations of the Weighted Average Cost of Capital, the derivation of the Regulated Asset Base and the NSW reliability standard) versus consumer demand for new connections, services and activities.

It appears evident to NSWIC that the current regulatory framework is not fit-for-purpose if a regulated business proposes reductions in both Operational and Capital expenditure over the next regulatory period (please see further below) whilst network charges continue to rise. Based on the fact that the Regulated Asset Base and the Weighted Average Cost of Capital are key drivers of Essential Energy's future revenue allowance[1], the information that is provided by Essential Energy is extremely concerning. As per the information on page 44 of the draft regulatory proposal, customers in Essential Energy's service area will experience a rise in the value of the regulatory asset base until 2040, suggesting that a decrease in distribution network charges are unlikely to materialise prior to this point (unless further significant efficiency gains can be achieved for Essential Energy's operational expenditure). Given that current network distribution charges are considered unsustainable for many of Essential Energy's customers – including irrigators – this potential price projection is likely to accelerate the move to go off-grid, i.e. through the installation of individual energy generational assets (i.e. solar or otherwise) at home or on business premises. In order to incentivise customers to remain on the grid, it will be vital that Essential Energy redoubles its effort to find ways to drive down future distribution network charges and provide customers with more choice about their tariffs (including amendments to the proposed new tariffs related to new technologies – further below).

Further, NSWIC believes that the impact of Essential Energy's tariff change project is still not well understood by those impacted by the change. As NSWIC and others have raised during the previous consultation sessions, primary producers who have been on one of the now obsolete network distribution tariffs and who have not yet installed an interval meter, would have very little understanding about what the change would mean for them financially. NSWIC have been informed that the full impact of the tariff change project could be a doubling of costs without any corresponding increase in electricity use. Despite the proposal by Essential Energy and the acceptance by the Australian Energy Regulator to have a five-year phase-in period for the new tariff provisions, further education and information provision (i.e. bill impacts and alternative options to mitigate the price impacts) must be made available to those impacted by the change.

In addition, NSWIC seeks further detail on how the 1.63 per cent (real, 2017/18) average annual price increase will translate to actual price increases which are distributed across Essential Energy's various tariff classes. NSWIC has reviewed Essential Energy's draft Tariff Structure Statement (TSS) however was unable to find sufficient information or estimations that would indicate what the cost impact would be for large electricity users, including irrigators. It is a significant concern to NSWIC that the burden of the price increase will be disproportionally born by large electricity users. While we understand that the TSS process is different to Essential Energy's regulatory proposals, irrigators remain concerned about future price increases in light of overall falling Operating and Capital expenditures by Essential Energy.

Also, NSWIC would like to better understand the rationale for Essential Energy's augmentation and replacement capital proposals in the context of many unknowns in the National Electricity Market.

[1] Essential Energy Draft Regulatory Proposal, p. 44

As outlined by the draft regulatory proposal, the future of the energy market is highly uncertain, particularly given the increasing penetration of distributed energy generation, energy storage systems and other new technologies.

In respect to Essential Energy's other building blocks, NSWIC would like to raise its concerns about the Weighted Average Cost of Capital calculations (WACC), the revenue smoothing component, the proposed future capital expenditure and the revenue cap calculations.

In respect to the WACC calculations, NSWIC is concerned that the WACC calculations and the current value of the Regulated Asset Base would result in a proposed $2.55 billion return on capital – half of Essential Energy's proposed revenue allowance. As a state-owned corporation, this 'return' would be passed on to the State Government. It is simply untenable to continue to assume that such large returns for Essential Energy's debit and equity holders are justified. The WACC calculations provided by Essential Energy of 6.34% weighted average rate of return is far higher than current market conditions (i.e. subject to the Australian Energy Regulator review of the Rate of Return Guidelines which are expected to be completed in December 2018. We will continue to engage with the Australian Energy Regulator on the review of the Rate of Return Guidelines.) We encourage Essential Energy to make their actual returns accessible to the public.

Further, NSWIC would like to query the $7 million revenue smoothing component that Essential Energy is proposing for the next regulatory determination. Is Essential Energy able to clarify whether the additional $7 million would constitute an additional cost to customers over and above the proposed revenue requirements for Essential Energy?

In addition, NSWIC would like to query the proposed future capital expenditures by Essential Energy. As outlined in Appendix A of the draft regulatory proposal, Essential Energy's proposed forecast capital expenditure in 2018/19 is $472 million which is followed by $494 million in 2019/20. While both of these values appear to have different benchmark years, NSWIC cannot ascertain how this would constitute a decrease in capital expenditure. On the contrary, NSWIC suggests that the alleged 6% reduction in capital expenditure as outlined in the headline document is misleading. NSWIC strongly urges Essential Energy to provide further detail and information on the proposed capital expenditure, particularly around their proposed IT work worth $166 million as well as the replacement capital of $1,25 billion and the augmentation capital expenditures of $223 million.

Finally, NSWIC would like to seek further clarity on the revenue cap approach, particularly its application in the last year of the regulatory determination. Should the distribution network charges not match with forecast demand, NSWIC would like to understand whether the balance is carried over to the next regulatory period.

Tariff Structure Statement

NSWIC is encouraged that Essential Energy continues on the path of having a differential pricing structure for its peak, shoulder and off-peak rates. NSWIC and other consumer groups have been pushing for this differential pricing structure for a long time and we are glad that it is proposed to be carried forward into the new regulatory determination. In addition, NSWIC is also encouraged that Essential Energy has removed the morning peak for those customers who have interval meters.

Despite these positive developments however, NSWIC is disappointed that Essential Energy continues to suggest an increase in the fixed charge component of the network distribution charges. NSWIC cannot understand how an increase in fixed charges aligns with the principle of the 2014 Australian Energy Market Commission rule change on cost reflective tariffs. Further, fixed charges do not incentivise consumers to change their behaviour or encourages them to use less energy.

Furthermore, NSWIC would like to again stress that irrigators have no choice in their tariff assignment as many irrigation businesses are classified as large electricity consumers. The issues around the current tariff structure is well known to Essential Energy and will not be repeated here. However, NSWIC is slightly alarmed about a reference made in the draft regulatory proposal that suggests a 'pricing refence group' had given their support about how the current capacity charges were calculated. NSWIC tried to find further information on the pricing reference group and only found reference to one meeting which we attended. At this meeting, we made it very clear that we would like Essential Energy to consider alternative ways to calculate the current capacity charge component as the current charging mechanism does not align with irrigators' operation und unfairly penalises primary producers the form of higher charges and greater costs.

In conclusion, NSWIC believes there is a range of outstanding issues that require a resolution. Firstly, as outlined in previous discussions with Essential Energy, the issue around meter installation as part of the tariff change project still remains an ongoing issue for NSW irrigators. Further, those customers who are impacted by the tariff change project require further information and data about the financial impacts of the transition to new demand-driven tariffs. In conjunction with this issue, NSWIC encourages Essential Energy to work with customers around possible alternative technologies that could assist in mitigating the likely cost impacts.

On a related point, NSWIC is disappointed that Essential Energy seems to discourage the introduction of new technologies through the introduction of new opt-out demand drive tariffs for these technologies. Whilst Essential Energy suggests that the ongoing penetration of renewable energy into the National Electricity Market has significant cost impacts on the business, insufficient evidence or data has been provided that outlines what the magnitude (if any) of the cost has been on the business. The only evidence NSWIC could find in the draft regulatory proposal was the reference to "(the) biggest challenge for the network distributions are how to address demand and load caused by proliferation of new technologies and how to achieve energy exchange on the network". Stakeholders like NSWIC would like to see further evidence of addressing these demands and loads and suggest that instead of seeing the advancement in technologies and future smart systems as a cost, these technologies should be seen as a benefit.

ENDS.