Ethnic Communities' Council of NSW Inc.

221 Cope Street Waterloo NSW 2017
Tel: (02)9319 0288 Fax: (02)9319 4229 Email: energy@eccnsw.org.au

11 October 2013

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

Dear Mr Anderson

Submission to Better Regulation: Draft Rate of Return Guidelines

This submission is made on behalf of the Ethnic Communities Council of NSW (ECC) and the Federation of Ethnic Communities Councils of Australia (FECCA). We welcome the opportunity to comment on the ***AER Draft Rate of Return Guidelines***

Since its formation 36 years ago the ECC NSW has been the peak body for culturally and linguistically diverse (CALD) community members and representative organisations in NSW. The ECC's main activities are advocacy, education and community development and it has managed a program providing information to CALD communities and businesses to enable them to live sustainably, including energy efficiency, for more than 15 years.

The ECC NSW is a member of the Federation of Ethnic Communities Councils of Australia (FECCA). In recognition of the NSW sustainability and energy efficiency expertise, FECCA has based the national energy advocacy role within the ECC NSW.

Background

The Australian Energy Market Commission (AEMC) made a number of important changes to the rules governing electricity distribution pricing regulation in November 2012. As a result of this, the Australian Energy Regulator (AER) commenced the Better Regulation program in December 2012.

A key aspect of the new regulatory program is the ***Draft Rate of Return Guidelines*** published in August 2013. In the past AER determinations have delivered rates of return well in excess of the cost of capital which contributed to higher network prices for consumers. The AER acknowledges that the return on investment can make up approximately 50% of revenue needs for network businesses.

The guidelines set out a new approach allowing the AER to determine rates of return over time that is consistent with market conditions and in the long term interests of consumers. For this reason the **ECC recommends that the guidelines are mandatory not optional.**

ECC's position

The ECC due to resource constraints was unable to take an active role in the development of these guidelines. Our role has been one of listening to both the AER

Community Reference Group (CRG) forums and to other more active participants who are also members of the CRG. As a result of these activities, the ECC has concluded that it supports the position taken by the NSW Public Interest Advocacy Centre (PIAC) in their submission on these guidelines.

The ECC is particularly concerned with two main issues:

1. The support of the foundation model, the Sharpe Lintner Capital Asset Pricing Model (SL CAPM) when assessing the return on equity. The Network Service Providers (NSPs) are low risk businesses and this model is commonly used by regulators and investors. The NSPs prefer a range of models so that they are able to take advantage of current market occurrences.

   SL CAPM although not perfect has standing and will give consumers some security as a firm model that will provide consumers with a positive outcome when the market is strong. This will also mean some losses for consumers. We think it is appropriate that consumers share the risk and reward, rather than changing models according to the vagaries of the market-giving networks all the reward and consumers all the risk.

2. The return on debt at present assumes that businesses raise all their debt at the same time, once every five years. The ECC supports the AER's proposal of transitioning to a 'trailing average' portfolio approach which aligns closely with efficient debt financing practices of regulated businesses and should lead to less volatile prices over time for consumers.

   However the ECC prefers a 5 years regulatory period which, for example, the Energy Retailers Association has adopted, having found it to be consistent with current debt financing practice. Five year markets are also far more liquid and offer more accurate and consistent measurement. On this basis, we would support the use of a 5 rather than 7 year term, which would also be easier to implement. The use of a 5 year period would also lessen the need for a messy transition to the new arrangement.

If you have any questions about this submission, please do not hesitate to contact Helen Scott on 02 9319 0288 or 0425 833 892.

Sincerely yours,

Mark Franklin
Executive Officer
Ethnic Communities' Council of NSW Inc.