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Mr Chris Pattas
General Manager Networks
Australian Energy Regulator
Level 35, 360 Elizabeth Street
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Email: AERInquiry@aer.gov.au

Dear Mr Pattas

United Energy's Revised Regulatory Proposal – 2016 to 2020

1. Introduction

We welcome the opportunity to respond to the issues raised in submissions on the Australian Energy Regulator's (**AER**) Preliminary Decision for our 2016 to 2020 regulatory control period.

We would like to thank stakeholders who have made written submissions on our Regulatory Proposal and the AER's Preliminary Decision. These submissions add to our own extensive consultation and are an important input for the AER in making a fully informed Final Decision.

This letter sets our response to issues raised in submissions from:

- The Victorian Government; and
- The Victorian Energy Consumer and User Alliance (**VECUA**).

Our response to each of these matters is set out below.

This letter also provides an update to our 2016 to 2020 Guaranteed Service Level (**GSL**) expenditure forecast arising from the Essential Services Commission of Victoria (**ESCV**) "Review of the Victorian Electricity Distributors' Guaranteed Service Level Payment scheme Final Decision".

We confirm the values and approach (i.e. the immediate transition) of our 2016 debt averaging period based on the latest RBA data. At the time of submitting our Revised Regulatory Proposal, RBA data for December 2015 was not available. Please find attached an updated Esquant report which sets out their analysis of the return of debt calculation for our averaging period. This analysis validates the values we submitted as part of our Revised Regulatory Proposal and is used as an input into various scenarios including the immediate transition.

2. Our response to the Victorian Government's Submission

The Victorian Government's submission of 8 January comments on a range of key issues to be considered by the AER in making its 2016 to 2020 Final Decision including:

- AMI benefits;
- Customer contributions for new connections;
- Vegetation management;
- Service Target Performance Incentive Scheme (**STPIS**) targets; and

- Future regulatory obligations.

Each of these matters is addressed below.

2.1. AMI benefits

In relation to AMI benefits, we are pleased to highlight that we are already delivering many network benefits to our customers and these efficiencies are reflected in our 2014 base year expenditure (which has also been adjusted to remove any once-off costs). These network benefits are set out in section 6.4 of our Regulatory Proposal and are summarised below:

- Customers have better access to energy consumption data and a broader range of pricing options
- Delivering Alternative Control Services at lower cost;
- Managing the network smarter and safer by:
    - Detecting hazardous 'Loss of Neutral' faults remotely;
    - Undertaking remote neutral integrity testing;
    - Enhancing our monitoring of supply to life-support customers during storm events;
    - Identifying faults remotely, to avoid wasted truck visits and restore supply more quickly;
    - Better assessment of damage claims;
    - More efficient use of existing capacity and greater use of spare capacity;
    - Improving network utilisation on peak demand days; and
    - Improving our identification of electricity and meter theft.

Where possible, we will continue to realise further benefits and the associated efficiencies will be shared with our customers through the AER's Efficiency Benefit Sharing Scheme (**EBSS**) as they are realised. Under the incentive framework, removing efficiency savings before they are realised would undermine the EBSS carryover mechanism which is designed to incentivise us to continually minimise our opex and share efficiency savings with customers as they are realised.

We further highlight that the benefits and associated savings set out in the 2011 Deloitte Report are outdated. Since 2011, there has been significant changes in the nature of network benefits that can be expected as the industry's understanding of the smart metering functionality and performance levels required to access them has evolved. We encourage the Victorian Government to have regard to these more recent reports.

2.2. Customer contributions for new connections

We support the introduction of the national AER Customer Contributions Guidelines to replace the Essential Services Commission's Guideline 14. This would remove the anomalous and unintended outcome arising under Guideline 14 which requires that we assume that the X factor in the final year of the current Distribution Determination will apply over a 15 to 30 year period (depending on the customer type).

In the 2011 to 2015 regulatory period, the application of Guideline 14 required us to apply the AER's approved X factor for 2015 of -8.1 per cent per annum to our calculations of incremental revenue. This meant that after 2015 we effectively assumed that distribution tariffs would increase in real terms at a rate of 8.1 per cent per annum for more than 25 years in the case of domestic customers. This resulted in us receiving about $80 million less in customer contributions over the 2011 to 2015 regulatory period.

The AER's national Customer Contributions Guidelines provides that the X-factor used to calculate the incremental revenue beyond the current regulatory control period will be zero (i.e. a flat real price path), thereby removing the anomalous outcome under Guideline 14.

We welcome the Victorian Governments commitment that Chapter 5A and the AER Customer Contributions Guidelines will apply from mid-2017, but note that the AER should adopt and X factor of zero for the purposes of our customer contributions in its 2016 to 2020 Final Decision.

2.3. Vegetation management

As part of our Revised Regulatory Proposal, we revised our forecast for complying with the new *Electricity Safety (Electric Line Clearance) Regulations 2015* (2015 ELC Regulations) which were finalised on 28 June 2015. Our revised forecast takes into account ESV's Guidance Information issued on 27 November 2015.

We have based our revised forecast of $11.7 million on a detailed cost build up having regard for the changes in the 2015 ELC Regulations. This takes into account any savings arising from the removal of any regulations or the introduction of less onerous obligation.

We also note that our indicative cost of complying with the exposure draft ELC Regulations was $111 million over the 2016 to 2020 period – not between "$4.2- $8.2" as suggested by the Victorian Government[1]. We raised our concerns with the exposure draft of the Regulations, noting that a more practical and cost effective approach should have been adopted – this is set out in our letter to ESV dated 12 January 2015.

2.4. STPIS targets

The Victorian Government submitted that:

> *The AER has accepted a couple of expenditure proposals that would be expected to result in a material improvement in supply reliability, but has not made any modifications to the DNSP's performance targets for the 2016-20 regulatory control period.*

We agree that an adjustment should be made to align performance targets with expenditure allowances where the AER's allowance results in a misalignment between the STPIS targets and expenditure allowances. In our Regulatory Proposal we proposed that should the AER not accept our proposed Value of Customer Reliability (VCR) then the AER should relax (i.e. make higher) our targets. Our Revised Regulatory Proposal provides that if the AER does not retain its Preliminary Decision on our Augmentation capex, VCR and demand forecast, then it should relax (i.e. make higher) our targets STPIS targets recognising the impact of lower capex allowance. Similarly, should the AER not accept our Repex forecast then it should relax our targets.

2.5. Future Regulatory Obligations

We do not support the Victorian Government's approach to developing regulations to determine whether and where in their networks (i.e. specific points in the network) distribution network service providers (**DNSPs**) must install REFCLs[2]. This approach is not consistent with the National Electricity Rules (**Rules**) which are based on a proposed-respond model, whereby DNSPs identify and justify their investment requirements based on their own assessment of the investment required to meet the Rules' capex and opex objectives as well as their safety, reliability and other legislative and regulatory obligations.

The Victorian Government's approach is also not consistent with the AER's approach to determining a DNSP's expenditure allowance. The AER reviews the expenditure forecasts proposed by DNSPs and determines a capex and opex allowance which ensures the DNSP has:

> *"a reasonable opportunity to recover at least the efficient costs it incurs in providing direct control network services and complying with its regulatory obligations and requirements*".

[1] The cost referred to in the Jaguar Consulting RIS, September 2014, page 6 we not DNSP costs but rather MEC costs.

[2] Acil Allen Consulting, Report to Department of Economic Development, Jobs, Transport and Resources, Regulatory Impact Statement Bushfire Mitigation Regulations Amendment, 17 November 2015

Our 2016-2020 Repex forecast in our Revised Regulatory Proposal includes expenditure for undertaking two REFCLs as this investment will reduce our overall bushfire risk by 35 per cent at a cost commensurate with the value of the risk reduction Bushfire Mitigation ALARP Risk Assessment.

We understand that ESV has been engaging with you on this matter and has expressed its support for this investment.

3. Our response to the VECUA submission

VECUA sets out a number of concerns with the rate of return proposal in our Regulatory Proposal as well as our supporting submissions. Our Revised Regulatory Proposal provides a comprehensive response to the AER's Preliminary Decision, which addresses each of the issues raised by VECUA.

In particular:

- In response to concerns regarding the multi-model approach, we have put forward an alternative approach to estimating the return on equity which relies on the Sharpe Lintner Capital Asset Pricing Model (SL CAPM) alone but with appropriate adjustments to account for known weaknesses in this model; and
- We have also revised our approach to estimating the return on debt, adopting a simpler approach of transitioning immediately to the trailing average method.

We consider that each of the concerns previously expressed by the AER and stakeholders have now been addressed in our Revised Regulatory Proposal and supporting documents submitted on 6 January 2016.

3.1. VECUA's submissions on the AER's WACC determination approach

(a) Insufficient consideration of market data and other evidence

We agree with VECUA that the AER has had insufficient regard to market evidence in determining the rate of return. However we do not agree with VECUA's submission that a proper consideration of available market data and other evidence would support a lower rate of return than that determined by the AER. On the contrary, as noted in our Revised Regulatory Proposal:[3]

- The AER's estimate of the return on equity is below any comparable recent estimate from market practitioners, including estimates from the AER's review of recent broker reports and independent expert reports; and
- The AER's estimate of the return on equity is below that indicated by current market prices for traded equities and the AER's market-wide dividend growth model (**DGM**) analysis.

This outcome is due to the AER mechanistically applying the foundation model approach developed in the Rate of Return Guidelines, without any meaningful consideration of whether such an approach leads to an estimate of the return on equity that is consistent with the allowed rate of return objective and commensurate with prevailing market conditions.

More specifically, this is the result of the AER:

- Relying solely on the output of a model that is known to produce biased estimates, without properly correcting for that bias;
- Applying this model in a way that does not reflect market practice and which results in the return on equity simply tracking movements in the risk-free rate; and
- Making errors in the interpretation of key evidence.

[3] UE, Response to AER Preliminary Determination, Rate of return and gamma, 6 January 2016, pp 38-40.

Further evidence provided with this submission reinforces these points. Evidence from investors indicates that the AER's proposed return on equity of 7.3% is not too high, as suggested by the VECUA submission, but rather it is too low.

A submission made by listed infrastructure fund Spark Infrastructure in relation to the AER's April 2015 preliminary determination for SA Power Networks explains that:

- The regulatory returns resulting from the AER's implementation of the SL CAPM using short term base rates and long run average market risk premium are well below the prevailing market rates;[4]
- The AER's approach of combining short term base rates and long run average market risk premium in the SL CAPM is inconsistent with market practice in relation to estimation of hurdle rates for investment;[5] and
- The returns allowed in the AER's latest determinations are not sufficient to attract equity investment when compared to competing investment opportunities.[6]

Spark's view has been informed by feedback from a broad range of pension funds and other ultimate suppliers of investment funds. Their feedback to Spark was universally that the regulatory returns currently expected for the next regulatory periods are inadequate to sustain long run decisions to invest in the sector.[7]

The statements made by Spark Infrastructure in its submission in relation to the AER's April 2015 determinations remain apposite in this case. In the AER's Preliminary Decision for UE, it has applied the same method for estimating the return on equity as it applied in the April 2015 determinations, and the resulting return on equity estimate is very similar (7.3% compared to 7.1%).

(b) The AER's focus on our proposal

We do not agree that the AER has "inappropriately" focused on the rate of return proposals put forward by the Victorian businesses.

Similar to the other Victorian businesses we have provided cogent evidence as to the required return of equity and return on debt for the forthcoming regulatory period. It is entirely appropriate (and required under the NER) for the AER to have proper regard to this evidence.

We considers that in fact the AER has not sufficiently had regard to all of the evidence it has submitted to date. In particular, the AER does not appear to take into account the estimates of the return on equity provided by Frontier Economics using the Black CAPM, the Fama French Model and DGM. Rather, the AER has solely relied on its implementation of the SL CAPM to determine the return on equity.

(c) Implications of the recent TransGrid sale

VECUA submits that the outcome of the recent TransGrid sale process "makes a mockery" of claims made by network service providers regarding the required return on equity.[8] VECUA appears to consider that the fact that the agreed sale price for TransGrid exceeds its regulated asset base (**RAB**) value indicates that the return on equity allowed by the AER for TransGrid (7.1%) is at least sufficient for it to meet efficient financing costs and attract equity investment.

This issue is addressed in the Frontier Economics report provided with this submission.[9]

Frontier Economics conclude that the fact that the TransGrid sale price exceeded the RAB value does not constitute any evidence of the adequacy of the AER's allowed return on equity of 7.1% for the remaining four years of the current regulatory period. The reasons for this conclusion include:[10]

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[4] Spark Infrastructure, *Appropriate rate of return for electricity distribution businesses*, 3 July 2015, p 2.
[5] Spark Infrastructure, *Appropriate rate of return for electricity distribution businesses*, 3 July 2015, p 4.
[6] Spark Infrastructure, *Appropriate rate of return for electricity distribution businesses*, 3 July 2015, p 5.
[7] Spark Infrastructure, *Appropriate rate of return for electricity distribution businesses*, 3 July 2015, p 2.
[8] VECUA submission, p 14.
[9] Frontier Economics, *Response to submissions on the relevance of the TransGrid sale*, January 2016.
[10] Frontier Economics, *Response to submissions on the relevance of the TransGrid sale*, January 2016, pp 4-5.

- The sale price reflects not only the allowed return on equity of 7.1% for the next four years, but also a range of other factors, including:
    - Expected cash flows over the full 99-year lease period;
    - The extent to which the acquirer considers that it may be able to outperform regulatory benchmarks under incentive-based regulation or be eligible to receive incentive payments (e.g. its expected ability to achieve operating efficiencies);
    - The acquirer's assessment of the value attributed to non-regulated assets owned by TransGrid;
    - The potential for future growth in the earnings of the firm over the 99-year lease period, arising from: the expansion of existing non-regulated activities; the development of new non-regulated activities; and/or increasing the scale and/or efficiency of regulated activities;
    - Any synergies with the acquirer's existing business;
    - Any diversification benefits available to the acquirer;
    - Any strategic value to the acquirer (e.g. value in seeking to establish an operation in a new market or reach an efficient scale in a market where it already has some interests); and
- Since controlling interests are purchased at a material premium to ordinary equity, the prices paid for controlling interests cannot be used to infer anything about the required return on ordinary equity – even aside from the other reasons set out above.

Frontier also notes that the return on equity allowance of 7.1% recently determined by the AER for TransGrid only applies for four years of the 99-year lease period, and that beyond this four-year period it may reasonably be assumed that allowed returns would return to more acceptable levels. This could occur either as a result of a change in the AER's methodology (e.g. following a rule change or Tribunal ruling against the current AER method) or continuation of the AER's current methodology in different market conditions (i.e. with a higher risk-free rate, leading to a higher return on equity under the AER's method).

The TransGrid equity investment prospectus published by Spark Infrastructure (referred to in the VECUA submission) confirms the above analysis. This prospectus does not indicate that the regulated return on equity allowed for TransGrid for the next four years is a driver of the agreed sale price or of the acquirer's perception of the value of TransGrid – the only comment that is made about this is that "TransGrid's current regulatory determination applies for 4 years only (to 30 June 2018) and was not appealed by its previous owners".[11] Rather, the prospectus identifies other areas of value in the TransGrid business as including:[12]

- Strategic benefits for Spark in increasing diversity of cashflow sources, thereby reducing overall portfolio risk;
- Scope to increase efficiency through better asset utilisation and process improvements;
- Scope for long term growth in regulated activities (and hence RAB growth), supported by macro-economic driven demand growth expectations, and change in generation mix to renewables;
- Spark's ability to leverage TransGrid's assets and apply its own expertise to develop and grow non-regulated business opportunities. The prospectus notes in particular some scope to grow a telecommunications service offering that leverages TransGrid's market positioning across NSW.

Therefore, consistent with previous conclusions of the AER[13] and its experts[14], we considers that nothing can be inferred from the outcome of the TransGrid sale process, as to the adequacy or otherwise of the regulated return on equity for TransGrid or any other business.

[11] Spark Infrastructure, *Equity Investment in TransGrid and Equity Raising*, 25 November 2015, p 26.
[12] Spark Infrastructure, *Equity Investment in TransGrid and Equity Raising*, 25 November 2015, pp 9-10.
[13] AER, *Rate of Return Guideline Explanatory Statement*, December 2013, p 48.
[14] McKenzie and Partington, *Equity market risk premium*, December 2011, p 34.

3.2. VECUA's submissions on the AER's WACC determinations

(a) Relevance of asset indexation to the AER's return on equity determination

VECUA argues that the AER has failed to consider the impact of asset indexation in its return on equity determinations. It is said that the AER's calculation of its return on equity allowances does not reflect the reality that networks apply annual asset indexation to their regulatory asset bases (**RABs**).

This is not correct. The method adopted by the AER for determining annual revenue requirements does take into account the fact that, under the NER, the RAB must be indexed each year for inflation[15] and a nominal rate of return must be applied to this indexed RAB value to determine the return on capital allowance.[16] This is accounted for by making an adjustment to the annual revenue requirement calculation for each year for indexation of the regulatory asset base, as required by the NER.[17] The adjustment that is made to the annual revenue requirement is a negative adjustment equal to the amount by which the RAB is indexed for inflation in that year.[18]

Therefore, no further adjustment to the method for dealing with inflation is required, nor would any further adjustment be permitted under the NER. As explained above, the NER clearly prescribe how inflation is to be accounted for in determining the rate of return (i.e. the rate of return is to be determined on a nominal basis), rolling forward the RAB (the RAB is to be adjusted for inflation in each year) and determining revenue requirements (the annual revenue requirement is to include a negative adjustment for indexation of the regulatory asset base).

As discussed in our Revised Regulatory Proposal, this gives rise to important interrelationships between the method for forecasting inflation and other aspects of the AER's determination, particularly its determination of the allowed rate of return. Given these interrelationships, it is important that the forecast of inflation be as accurate as possible, and consistent with the implied forecast of inflation in the nominal rate of return. This issue is discussed further in our Revised Regulatory Proposal January submission.[19]

(b) Estimation of the return on equity

VECUA argues that the AER has over-estimated the return on equity, by applying a market risk premium (**MRP**) and equity beta in the SL CAPM that are too high. VECUA argues that both the MRP and equity beta should be set to the bottom of the AER's ranges for those parameters (i.e. 5% and 0.4 respectively).

VECUA's submissions on the return on equity rest on the following contentions:

- That it is appropriate to use the SL CAPM alone to estimate the return on equity, with no adjustment for any of the known weaknesses in this model;
- Best estimates of the MRP and equity beta are 5% and 0.4 respectively; and
- Using an MRP of 5% and equity beta of 0.4 in the SL CAPM will lead to a reasonable estimate of the return on equity, and one that contributes to the achievement of the allowed rate of return objective.

For reasons set out in our Revised Regulatory Proposal, the evidence before the AER does not support the first contention. The empirical evidence points to shortcomings in the design of the SL CAPM which mean that it will underestimate the required return on equity for businesses with a beta below one and businesses with high book-to-market ratios.[20]

VECUA's submission as to the best estimates of the equity beta and MRP are also not supported by the evidence before the AER. No expert (including the AER's expert) concludes that the best empirical estimate of the equity beta is 0.4[21]; rather, the expert evidence supports an SL CAPM equity beta of 0.82 (before any adjustment to

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[15] NER cl 6.5.1; S6.2.3(c)(4).
[16] NER, cl 6.5.2(d)(2).
[17] NER, cl 6.4.3(a)(1).
[18] NER, cl 6.4.3(b)(1).
[19] UE Response to AER Preliminary Determination - Rate of return and gamma, 6 January 2016, pp 106-107
[20] Refer to: UE Response to AER Preliminary Determination - Rate of return and gamma, 6 January 2016, section 4.3.
[21] VECUA refers to "Professor Henry's estimate of 0.4". Professor Henry did not recommend an estimate of 0.4. Rather, Professor Henry recommended a range of 0.3 – 0.8, based in the limited sample of domestic businesses that he was instructed to use (Olan T Henry, *Estimating β: An update*, April 2014, p 63).

account for biases in this model).[22] Similarly, the expert evidence before the AER does not support an MRP of 5%, but rather supports a much higher estimate of the prevailing MRP (Frontier Economics recommend an estimate of 7.9%[23]).

Finally, VECUA's submissions do not include any consideration of whether the return on equity and overall rate of return that would result from its proposed approach is reasonable and consistent with the allowed rate of return objective. If VECUA's proposal were to be implemented, this would deliver an equity risk premium (**ERP**) of just 2% and a return on equity of approximately 4.8%. This is significantly below the ERP and return on equity ranges indicated by the reasonableness checks (or "cross-checks") referred to by the AER in the Preliminary Decision.[24] VECUA's submission would also imply a return on equity that is significantly below the prevailing return on debt.

The relevant evidence in relation to each of these issues is addressed in detail in our Revised Regulatory Proposal.

(c) Return on debt

VECUA raises two issues in relation to estimation of the return on debt:

- VECUA claims that, by using broad BBB data series for estimation of the return on debt, the AER has provided significantly higher cost of debt allowances than appropriate; and
- VECUA argues that the AER should benchmark businesses' actual debt costs to inform its return on debt allowances.

The first of these issues was addressed in our Revised Regulatory Proposal. For reasons explained in that submission, continuing to use a broad BBB band data series to estimate the return on debt will not lead to an allowance that is 'too high'. Rather, given that the evidence supports a credit rating of BBB to BBB+, using a broad BBB band data series is entirely appropriate.[25]

In relation to the second issue, we consider that it would not be appropriate, and not consistent with the NER and NGL, for the return on debt allowance to be based on businesses' actual debt costs. Such an approach would be inconsistent with:

- The allowed rate of return objective, which requires the rate of return to be commensurate with the efficient financing costs of a benchmark efficient entity (not the actual financing costs of the regulated business);[26]
- The revenue and pricing principles, which provide for recovery of at least the efficient costs incurred in the provision of direct control network services (not actual costs) and the provision of effective incentives to promote economic efficiency;[27]
- The national electricity objective, which is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers;[28] and
- The principles of incentive-based regulation, including that service providers should be compensated for the efficient costs of service delivery (not actual costs), so that at least some of the rewards or penalties associated with over- or under-performance against the efficient cost benchmark flow to the service provider.

As has been recognised by policy-makers and the AER on numerous occasions, in order to promote efficient investment in, and efficient operation and use of, regulated services, businesses should be compensated for the

[22] Frontier Economics, *Estimating the equity beta for the benchmark efficient entity*, January 2016. See also: UE Response to AER Preliminary Determination - Rate of return and gamma, 6 January 2016, section 4(c).
[23] Frontier Economics, *The required return on equity under a foundation model approach*, January 2016, Table 5. See also: UE Response to AER Preliminary Determination - Rate of return and gamma, 6 January 2016, section 4.4(b)
[24] For an analysis of these cross-checks, refer to: UE Response to AER Preliminary Determination - Rate of return and gamma, 6 January 2016, 6, section 3.5.
[25] UE Response to AER Preliminary Determination - Rate of return and gamma, 6 January 2016, pp 33-35
[26] NER, cl 6.5.2(c).
[27] NEL, s 7A.
[28] NEL, s 7.

efficient cost that would be incurred by the relevant benchmark efficient entity. Setting regulated allowances based on actual costs potentially provides businesses with a perverse incentive to inflate their actual costs.

This was explained by the AEMC is its final rule determination accompanying the November 2012 changes to the rate of return rules. The AEMC stated (referring to statements in its draft rule determination which were affirmed in the final determination):[29]

> *"The draft rule determination stated that the primary objective of the allowed rate of return is to provide service providers with a return on capital that reflects efficient financing costs. A rate of return that reflects efficient financing costs will allow a service provider to attract the necessary investment capital to maintain a reliable energy supply while minimising the cost to consumers. The Commission also stated that it is important for recovery of financing costs to be based on benchmark efficient finance costs. This is to provide incentives for firms to adopt efficient financing arrangements and to protect consumers from the effects of inefficient ones."*

Specifically in relation to the return on debt, the AEMC stated:[30]

> *The return on debt allowance must still be estimated in a manner consistent with the overall rate of return objective. That is, it must be a benchmark cost of debt for an efficient firm. It should not be misinterpreted as suggesting that it must reflect a service provider's actual cost of debt.*

It is our understanding that the AER does not intend to depart from long-standing regulatory practice in this respect, including for the reasons set out above. However if the AER was to change its practice and seek to rely on any information on actual debt costs in determining the return on debt allowance in the final decision, we would need to be provided with a reasonable opportunity to respond. [31]

4. Guaranteed Service Level Payments

Table 6-2 of our Revised Regulatory Proposal set out the impact on our GSL expenditure forecast arising from the ESCV "Review of the Victorian Electricity Distributors' Guaranteed Service Level Payment scheme Final Decision" (GSL Final Decision) other than for "Individual duration of interruptions".

As the GSL Final Decision was published on 23 December, we had limited time to assess its impact on our 2016 to 2020 GSL expenditure forecast. The information required to assess the cost impact of the introduction of payments for "Individual duration of interruptions" was not available in time for inclusion in our Revised Regulatory Proposal.

We have now updated Table 6-2, represented below, to include the forecast costs for "Individual duration of interruptions".

Table 6-1: Increases arising from ($'000s, Real 2015)

	RRP	4th Feb
2014 Base Year GSL Opex	1,123.9	1,123.9
Increases for changes to GSL scheme:		
– New Connections 1-4 day delay	8.0	8.0
– New Connections - 5+ day delay	4.0	4.0
– Individual unplanned	n/a	188.4

[29] AEMC, *Rule Determination: National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012; National Gas Amendment (Price and Revenue Regulation of Gas Services) Rule 2012*, 29 November 2012, p 43. The AEMC affirms that this statement remains apposite in respect of the final rule at pages 65 and 67.
[30] AEMC, *Rule Determination: National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012; National Gas Amendment (Price and Revenue Regulation of Gas Services) Rule 2012*, 29 November 2012, p 86.
[31] NEL, 16(1)(b).

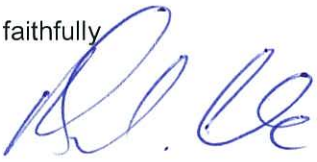
– Annual Duration of Unplanned Interruptions - 20 hours	7.0	7.0
– Annual Duration of Unplanned Interruptions - 30 hours	103.0	103.0
– Annual Duration of Unplanned Interruptions - 60 hours	108.0	108.0
– Low reliability payments - 10 events (>8 events)	8.0	8.0
– Low reliability payments - 15 events (>12 event)	28.0	28.0
– Low reliability payments - 30 events (>24 event)	22.0	22.0
– Annual Frequency of Momentary Interruptions - 24	-	-
– Annual Frequency of Momentary Interruptions - 36	-	-
– Street lights not repaired in 2 days	-	-
– New Connections 1-4 day delay	1.0	1.0
Total Scheme Changes	**289.0**	**477.4**
Revised Total GSL Opex per annum	**1,412.9**	**1,601.3**

5. Closing

We are committed to open and ongoing engagement with the AER and our other stakeholders as they consider our Revised Regulatory Proposal and the AER makes its Final Determination.

Should you have any questions, please contact Stephanie McDougall, Price Review Manager, on (03) 8846 9538 or Stephanie.McDougall@ue.com.au.

Yours faithfully



Andrew Schille
General Manager – Regulatory and Corporate Affairs