

19 August 2010

Mr Chris Pattas
General Manager Network Regulation South
Australian Energy Regulator
GPO Box 520
Melbourne
VIC 3001

By email: aer inquiry@aer.gov.au

Dear Mr Pattas

Submission in response to the AER draft electricity distribution determination for Victoria and the distribution businesses revised revenue proposals

The Consumer Utilities Advocacy Centre Ltd (CUAC) would like to thank the Australian Energy Regulator (AER) for the opportunity to comment on their draft decision and the revised revenue proposals from the Victorian distribution network service providers (DNSPs). CUAC represents the interest of Victorian electricity consumers in regulatory processes. The ultimate outcome of this distribution determination process will have significant bearing on the price that these consumers pay for their electricity over the next five years. In developing this response, CUAC has regard to both the affordability and reliability of electricity supply to end users in Victoria.

CUAC had been concerned that the original revenue proposals developed by Victoria's five DNSPs had sought revenue that was above the level that was required for the efficient operation of their respective distribution networks. Were these proposals accepted, consumers would have been paying an excessive amount for the provision of electricity to their homes and businesses.

CUAC was particularly concerned that the forecasting used by the DNSPs to justify their revenue requirements was an inaccurate guide or reference point for the determination of revenue and expenditure into the future. Given this, CUAC was pleased at the approach taken by the AER that adopted a more realistic approach to the appropriate calculation of future revenue requirements. CUAC is of the view that the revenue requirements of the five DNSPs as amended by the AER in their draft decision were measured and appropriate. However, the revised proposals submitted by the DNSPs in response to this draft decision seem again to be out of step with required revenue levels for the efficient operation of the network. CUAC urges the AER to closely consider the revised DNSP proposals and maintain the high levels of regulatory scrutiny that were evident in the draft decision.

Forecast versus historical expenditure

It seems that a key point of contention between the AER and the DNSPs relates to the most appropriate method for calculating the future revenue requirement. DNSPs seem largely to have relied on forecasts developed for them by the National Institute of Economic and Industry Research (NIEIR). The AER, in contrast, has adopted a revealed cost approach through the use of historical expenditure trends.

In CUAC's submission in response to the DNSPs original proposals, CUAC noted the fallibility of forecasting techniques and opined that such forecasts could not be relied upon to set efficient revenue levels in the regulatory period going forward. CUAC supports the AER's alternative approach in the draft decision of examining historical expenditure levels. An examination of trend levels of network expenditure suggests a fairly predictable trend. CUAC could not see any substantive reason why the DNSPs required revenue significantly in excess of the historical trend for the 2011-2015 period. Moreover, CUAC is of the view that any ageing network assets should be replaced progressively over time to ensure the minimisation of one-off price impacts to consumers. This is in contrast with the approach adopted in DNSP proposals, which advocate significant up front capital expenditure.

CUAC supports the approach taken by the AER in its draft decision that relies on revealed cost and historical experience as a basis for predicting future expenditure. CUAC is of the view that such an approach is consistent with the National Electricity Rules and will provide DNSPs with adequate revenue to maintain service standards. The maintenance of a revealed cost approach in the draft decision is, in CUAC's view, strongly in the consumer interest.

Market risk premium

CUAC remains unconvinced that the market risk premium (MRP) of 6.5 per cent is appropriate given the continuing strength of the Australian Economy and the relatively secure operating environment confronted by the Victorian distribution businesses. CUAC recommend that the AER consider the possibility of a reduction in the MRP to the 6 per cent that was originally established in the explanatory statement on the review of the weighted average cost of capital (WACC) parameters in 2008. The more secure global economic position results in lower costs of finance and should be sufficient for, at the very least, a reconsideration of the elevated market risk premium.

Further consultation required on tariff setting and approval process

CUAC notes that there is limited time available for the network tariff approval process and no requirement for this process to occur in consultation with consumers. CUAC urges the AER to adopt a collaborative process to tariff approvals that involve cooperation between DNSPs, consumer groups and the AER. It would be desirable for the DNSPs to provide information on their proposed tariffs prior to the date required by the timetable for the regulatory determination to allow time for consultation with consumer representatives. It is not only the amount of revenue collected by DNSPs that impacts on affordability and the consumer experience. Tariff structures and the way that tariffs are applied to different classes of consumers can also have a significant impact on the affordability of electricity for certain members of the community. CUAC emphasises the importance of consumer

involvement in tariff setting process in order to ensure the appropriateness of the proposed network tariffs through a transparent process.

Consumer Advocacy Panel procedures and the inability to share information between consumer groups

CUAC notes that the Consumer Action Law Centre (Consumer Action) has received support from the Consumer Advocacy Panel (CAP) to engage a consultant to review the draft determination and revised DNSP proposals. However, as a result of the new procedures implemented by the Consumer Advocacy Panel at the instigation of the Ministerial Council on Energy (MCE), CUAC is unable to access the work undertaken as part of the CAP funded project. The new procedures require the MCE to 'vet' any projects that are funded by the Consumer Advocacy Panel prior to the public release of the project findings. This is a significant barrier to the sharing of relevant research and information into energy policy and regulation from a consumer perspective. This limits the availability of information and evidence for this submission. CUAC encourages the AER to express its concern to the MCE about these new restrictive procedures.

Once again, CUAC would like to thank the AER for the opportunity to comment on this important regulatory process. If you have any queries about this submission, do not hesitate to contact David Stanford on 03 9639 7600.

Yours sincerely,



Jo Benvenuti
Executive Officer