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Mr Lewis W Owens
Chairperson
Essential Services Commission of South Australia
GPO Box 2605
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Dear Mr Owens

I refer to your letter dated 30 November 2004, providing me with a copy of the Essential Services Commission of South Australia (ESCOSA) Draft 2005 to 2010 Electricity Distribution Price Determination.

On behalf of the Government, I have made numerous submissions to ESCOSA on the various discussion and working conclusion papers that have been released for comment regarding the regulatory components that form the basis for this Draft Determination.

As I have noted previously, the Government considers that the Distribution Price Review process is critical for South Australian consumers, particularly as this is the first opportunity to review the pricing arrangements put in place by the former Government to maximise the proceeds from privatisation.

Accordingly, the government welcomes the Draft Determination and the proposed reduction in distribution prices for South Australian residential customers.

In particular, the Government strongly endorses the reaffirmed position of ESCOSA not to revalue easements. Consistent with my previous submission regarding the value of easements, the Government considers that easements have a different nature to other assets, as they are not likely to be replaced and are not consumed over time. Importantly, this decision ensures that consumers are not subjected to upward price shocks as a result of a large revaluation of the value of easements.

Additionally, the Government supports the pre-tax real Weighted Average Cost of Capital (WACC) that has been included in the Draft Decision, especially since it is consistent with comparable WACC decisions made recently by regulators in other jurisdictions, in particular that of the NSW Independent Pricing and Regulatory Tribunal (IPART).

The Government notes that when setting the level of capital and operational expenditure benchmarks, ESCOSA must strike a balance between ensuring the lowest possible cost to consumers against the need for continued investment in the electricity network. I have previously noted the results of the Consumer Preference Survey, that indicated that consumers were not generally willing to pay for an increase in reliability.

Accordingly, the tasks for ESCOSA is to find the funding level that allows ETSA Utilities to maintain the current reliability and service levels over the medium to longer terms, nothing that the decision allows for an immediate improvement in services for Kangaroo Island residents. I note that following the PB Associates review, ESCOSA have determined that the capital expenditure level will be increased by 35 percent from current levels, mainly owing to the ageing nature of the network assets.

In my submission, dated 6 September 2004, on the Working Conclusions Paper concerning Prescribed and Excluded Distribution Services, I noted some concern regarding the allowance for the establishment of processes and systems to ensure that ETSA Utilities is capable of acting as the Retailer of Last Resort (ROLR).

I further noted that the Government had introduced legislation to require that ESCOSA make it a condition of a retail licence that retailers be required to provide retail services on behalf of ETSA Utilities should it be requested to do so by ESCOSA, and therefore any allowance for the establishment of ROLR systems should be minimal.

In the Draft Distribution Price Determination, \$1 million per annum has been allowed for the "potential operating costs" ETSA Utilities will incur in establishing the capability to provide ROLR services. I note that the Draft Determination does not provide any detail on what would be provided by this expenditure and why there is an ongoing requirement for \$1 million per annum.

Given that retailers would be obliged to provide ROLR services, it would appear that the allowance for ROLR service ahead of any such event is excessive, since ETSA Utilities should only need to establish a process for communication with retailers. Retailer costs incurred during a ROLR event are a separate issue, since these would be recovered, as appropriate, after the event. In any case, I encourage ESCOSA to explain its decision in relation to ROLR services as part of the Final Determination or to remove this provision entirely.

I would like to take this opportunity to thank ESCOSA for the robust manner in which this Distribution Price Review has been conducted. The Draft Determination is a good result for all South Australians, not only in terms of a reduction in prices, but also as it includes increases in expenditure to ensure continued reliability.

Overall, the Government's view is that ESCOSA has got the balance between cost to consumers and funding of network infrastructure substantially right in its Draft Determination and would expect a similar outcome to be reflected in the Final Determination.

Yours sincerely



HON PATRICK CONLON MP
MINISTER FOR ENERGY

25 January 2005