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By Email

Dear Ms Conboy

United Energy Revised Regulatory Proposal 2016-2020

On 6 January 2016, we submitted our Revised Regulatory Proposal for the 2016-2020 regulatory period to the AER.

Since that time the Australian Competition Tribunal (Tribunal) has handed down its decisions in respect of the Networks New South Wales and ActewAGL Distribution merits review applications.¹ We acknowledge that the AER has sought judicial review of the Tribunal's decisions. However, we understand the AER's applications for judicial review will not be heard prior to the release of the AER's Final Decision which we understand is by the end of May 2016.

One matter, the subject of the Tribunal decisions, which is common to our Distribution Determination relates to gamma. The AER took the same approach to estimating gamma in the Networks New South Wales and ActewAGL decisions as it did in its Preliminary Decision for United Energy and adopted a value of imputation credits of 0.4 from within a range of 0.3 to 0.5.

In our Revised Regulatory Proposal we submitted that the best estimate of gamma was 0.25, calculated as a distribution rate of 0.7 x theta of 0.35 (based on SFG's updated dividend drop-off study).²

The Tribunal in *Ausgrid* found error in the AER's approach to estimating the value of imputation credits. In particular the Tribunal found that:

1. In respect of the distribution rate, the AER erred in using a listed equity only measure (0.8) and that it is appropriate to follow the past practice of using an all equity based estimate, giving a distribution rate of 0.7.³

¹ The lead decision being in *Applications by Public Interest Advocacy Centre Ltd and Ausgrid 26 February 2016*, [2016] ACompT1(*Ausgrid*).

² UED, Response to AER Preliminary Determination Re: Rate of Return and gamma, Chapter 5.

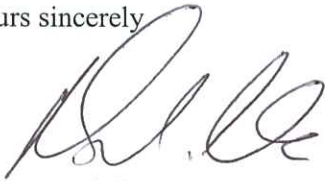
³ At [1104] to [1106].

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2. That tax statistics can only provide an upper bound on the estimate of theta.⁴
 3. The equity ownership approach overstates the redemption rate and are above the true maximum possible figure for theta. That approach can only be used, like tax statistics, as a check on other estimates.⁵
 4. The AER's equity ownership and tax statistics approaches are inconsistent with a proper interpretation of the Officer Framework underlying Section 6.5.3 of the NEL.⁶
 5. For this reason the equity ownership approach and tax statistics estimates can be no better than upper bounds on the market value of imputation credits.⁷
 6. It follows that the assessment of theta must rely on market studies.⁸
 7. That the best estimate of theta is that derived from the updated SFG study of 0.35.⁹
 8. The AER's conceptual approach to gamma, redefining it as the value of imputation credits that are available for redemption, is inconsistent with the concept of gamma in the Officer Framework for the WACC and the objective of ensuring a market rate of return on equity.¹⁰
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The Tribunal set aside the AER's Decision and directed the AER to make the decision again adopting a value for gamma of 0.25.¹¹

The above findings of the Tribunal are consistent with and endorse the gamma proposal put by us in our response to the AER's Preliminary Determination. We consider that the Tribunal's decisions reflect the correct approach to the estimate of gamma and submit that the AER should apply a gamma of 0.25 in its 2016 to 2020 Final Decision.

Yours sincerely



Andrew Schille

General Manager
Regulation and Corporate Affairs

⁴ At [1048].

⁵ At [1093].

⁶ At [1095].

⁷ At [1095].

⁸ At [1096].

⁹ At [1105].

¹⁰ At [1108].

¹¹ Order 1(c) of the Tribunal's orders in *Ausgrid*.