



**Structure of licence fees for the electricity, gas and  
water and sewerage sectors**

**Consultation Paper**

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# 1 INTRODUCTION

## 1.1 Purpose of this paper

The purpose of this consultation paper is to provide an overview of the process, and considerations, of the Regulator in determining licence fees (or their equivalent) under the *Electricity Supply Industry Act 1995* (the ESI Act); the *Water and Sewerage Industry Act 2008* (WSI Act); the *Gas Act 2000* and the *Gas Pipelines Act 2000* (Gas Acts) for the three-year period 1 July 2017 to 30 June 2020.

The Office of the Tasmanian Economic Regulator (OTTER) supports the Regulator in undertaking its functions under the four Acts mentioned above. Each of these Acts provides, in effect, for the Regulator to recover its reasonable costs in the administration of those Acts through licence fees or other means.

The Regulator has prepared a “Draft structure of licence fees for the electricity, gas and water and sewerage sectors” (Draft Structure of Licence Fees) for application from 1 July 2017, provided in addition to this paper, and invites comment from licensees and interested parties.

The Draft Structure of Licence Fees varies from the current approved structure (applicable until 30 June 2017) in that it proposes a move to fully variable licence fees for electricity and gas entities (with the exception of small LPG gas distributors and retailers who will continue to pay a nominal amount). Such an approach is considered more cost reflective and simpler than the current application of fixed licence fee components, for some licensees, which has increased the complexity of licence fee calculations and has not addressed volatility in regulatory effort applied to individual entities within industry sectors between the years.

The Draft Structure of Licence Fees also proposes a change to the calculation of part year licence fees for new entrants into the electricity, gas and water and sewerage sectors. Specifically, it is proposed that licence fees for new entrants be determined on a case-by-case basis. This approach is offered on the basis that the likelihood of new entrants is minimal and that it would afford the Regulator greater flexibility in determining a licence fee more accurately tailored to an individual entity.

## 1.2 Background

Since its inception, the Tasmanian Electricity Code (TEC) has required the Regulator to develop an electricity licence fee structure that is consistent with a set of principles set down in that TEC.

The structure of electricity licence fees is reviewed periodically. The last review was completed in early 2014 and applies to the period 1 July 2014 to 30 June 2017. The outcomes of the 2014 review were outlined in the Regulator’s publication titled *Structure of licence fees for the electricity, gas and water and sewerage sectors - March 2014*.

The Draft Structure of Licence Fees documents the methodology that applies in the determination of licence fees (or their equivalent) in all areas of the Regulator's industry-funded activities (electricity, gas and water and sewerage).

In addition to licence fees, certain industry-funded activities are invoiced directly to the entity concerned. For example, the Tasmanian Water and Sewerage Corporation Pty Ltd (TasWater) will be invoiced separately for costs associated with the upcoming Price Determination Investigation.

### 1.3 Consultation

Transparency is a feature of the Tasmanian regulatory regime and the Regulator provides opportunity for industry, customer and interested party participation in its processes. This consultation paper is issued in accordance with the *Consultation Policy and Procedures of the Regulator (Version 6, November 2016)* and the TEC.

Written submissions on this consultation paper and the attached "Draft Structure of Licence Fees" may be forwarded to:

The Director  
Office of the Tasmanian Economic Regulator  
GPO Box 770  
HOBART TAS 7000

or by email to

[office@economicregulator.tas.gov.au](mailto:office@economicregulator.tas.gov.au)

marked to the attention of the Director, Office of the Tasmanian Economic Regulator.

Submissions must be received by no later than 10 February 2017.

It is normal practice for all submissions to be published on the Regulator's website unless the author of the submission requests confidentiality in relation to the submission (or any part of the submission). Those parts of a submission that are requested to be kept confidential should be submitted as an attachment to that part suitable for publication.

The Regulator will not publish submissions which contain material that the Regulator believes is, or could be, derogatory or defamatory.

Following the consideration of relevant matters contained in submissions, a final structure of licence fees will be published by 31 March 2017.

## 2 CONTEXT

### 2.1 Electricity supply industry

#### 2.1.1 Legislative framework

The *Electricity Supply Industry Act 1995* (ESI Act) provides for the issue of a licence subject to a number of conditions including ‘... *the electricity entity must pay periodic and other fees and charges fixed by or in accordance with the licence*’.<sup>1</sup> Through the TEC, the Regulator has established technical standards and administrative arrangements that apply to licensed entities within the Tasmanian electricity supply industry. The TEC provides for the payment of licence fees by licensed electricity entities in Tasmania to meet the budgeted revenue requirements of the Regulator.

##### 2.1.1.1 TEC requirements - structure of licence fees

The TEC requires the Regulator to develop, review and publish, in consultation with licensees and such other persons as the Regulator considers appropriate, the Structure of Licence Fees for such periods as the Regulator considers appropriate. In undertaking the process, the Regulator must consider other fee structures in existence that it thinks appropriate for comparison purposes.

The TEC also identifies certain principles that should guide the Structure of Licence Fees, namely that it be simple; recover the budgeted revenue requirements of the Regulator; be reflective of the extent to which the budgeted revenue requirements involve that licensee; and that it not unreasonably discriminate against licensees.

The TEC requires the Regulator to publish a report that sets out the fee structure that has been determined, the methods used in determining the fee structure and an assessment of the extent to which it complies with the principles set out in Chapter 2 of the TEC. The structure must be published at least three months prior to the implementation of the structure.

Costs incurred by the Regulator in undertaking price investigations under the *Electricity Supply Industry (Pricing and Related Matters) Regulations 2013* are recovered separately from those businesses that are the subject of the investigation. By doing so, these relatively infrequent and resource-intensive activities can be excluded from licence fee calculations. However, costs incurred in administering a price determination after the conclusion of an investigation are recovered through licence fees.

### 2.2 Water and sewerage industry

Section 39 of the Water and Sewerage Industry (WSI) Act sets out the legislative obligations in relation to the setting and payment of annual licence fees. Unlike the

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<sup>1</sup> ESI Act, section 22

electricity and gas supply industries, the Regulator does not determine the licence fees in the water and sewerage sector. The Draft Structure of Licence Fees reflects how the Regulator currently determines its portion of these annual licence fees.

Section 39 (1) states:

(1) The Regulator must require a regulated entity to pay to the Minister such amount, by way of an annual licence fee, as the Minister may from time to time determine in respect of the following:

- (a) a licence;
- (b) an interim licence granted under section 89.

and 39(4):

(4) The amount so determined by the Minister is to be an amount that the Minister considers to be a reasonable contribution towards the cost of administering this Act, including any of the following:

- (a) the costs to be incurred by the Regulator in performing functions and exercising powers, under this Act;
- (b) the costs to be incurred by the Ombudsman in investigating complaints under section 76;
- (c) the costs which will arise from the regulation, by prescribed persons, of activities specified in the licence –

during the year to which the fee relates, in relation to a regulated entity.

As with the electricity supply industry, costs incurred by the Regulator in undertaking price investigations under the *Water and Sewerage Industry (Pricing and Related Matters) Regulations 2011* are recovered separately from licence fees. However, costs incurred in administering a water and sewerage price determination after the conclusion of an investigation are recovered through licence fees.

## **2.3 Gas industry**

### **2.3.1 Gas Act**

Section 27 of the Gas Act is relevant in the setting of annual licence fees for gas supply industry participants. Section 27(1) states:

A person is not entitled to the issue or renewal of a licence unless the person first pays to the Regulator the relevant annual licence fee, or the first instalment of the relevant annual licence fee, as the case may require.

And section 27(2)(b):

The holder of a licence issued for a term of 2 years or more must in each year (other than a year in which the licence is due to expire) pay to the Regulator,

before the date prescribed for that purpose, the relevant annual licence fee, or the first instalment of the relevant annual licence fee, as the case may require.

And section 27(3):

(3) Subject to subsection (4), the annual licence fee for the distribution and retailing of gas is to be a fee fixed by the Regulator of an amount that the Regulator considers appropriate as a reasonable contribution towards the costs of administration of this Act having regard to the nature and scale of the operations that are authorised by the licence.

Note that the costs of administration of the Gas Act can include the costs of both the Regulator and the Director of Gas Safety.

### **2.3.2 Gas Pipelines Act**

An annual licence fee is also chargeable under the Gas Pipelines Act, which states at section 14(1):

A licensee must pay to the Regulator annually and in advance a fee determined by the Regulator that represents the reasonable cost of the administration of this Act with respect to the relevant pipeline licence.

Again, the costs of administration of the Act can include the costs of both the Regulator and the Director of Gas Safety.

## **3 PRINCIPLES**

### **3.1 Principles to be applied by the Regulator in determining the fee structure**

In determining the fee structure in the electricity supply industry, the Regulator is bound by the TEC. The TEC requires that the Structure of Licence Fees be consistent with a set of principles. As part of its last structure review, the Regulator extended the application of these principles to the setting of fee structures for the gas and water and sewerage sectors. In this way, the principles are now applied in the determination of licence fees across all regulated industries under the Regulator's purview.

The principles to be applied in setting a licence fee structure are as follows:

- The Structure of Licence Fees will be simple.
- Licence fees will recover the budgeted revenue requirements for the Regulator.
- The Regulator will prepare a budget before the beginning of each financial year which will identify the Regulator's revenue requirements and will take into account any revenue requirement shortfall or surplus from the previous year, as can reasonably be determined at the time of preparing the budget.

- The components of the licence fees charged to each licensee will be reflective of the extent to which the Regulator's budgeted revenue requirements for the Regulator involve that licensee.
- Licence fees will not unreasonably discriminate against licensees.

In undertaking this process, the Regulator will consider other fee structures in existence which it thinks appropriate for comparison purposes.

## **4 COST DRIVERS**

### **4.1 Regulator's activities**

The Regulator's objectives and functions under the ESI Act, WSI Act, Gas Pipelines Act and Gas Act are met through the conduct of a number of activities and projects. These are reflected in the Regulator's operating plan and annual report which are published each year on the OTTER website.

### **4.2 The Regulator's total budgeted revenue requirement**

Provided that there are no significant deviations in the Regulator's anticipated responsibilities and functions over the next three years, any variations in the Regulator's overall budget will be primarily reflective of changes in staff salaries. Licence fees for licenced entities will, however, change to reflect activity in the relevant sector and, as relevant, increased or decreased regulatory effort applied to the licensee(s) concerned.

As discussed under section 6 below, and following introduction of proposed amendments to the TEC, the estimated licence fees for 2017-18, with respect to licenced entities in all industry sectors, will be produced by OTTER by (approximately) end February 2017 and will be based on the Structure of Licence Fees approved to apply from 1 July 2017. The final licence fees for 2017-18, the calculation of which will include the actual expenditures of the Regulator for the 2016-17 financial year, will then be prepared and distributed to licenced entities after 1 July 2017. It is proposed that this process will operate on an annual basis.

## **5 CONSIDERATION OF OTHER FEE STRUCTURES**

The TEC requires the Regulator, in developing a Structure of Licence Fees for the electricity supply industry, to "*consider other fee structures in existence, which it thinks*

*appropriate for comparison purposes*”.<sup>2</sup> The Regulator has also considered other fee structures in the gas and water and sewerage sectors where appropriate for comparison purposes.

Direct comparison of the quantum of licence fees in each jurisdiction is not necessarily useful. The budgeted revenue requirements for each regulator will depend on the range of regulatory activities to be met by the funding and the size of the regulated industries. The number of licensees in a jurisdiction over which the costs can be spread can differ significantly. The budgeted revenue requirements of some other jurisdictions also include other costs driven by requirements specific to the jurisdiction. Further it is noted that the transfer of functions to the national bodies (Australian Energy Regulator, Australian Energy Market Operator and the Australian Energy Market Commission) may also impact on the quantum of costs incurred and thus the state and territory regulators’ revenue requirements.

The Regulator has considered the licence fee methodologies of other jurisdictional energy regulators. Research in this regard has indicated that budgeted revenue requirements are largely met by the industries which are regulated, with licence fees being representative of regulatory effort (time spent on regulatory activities).

Having regard to these other fee structures, the Regulator has prepared a “Draft Structure of Licence Fees”, provided additionally to this paper, for application from 1 July 2017.

## 6 KEY CHANGES

As noted in section 3, the Regulator is required to prepare and publish, before the beginning of each financial year, a preliminary budget of the revenue requirements for the Regulator for that financial year, and this is to include the Regulator's estimated expenditures for the current financial year.

However, estimating expenditure for the current financial year is traditionally done by OTTER staff in the final day(s) of the financial year and is a very time consuming and labour intensive exercise. To be able to prepare and publish the preliminary budget before the beginning of the financial year with this information included, as required by the TEC, is difficult. Furthermore, publishing the Regulator’s preliminary budget before the beginning of the financial year is of little importance to licenced entities, which, undoubtedly, would be more interested in an estimate of their licence fee for the forthcoming year, as opposed to the Regulator’s overall budget requirement.

The Regulator, therefore, proposes to amend clause 2.4.3 of the TEC to remove the relevant ‘preliminary budget of the revenue requirements for the Regulator’ provisions. In addition, the Regulator proposes to include in the Structure of Licence

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<sup>2</sup> Clause 2.4.1(c) of the TEC

Fees requirements with respect to the timing of its preparation, and notification to licensees, of estimates and actual licence fees payable.

To this end, the Draft Structure of Licence Fees has been prepared to include provisions that licence holders will be notified by the Regulator early in the calendar year of a licence fee estimate for that licensee for the forthcoming financial year. That is, the Regulator will advise licensees of their estimated licence fee by (approximately) the end of February. The final licence fees for the forthcoming year, the calculation of which will include the actual expenditures of the Regulator for the previous financial year, will then be prepared and distributed to licenced entities after 1 July.

Preparing and providing licence fee estimates in February, as proposed, is the earliest feasible date at which OTTER is able to more accurately calculate estimates based on its internal budgeting timeline. It is anticipated that the February notification of licence fee estimates will also work well with the budgetary processes of individual licensees.

The Regulator, therefore, proposes that amendments to the TEC be progressed immediately to facilitate the above suggested approach. The Regulator proposes to progress all required Code amendments in accordance with the 'fast track' provisions of the TEC.