



Australian Energy Market Commission

DRAFT RULE DETERMINATION

National Electricity Amendment (Assumed utilisation of imputation credits) Rule 2012

Rule Proponent(s)

ElectraNet
SP AusNet

Commissioners

Pierce
Henderson
Spalding

28 June 2012

JOHN PIERCE

Chairman

For and on behalf of the Australian Energy Market Commission

**RULE
CHANGE**

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About the AEMC

The Council of Australian Governments, through its Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005. The AEMC has two principal functions. We make and amend the national electricity and gas rules, and we conduct independent reviews of the energy markets for the MCE.

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Summary of draft rule determination

The Australian Energy Market Commission (AEMC or Commission) has determined not to make a draft rule in response to the consolidated rule change request on the assumed utilisation of imputation credits applying to transmission network service providers (TNSPs).

This draft rule determination outlines why the Commission considers that the consolidated rule change request is unlikely to contribute to achievement of the National Electricity Objective.

Consolidated rule change request

On 18 November 2011, SP AusNet submitted a rule change request relating to the value of the assumed utilisation of imputation credits (gamma) applying to TNSPs under chapter 6A of the National Electricity Rules (NER). On 30 November 2011, ElectraNet submitted a rule change request to the AEMC on the same matter.

The SP AusNet and ElectraNet consolidated rule change request consisted of amendments to clause 6A.6.4 of the NER regarding a change to the value of gamma (proposed rules). The effect of the proposed rules would be to change the value of gamma from 0.65, the current value prescribed in the 2009 review of the rate of return elements, to 0.25.

The Commission assessed the consolidated rule change request on a transitional basis, that is, whether the value of gamma should be amended from 0.65 to 0.25 for the forthcoming revenue determinations for SP AusNet and ElectraNet. The broader amendments proposed as part of the consolidated rule change request regarding the impact of merits review decisions on the rate of return framework more generally are being considered as part of the AER initiated rule change requests on network regulation [ERC0134].

The Commission's draft rule determination

The Commission has acknowledged that the current rate of return framework for TNSPs does not provide sufficient flexibility to adapt to changing circumstances.¹

The Commission is not however, satisfied that the proposed rules providing for a revised gamma of 0.25 to apply to the next revenue determination for SP AusNet and ElectraNet will, or are likely to, contribute to the achievement of the NEO because:

- the framework for calculating the rate of return for transmission businesses is codified in chapter 6A of the NER. The chapter 6A framework requires that all elements of the rate of return (including gamma) be considered as part of a single periodic review. The rate of return is set for five years. Permitting gamma or any

¹ AEMC 2012, *Economic Regulation of Network Service Providers, and Price and Revenue Regulation of Gas Services*, Directions Paper, 2 March 2012, Sydney.

other individual rate of return element to be amended on an ad hoc basis outside of that framework would undermine the integrity of the current rate of return framework and create regulatory uncertainty, thereby resulting in an increase in the regulatory risks faced by network businesses;

- varying the value of gamma as proposed by SP AusNet and ElectraNet in the absence of analysing the cross-linkages between gamma and the other parameters could result in an underlying change in the incentive arrangements for the network businesses that would not be in the long-term interests of consumers; and
- it is neither appropriate nor efficient for the AEMC to conduct a review of the appropriate value of gamma or any other parameter, as this review is more appropriately carried out by the AER.

Consultation on the draft rule determination

The Commission invites submissions on this draft rule determination by 10 August 2012.

Any person or body may request that the Commission hold a hearing in relation to the draft rule determination. Any request for a hearing must be made in writing and must be received by the Commission no later than 5 July 2012.

Submissions and requests for a hearing should quote project number “ERC0143” and may be lodged online on the Commission's homepage.

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1 SP AusNet and ElectraNet's rule change requests

1.1 The consolidated rule change request

On 18 November 2011, SP AusNet submitted a rule change request relating to the value of the assumed utilisation of imputation credits applying to transmission network service providers (TNSPs) under chapter 6A of the National Electricity Rules (NER). On 30 November 2011, ElectraNet submitted a rule change request to the AEMC on the same matter. These rule change requests have been consolidated and are being treated as one request (consolidated rule change request).

1.2 Relevant background

The consolidated rule change request concerns the value of gamma (γ), which is related to the value of assumed utilisation of imputation credits applying to TNSPs. Prior to explaining the rationale behind the consolidated rule change request, this section briefly explains gamma concept.

1.2.1 Gamma

In chapter 6A of the NER, the weighted average costs of capital (WACC) is an estimate of the fair rate of return on capital that investors (including both debt and equity holders) in the benchmark firm might reasonably expect as having their capital at risk.

Under chapter 6A, the Australian Energy Regulator (AER) must conduct a review of the WACC parameters every five years. For some parameters, the specific values adopted in that review cannot be departed from in determinations over the subsequent five year period. These parameters include equity beta, market risk premium, gearing, credit rating, and gamma; the last of which is the subject of this rule change request. The last review was carried out in 2009 and the next is scheduled for 2014. The parameters from the last review will apply to the forthcoming revenue determinations for SP AusNet and ElectraNet.

The estimated cost of corporate income tax is usually considered in conjunction with WACC parameters. It is important because the investors' return on capital must be after corporate tax. For this reason, the estimated cost of corporate income tax is added to a TNSP's revenue requirements.

Gamma is relevant to the estimated cost of corporate income tax. It represents the value of imputation credits and has an effect on the "grossing up" of a TNSP's revenue requirements for corporate income tax.

Where the value of imputation credits or gamma is higher, the estimate of corporate income tax that is added to a TNSP's revenue requirement will be lower because individual investors can offset more of their individual tax liability with the imputation credits. Where the value of imputation credits is lower, the estimate of corporate

income tax that is added to a TNSP's revenue requirement will be higher as investors will require a higher return to cover their tax liability from income earned from their investment in that TNSP.

In summary, the value of gamma has the following impact on the building block revenue and prices:

- a decrease in gamma increases the building block revenue and prices; and
- an increase in gamma decreases the building block revenue and prices.

1.2.2 Merits review

Under chapter 6 of the NER, the AER can consider persuasive evidence from distribution network service providers (DNSPs) to depart from the outcomes of the periodic WACC review. This decision is also subject to merits review.

The value of gamma has been subject to merits review by a number of DNSPs, namely ENERGEX, Ergon Energy and ETSA Utilities. As a result of that merits review in the electricity distribution context, the Australian Competition Tribunal (the Tribunal) determined that the correct value of gamma for electricity distribution network service providers is 0.25, as opposed to 0.65 (the value also determined by the AER in its 2009 WACC review for TNSPs).

Since the merits review of gamma, the AER has adopted the revised value of 0.25 in electricity distribution (and gas). The NER do not, however, permit the AER to consider applying the revised gamma to any TNSP revenue determination until the next scheduled review of the rate of return parameters (scheduled for 2014). Clause 6A.6.4(f) provides:

“If, as a consequence of a review, the AER decides to adopt a revised value or methodology, it must use that revised value or methodology, but only for the purposes of a Revenue Proposal that is submitted to the AER under clause 6A.10.1(a) after completion of the first review or after completion of the five yearly reviews (as the case may be).”

This means that even if the AER considers that the gamma value determined by the Tribunal in the context of DNSPs is the correct value that should be applied for all network service providers, the AER must continue to apply the gamma value that it fixed in its 2009 review for electricity transmission.

1.3 Rationale for the rule change request

The problems raised in the consolidated rule change request are summarised as follows:

- the rules for TNSPs differ from those that apply to electricity distributors and gas networks, where the gamma is not 'locked in'. It is anomalous that the current

NER require a known “error” in the proponents view in relation to gamma to be perpetuated in future transmission revenue determinations until March 2014. The anomaly is exacerbated because it is confined to TNSPs while determinations for other energy networks will be able to adopt the correct gamma value.²

- future transmission determinations for TNSPs would otherwise be subject to a gamma value that is known to be erroneous in the view of the proponent.³ That is, any revision of gamma in the AER's next review of the WACC and tax parameters will only apply to revenue proposals submitted after the completion of that review. This means that in the absence of any rule change, a value for gamma of 0.65 must apply to transmission determinations for South Australia (ElectraNet - 1 July 2013 to 30 June 2018), Victoria (SP AusNet - 1 April 2014 to 31 March 2019), and possibly NSW (Transgrid - 1 July 2014 to 30 June 2019) and Tasmania (Transend - 1 July 2014 to 30 June 2019);⁴ and
- a gamma of 0.65 if applied is inconsistent with the revenue and pricing principles in the NEL which state that a regulated network service provider should be provided with a reasonable opportunity to recover at least the efficient costs the operator incurs in providing direct control network services. Continuing to apply a value for gamma that is demonstrably too high will lead to an understatement of the cost of corporate income tax in TNSP's revenue allowances and will therefore prevent recovery of efficient costs.⁵

1.4 Solution proposed in the rule change request

The consolidated rule change request includes proposed rules. However, to enable SP AusNet and ElectraNet to use the Tribunal determined value of gamma in their forthcoming revenue proposals, two separate solutions are proposed (proposed rules):

- SP AusNet proposed an amendment to clause 6A.6.4(f) of the NER and the addition of a new clause 6A.6.4(g) that stated, “if the Tribunal determines that the AER’s most recent review of the matters referred to in clause 6A.6.4(d) resulted in an error or errors, and as a consequence of that determination, a different methodology or value is ascribed to the assumed utilisation of imputation credits, the AER must use that different methodology or value for the purposes of clause 6A.6.4(f)”.⁶
- On the other hand, ElectraNet proposed that clause 6A.6.4 be updated to deem the value for gamma as it has been determined by the Tribunal, subject to future periodic reviews of WACC and tax parameters. ElectraNet submitted that this simple amendment would maintain the original intent of the rules in respect of

2 SP AusNet rule change request, 18 November 2011, Attachment 2, p. 1.

3 ElectraNet rule change request, 30 November 2011, p. 6.

4 Ibid.

5 Id., p. 5.

6 SP AusNet rule change request, 18 November 2011, Attachment 2, p. 8.

the determination of tax and WACC parameters for TNSPs, while providing for correction of the value for gamma. In addition, ElectraNet proposed a one-off transitional rule under Chapter 11 of the rules. This amendment would have the effect of obliging the AER to apply a value for assumed utilisation of imputation credits of 0.25 in determining the estimated cost of corporate income tax referred to in clause 6A.6.4 for the South Australia transmission determination for the regulatory control period commencing 1 July 2013.⁷

1.5 Commencement of rule making process

On 22 March 2012, the Commission published a notice under section 95 of the National Electricity Law (NEL) advising of its intention to commence the rule making process and the first round of consultation in respect of the consolidated rule change request. A consultation paper prepared by AEMC staff identifying specific issues or questions for consultation was also published with the consolidated rule change request. Submissions closed on 19 April 2012.

The Commission received two submissions on the rule change request as part of the first round of consultation. They are available on the AEMC website.⁸

1.6 Consultation on draft rule determination

In accordance with the notice published under section 99 of the NEL, the Commission invites submissions on this draft rule determination by 10 August 2012.

In accordance with section 101(1a) of the NEL, any person or body may request that the Commission hold a hearing in relation to the draft rule determination. Any request for a hearing must be made in writing and must be received by the Commission no later than 5 July 2012.

Submissions and requests for a hearing should quote project number "ERC0143" and may be lodged online at www.aemc.gov.au or by mail to:

Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

⁷ ElectraNet rule change request, 30 November 2011, p. 10.

⁸ www.aemc.gov.au

2 Draft rule determination

2.1 Commission's draft determination

In accordance with section 99 of the NEL the Commission has made this draft rule determination in relation to the rules proposed by SP AusNet and ElectraNet.

The Commission has determined it should not make the proposed rules. The Commission's reasons for making this draft rule determination are set out in section 2.4.

2.2 Commission's considerations

In assessing the consolidated rule change request the Commission considered:

- the Commission's powers under the NEL to make the rule;
- the rule change requests;
- the fact that there is no relevant Ministerial Council on Energy (MCE) statement of policy principles;⁹
- submissions received during first round consultation;
- the Commission's analysis as to the ways in which the proposed rules will or are likely to, contribute to the National Electricity Objective (NEO)
- the revenue and pricing principles under section 7A of the NEL;
- the Commission's November 2008 determination relating to the parameter values, equity beta and gamma rule change request from the Energy Users Association of Australia;¹⁰ and
- the Australian Competition Tribunal May 2011 decision relating to gamma.¹¹

2.3 Commission's power to make the rule

The Commission is satisfied that the proposed rules fall within the subject matter about which the Commission may make rules. The proposed rule falls within section 34 of the NEL as it relates to sections 34(1)(a)(i), the operation of the national electricity market, and 34 (1)(a)(iii), the activities of persons (including Registered Participants)

⁹ Under section 33 of the NEL the AEMC must have regard to any relevant MCE statement of policy principles in making a rule.

¹⁰ AEMC 2008, *Final rule determination - Parameter values, equity beta and gamma*, Final rule determination, 13 November 2008.

¹¹ Application by Energex Limited (Gamma) (No 5) [2011] ACompT 9 (12 May 2011).

participating in the national electricity market or involved in the operation of the national electricity system.

Further, the proposed rule falls within the matters set out in schedule 1 to the NEL, as it relates to item 15 because the rule change request is about the regulation of revenues earned or that may be earned by owners, controllers or operators of transmission systems from the provision by them of services that are the subject of a transmission determination.

2.4 Rule making test

Under section 88(1) of the NEL the Commission may only make a rule if it is satisfied that the rule will, or is likely to, contribute to the achievement of the NEO. This is the decision making framework that the Commission must apply.

The NEO is set out in section 7 of the NEL as follows:

“The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to:

- (a) price, quality, safety, reliability and security of supply of electricity;
and
- (b) the reliability, safety and security of the national electricity system.”

For the consolidated rule change request, the Commission considers that the relevant aspect of the NEO is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to price.¹²

The Commission is not satisfied that the proposed rules providing for a revised gamma of 0.25 to apply to the next revenue determination for SP AusNet and ElectraNet will, or are likely to, contribute to the achievement of the NEO because:

- the framework for calculating the rate of return for transmission businesses is codified in chapter 6A of the NER. The chapter 6A framework requires that all elements of the rate of return (including gamma) be considered as part of a single periodic review. The rate of return is set for five years. Permitting gamma or any other individual rate of return element to be amended on an ad hoc basis outside of that framework would undermine the integrity of the current rate of return framework and create regulatory uncertainty, thereby resulting in an increase in the regulatory risks faced by network businesses;

¹² Under section 88(2), for the purposes of section 88(1) the AEMC may give such weight to any aspect of the NEO as it considers appropriate in all the circumstances, having regard to any relevant MCE Statement of Policy Principles.

- varying the value of gamma as proposed by SP AusNet and ElectraNet in the absence of analysing the cross-linkages between gamma and the other parameters could result in an underlying change in the incentive arrangements for the network businesses that may not be in the long-term interests of consumers. Without considering the other parameters, there is risk of over-recovery of costs to the detriment of consumers and the Commission could not conclude with any certainty that the overall rate of return would be improved; and
- the consolidated rule change request effectively requires the AEMC to review a decision of the AER. It is neither appropriate nor efficient for the AEMC to conduct a review of the appropriate value of gamma or any other parameter, as this review is more appropriately carried out by the AER as economic regulator.

Generally, the role of the AEMC is to assess and amend the frameworks applicable to market participants under the NER which, for the rate of return framework under chapter 6A of the NER, is currently being undertaken through the rule change requests initiated by the AER. The problem identified in the consolidated rule change request does not seek to amend these frameworks, but to substitute a single outcome of a review by the AER. The AEMC considers that substitution of a single AER decision is inconsistent with the NEO and undermines the overall framework.

2.5 Other requirements under the NEL

In applying the rule making test in section 88 of the NEL, the Commission has taken into account the revenue and pricing principles as required under section 88B of the NEL. The rule change request relates to the principles of providing a reasonable opportunity to recover efficient costs; effective incentives to promote efficiency, and to ensure that the prices should allow for a return commensurate with the regulatory and commercial risks involved in providing the service.

The revenue and pricing principles also state that regard should be had to providing network businesses with effective incentives in order to promote economic efficiency with respect to direct control network services the operator provides. Amending gamma in isolation, without analysing the possible cross-linkages between it and the other parameters, is unlikely to provide network businesses with the effective incentives required to promote economic efficiency.

3 Commission's assessment approach

This Chapter outlines the approach taken to assess the consolidated rule change request in accordance with the requirements set out in the NEL. This framework is the same as that used in the consultation paper.

The Commission has assessed the consolidated rule change request on a transitional basis. That is, the Commission has considered whether a revised gamma of 0.25 should be applied to the next revenue determinations for SP AusNet and ElectraNet. The Commission has not considered the broader issue of the Tribunal decisions on the rate of return more generally, as this is being considered as part of the AER's network regulation rule change requests.

In assessing any rule change request, the Commission must have regard to the extent to which the rule will, or is likely to, contribute to the achievement of the NEO. In making this assessment, weight may be given to any specific aspect of the NEO as appropriate.

The consolidated rule change request could potentially affect the ability of, and the efficient operation of, the incentives on SP AusNet and ElectraNet to invest in their network assets for their next regulatory control period. Generally, any change in the level of investment in networks is likely to impact the price, quality, reliability and security of supply of electricity.

The Commission has assessed whether the consolidated rule change request would better balance the need to attract sufficient investment in the networks with the need to ensure that prices for consumers are no more than necessary to provide an appropriate level of service.

In assessing the consolidated rule change request the following issues have been considered:

- recovery of efficient costs – would a revised gamma for distribution network services providers automatically be the appropriate gamma value for TNSPs? Would a revised gamma applying to SP AusNet and ElectraNet ensure that they are able to fully recover an efficient level of costs to encourage efficient investment in, and operation of, transmission networks for their next revenue determinations?
- investment incentives – would amending gamma for their next revenue determinations provide SP AusNet and ElectraNet with the required incentives necessary to undertake efficient investment in transmission networks?
- regulatory certainty and transparency – would a rule permitting the gamma to be revised for SP AusNet and ElectraNet's next revenue determination provide an appropriate amount of regulatory certainty and transparency to reduce ambiguity in the suitable value of gamma to apply? What impacts would this have on the current arrangements for other TNSPs?

It was also necessary to assess whether the proposed rule relating to the value of gamma to apply for the estimated cost of corporate income tax for the next revenue determinations for SP AusNet and ElectraNet, compared with the current arrangements, would meet the objectives and principles of the regulatory framework under chapter 6A of the rules, including:

- achieving a balance between the interests of TNSPs and end customers;
- having regard to the appropriate role of AER as economic regulator; and
- providing transparent and timely regulatory processes.

The proposed rules have been assessed against the relevant counterfactual arrangements, which in this case are the current provisions relating to gamma under the NER.

4 Amending gamma

4.1 Rule Proponent's view

SP AusNet stated that following appeals by electricity distributors ETSA Utilities, ENERGEX and Ergon Energy, the Tribunal found that the value of gamma determined by the AER reflected a number of errors in terms of approach and logic. For this reason, SP AusNet considered that the Tribunal decision renders clause 6A.6.4 anomalous because that clause requires in SP AusNet's opinion, the AER to continue to apply an erroneous value of gamma to future transmission revenue determinations.¹³

Similarly, ElectraNet stated its rule change request is intended to "amend clause 6A.6.4 of the NER to incorporate the value for gamma determined by the Tribunal and to add a corresponding transitional provision for the forthcoming revenue reset for South Australia".¹⁴ ElectraNet considered that its proposed NER amendment would provide transmission businesses with the same flexibility afforded other energy networks that are able to adopt the new value of gamma as it is not locked-in under the NER.¹⁵

Both SP AusNet and ElectraNet considered that their rule change request would not apply retrospectively, only applying to future transmission revenue determinations, where the revenue proposal is submitted prior to the completion of the AER's 2014 review of the WACC and tax parameters.

4.2 Stakeholder views

The Major Energy Users noted that "the development of the WACC parameters in 2009 reflected a balance of competing elements and therefore to change one parameter in isolation of an assessment of all other parameters has the potential to upset the balance between the competing elements".¹⁶ In its submission, the AER agreed with the Major Energy Users comments noting that "the Chapter 6A framework is operating as intended in that all parameters are to be considered as part of a single WACC review".¹⁷

In relation to assessing the consolidated rule change request on a transitional basis, the AER noted that "departing from the previous WACC review in respect of one discrete parameter does not provide any greater certainty that the objective of promoting investment in, and efficient use of, electricity services for the long term interests of consumers will be achieved".¹⁸ In its submission, the Major Energy Users agreed with the AER stating that it would be "neither equitable, nor in the interests of consumers

¹³ Ibid.

¹⁴ ElectraNet rule change request, 30 November 2011, p. 6.

¹⁵ Id., p. 1.

¹⁶ Major Energy Users submission on the consultation paper, April 2012, p. 2.

¹⁷ Australian Energy Regulator submission on the consultation paper, April 2012, p. 1.

¹⁸ Id., p. 2.

for action to be taken on one element of the WACC while not investigating the other elements".¹⁹

The Major Energy Users were of the view that "until there has been a decision on how and when WACC parameters are to be assessed, there should be no change to the current rules".²⁰

The AER also noted that it had "submitted a rule change to the AEMC that would increase the flexibility for the initiation of a periodic WACC review and the statutory review of the Limited Merits Review framework has been brought forward". The AER considered that together "these reviews are capable of addressing the issues raised by the rule change proponents for future regulatory decisions".²¹

The Major Energy Users considered that "if the current wide review of the network regulation rules changes the way the WACC parameters are set, then the new approach should apply immediately and not wait for the WACC parameter determination set for March 2014".²²

On another note, the Major Energy Users, in its submission was concerned that SP AusNet and ElectraNet appeared to suggest that "a Tribunal decision should be considered to have a higher standing than other decisions of the AER".²³ As it is the job of the Tribunal to "stand in the shoes of the regulator when reviewing AER decisions and the AER acts as a model litigant working with the Tribunal to identify the correct answer, a Tribunal decision does not possess a higher standing than those of the AER and should not be automatically used to change the NER".²⁴

4.3 Analysis and conclusion

4.3.1 Recovery of efficient costs and investment incentives

Applicability of Tribunal determined revised gamma to transmission businesses

SP AusNet and ElectraNet stated in their rule change requests that the Tribunal determined a revised value of gamma for a number of distribution businesses and this revised value should automatically be applied to transmission businesses. However, SP AusNet and ElectraNet provided no additional evidence to support the need for a revised value of gamma to apply to transmission businesses.

¹⁹ Major Energy Users submission on the consultation paper, April 2012, p. 2.

²⁰ Ibid.

²¹ Australian Energy Regulator submission on the consultation paper, April 2012, p. 1.

²² Major Energy Users submission on the consultation paper, April 2012, p. 3.

²³ Id., p. 2.

²⁴ Ibid.

The submissions received from the AER and the Major Energy Users did not directly substantiate this point. As noted above, these submissions pointed out more broadly that it was not appropriate to consider one rate of return or WACC element in isolation.

That is, the Major Energy Users and the AER indicated in their submissions that a change to one element in isolation of an assessment of all other elements has the potential to upset the balance between competing elements and is unlikely to satisfy the objective of promoting investment in, and efficient use of, electricity services for the long term interests of consumers. As the AER has stated, "even if it were accepted that the appropriate gamma value is 0.25, the AEMC can have no confidence that the quality of the overall rate of return estimate is improved by this rule change request".²⁵

Therefore, by amending gamma in isolation, there could be no certainty that the overall rate of return would be better than that determined within the context of the 2009 WACC review.

Incentive arrangements to undertake efficient investment in transmission networks

SP AusNet and ElectraNet submitted that the incentives for efficient investment will be distorted in circumstances where the value of gamma is knowingly set too low. In particular, such an outcome provides a strong incentive for a transmission business to defer capital expenditure to a later period when the value of gamma will be corrected.

However, without considering other elements and other data available, it is difficult to ascertain whether this is the case. Indeed it is the overall rate of return that establishes incentives for efficient investment. Thus the task of determining whether investment incentives have been distorted is more appropriately that of the AER. This is consistent with that of the AER being responsible for consideration of the rate of return framework as a whole.

In summary, varying the value of gamma as proposed by SP AusNet and ElectraNet in the absence of analysing potential cross-linkages between gamma and the other elements may result in an underlying change in the incentive arrangements for the network businesses. This raises the risk of over recovery of costs to the detriment of end consumers of electricity.

4.3.2 Regulatory certainty and transparency

The framework for determining the rate of return for transmission network businesses as part of their revenue determinations is contained under chapter 6A of the NER. The AEMC is currently assessing rule change requests from the AER and a group of large energy users (EURCC) relating to the rate of return frameworks. The AEMC has acknowledged that the rate of return framework that applies to TNSPs does not provide sufficient flexibility to adapt to changing circumstances. However, the

²⁵ Australian Energy Regulator submission on the consultation paper, April 2012, p. 2.

framework under chapter 6A is still the framework that currently applies to transmission network businesses.

Having a rate of return framework, regardless of its form, provides a level of regulatory certainty and transparency. All stakeholders can anticipate the outcomes of the regulatory process with an understanding of how key elements, such as the rate of return, are to be determined (whether the rate of return is set in advance as part of a periodic review, or determined on a case by case basis as part of each individual determination process).

The rate of return framework in chapter 6A requires that all parameters are to be considered as part of a single, periodic review. The certainty and transparency provided by the framework established in the NER and applied by the AER would be compromised if rule changes were made to amend elements of the application of that framework in isolation.

4.3.3 Conclusion

As stated above, the consolidated rule change request has been assessed on a transitional basis. That is, whether the Commission should make a rule that permits gamma to be amended from the current 2009 review of the WACC and tax parameters undertaken by the AER. This rule would amend the value of gamma from 0.65 to 0.25; however, all other elements of the rate of return framework would remain unchanged.

Consideration of the proposition within the consolidated rule change request from the perspective of recovery of efficient costs, investment incentives, or regulatory certainty, a rule that would amend one element of the rate of return framework in isolation, without considering other elements should not be made.

Abbreviations

AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Commission	See AEMC
DNSPs	distribution network service providers
EURCC	energy users rule change committee
MCE	Ministerial Council on Energy
NEL	National Electricity Law
NEO	National Electricity Objective
NER	National Electricity Rules
the Tribunal	Australian Competition Tribunal
TNSPs	transmission network service providers
WACC	weighted average cost of capital