

15 February 2013

Mr Warwick Anderson
General Manager – Network Regulation Branch
Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

Dear Mr Anderson

Response to Rate of Return Guideline Issues Paper

ActewAGL Distribution welcomes the opportunity to provide this submission in response to the AER's Rate of Return Guidelines Issues Paper.

ActewAGL Distribution is a member of the Energy Networks Association (ENA) and has contributed to and supports the ENA's comprehensive submission in response to the AER's Rate of Return Guideline Issues Paper. In addition to the matters raised in the ENA's submission, ActewAGL Distribution would like to note the following.

- ActewAGL Distribution considers that it is in all stakeholders' interest to establish a predictable and transparent framework for determining the overall Weighted Average Cost of Capital (WACC). The Rate of Return Guideline should provide sufficient clarity to allow stakeholders to replicate the calculation of the applicable rate of return at any time to improve predictability of outcomes. This was also the intention by the Australian Energy Market Commission (AEMC):

“The Commission expects that the guidelines will provide service providers and other stakeholders with an ability to make a good estimate of the rate of return for particular businesses at particular points in time.”¹

A framework that results in unpredictable outcomes over time would increase risk and result in higher funding costs which would flow on to consumers. However, ActewAGL Distribution also notes that it is paramount that the framework is flexible enough to ensure that the overall rate of return objective is achieved even when market circumstances are unusual.

- In addition to a predictable method, ActewAGL Distribution would, where possible, support a methodology and framework that results in stable rate of return outcomes. If there is an option to choose between two modelling approaches that both result in a rate of return consistent with the rate of return objective, ActewAGL Distribution's preference is to choose the model/method that generates more stable outcomes over time. ActewAGL Distribution believes that this would be in the interest of all stakeholders, supporting price stability and steady investment in the network so that customers would not face unnecessary volatility in reliability or tariffs across multiple control periods. It is paramount, however, that all outcomes are consistent with the rate of return objective.

¹ AEMC, Rule Determination, Final National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012 and National Gas Amendment (Price and Revenue Regulation of Gas Services) Rule 2012, p 57

- In relation to the AER's question of what individual cost of equity model best meets the allowed rate of return objective, ActewAGL Distribution does not believe there is one single model that should be relied on or which is 'best'. On the contrary, the Rate of Return Guidelines and future determinations should have regard to relevant estimation methods, financial models, market data and other evidence to ensure that a representative rate of return consistent with the rate of return objective can be determined. ActewAGL Distribution considers that this also has been clearly set out by the AEMC:

"Whether or not the estimated rate of return meets the allowed rate of return objective will invariably require some level of judgement, but this judgement should be based with reference to all relevant estimation methods, financial models, market data and other evidence that could reasonably be expected to inform a regulator's decision."²

- In relation to estimating the cost of debt, ActewAGL Distribution supports a guideline taking into account individual business's circumstances in relation to the appropriateness of an "on the day" approach or a trailing average sample period. In addition, ActewAGL Distribution considers that its relative size and corporate structure via partnership might provide a case that in a determination process would require further consideration. Also, ActewAGL Distribution would expect the AER to acknowledge that debt raising costs would be substantially higher when smaller tranches of bonds are issued.
- Finally, ActewAGL Distribution is a multi energy utility providing gas and electricity distribution services. ActewAGL Distribution supports the AER investigating whether there is a difference in the systematic risk between gas and electricity distribution services.

ActewAGL Distribution is conscious of the fact that market circumstances constantly change. With this in mind, if there are special circumstances, the Rate of Return Guideline must contain sufficient flexibility that a determination can achieve the rate of return objective set out in the new NER.

ActewAGL Distribution is keen to participate in the AER's Rate of Return Guideline process. Should you wish to discuss any of the raised matters above in detail, please contact Björn Tibell, Senior Financial Advisor on (02) 6248 3639 if you would like to discuss any aspects of our proposal.

Yours sincerely



David Graham
Director Regulatory Affairs and Pricing

² AEMC, Rule Determination, Final National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012 and National Gas Amendment (Price and Revenue Regulation of Gas Services) Rule 2012, pp 66-67