

Ref.: TP/CP



19 March 2009

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Dear Dr Tamblyn

AER RULE CHANGE PROPOSAL – WACC REVIEWS, EXTENSION OF TIME (Project No ERC0083)

I refer to the above Rule change proposal (**AER Rule change proposal**) and lodge this submission in response. I also refer to the submission lodged by ETSA Utilities on 4 March 2009 and the further submission lodged by ETSA Utilities (**ETSA**) on 6 March 2009 (jointly, the **ETSA Submission**).

1. AER RULE CHANGE PROPOSAL

1.1 No Support

Ergon Energy Corporation Limited (**Ergon Energy**) does not support the AER Rule change proposal in the form proposed by the AER.

1.2 Impact on Ergon Energy

Under the AER Rule change proposal, the AER proposes that the time for concluding its review of the matters referred to in clause 6.5.4(d) of the Rules be extended from 31 March 2009 to 1 May 2009 (and thereafter at intervals not exceeding 5 years). Following the review, the AER must issue a statement of regulatory intent (**SORI**) under clause 6.5.4(c).

In its Rule change proposal, the AER states (in paragraph C “Request for Expedited Process” of Attachment A):

“Allowing a one month extension for the release of the AER’s final decision will not affect the first businesses to which the outcomes of the review will apply”.

The AER also states (in paragraph C “Statement of Issues” part v “*Benefits and costs and potential impact on those likely to be affected by Rule change*” of Attachment A):

“The first businesses to submit a proposal subject to the outcomes of the AER’s review must lodge their proposals on 31 May 2009. Therefore granting the AER an extension until 1 May 2009 to complete its review will not affect the first businesses to become subject to the outcomes of the review.

The AER expects that a one-month extension will not materially affect the ability of the Queensland and South Australian electricity businesses to prepare building block proposals to be lodged by 31 May 2009.”

These statements are not correct.

The one month delay in the review and the issue of the SORI will have a significant adverse impact on Ergon Energy. We suspect it will also have a significant adverse impact on ENERGEX and ETSA.

We suspect that the delay will have less impact on other distribution entities and transmission entities as they are not obliged to submit regulatory proposals on 31 May 2009. They will have more time to absorb the SORI before they are required to submit.

1.3 Inconsistency with National Electricity Objective

The National Electricity Objective as stated in section 7 of the NEL is:

... to promote the efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.

Under clause 6.8.2(b)(1) of the Rules, Ergon Energy must submit, by 31 May 2009, its regulatory proposal for the regulatory control period commencing 1 July 2010 (**Regulatory Proposal**).

For the reasons set out in this submission, any delay in the finalisation of the AER's review and the issue of the SORI will have a significant adverse impact on Ergon Energy's ability to comply with this requirement. The compressed timeframe in which Ergon Energy will have to finalise and submit its Regulatory Proposal will severely limit its ability to properly consider the SORI and submit a fully considered, detailed and compliant Regulatory Proposal.

The process and timeframes set out in Chapter 6 of the Rules were set to give the AER, distribution entities and interested parties adequate time to consider and propose relevant regulatory instruments, consistent with the National Electricity Objective. Any change to those timeframes, without making consequential changes to other interdependent timeframes (or even considering their impact) is inconsistent with the National Electricity Objective.

1.4 Regulatory Proposal

(a) Significance of the SORI to the Regulatory Proposal

Ergon Energy supports the ETSA Submission in relation to the significance of the WACC parameters, which are an essential input into the Regulatory Proposal, and the requirement for reasonable and adequate timeframes to allow Ergon Energy to properly consider the SORI and submit a fully considered, detailed and compliant Regulatory Proposal.

The finalisation of the review and the issue of the SORI by the AER is a critical component in the formulation of Ergon Energy's Regulatory Proposal. Any delay in the issue of the SORI will have a significant adverse impact on Ergon Energy's ability to submit its Regulatory Proposal by 31 May 2009.

When preparing the Regulatory Proposal, Ergon Energy must make a choice whether to accept and apply the AER's SORI or whether instead to propose a departure from the SORI. Schedule 6.1.3(9) of the Rules provides that a building block proposal must contain:

"the provider's calculation of the proposed rate of return, including any proposed departure from the values, methods or credit rating levels set out in an applicable *statement of regulatory intent*;"

This means that Ergon Energy needs to know what the AER's final SORI is, in order to either accept the relevant provisions of the SORI or propose a departure from those provisions. If Ergon Energy proposes to depart from the AER's SORI, the departure needs to be explained with reference to the final SORI. In addition, as the Rules require "persuasive evidence justifying the departure", Ergon Energy may need to collate extensive supporting material substantiating the departure and provide this material in its Regulatory Proposal.

Following the decision to accept or depart from the SORI, Ergon Energy must then apply the WACC parameters to its forecasts and modelling to produce its Post Tax Revenue Model, building block proposal and annual revenue requirement.

All of these steps take a considerable amount of time. Any compression of the timeframe between the AER issuing the SORI and lodgement by Ergon Energy of its Regulatory Proposal will significantly compromise Ergon Energy's ability to submit a fully considered, detailed and compliant Regulatory Proposal.

(b) Governance Requirements

Ergon Energy supports the submissions made by ETSA in relation to the executive and Board oversight required to finally approve the Regulatory Proposal. In addition, as Ergon Energy is 100% owned by the Queensland Government and subject to regulation under the Government Owned Corporations Act 1993 (Qld) (GOC Act), it has additional statutory requirements to comply with that are over and above those in the Rules or that may apply to non-government owned entities.

Ergon Energy has established a working group and process to govern its Regulatory Proposal. It has established a detailed timetable and governance structure to ensure that all timelines are met and that the Regulatory Proposal and all information in it complies with all of the requirements of the Rules, the Regulatory Information Notices (RIN) issued by the AER and its obligations under the GOC Act.

As part of the requirements under the RIN, the Board of Directors are required to certify that the key assumptions that underpin the Regulatory Proposal are reasonable. This certification must be in accordance with a resolution of the Directors. In addition, I must sign a Statutory Declaration that the information provided is complete in all material respects and can be relied on by the AER. In order to obtain the necessary level of comfort to be able to give the certifications and declarations, Ergon Energy has established a very detailed governance and due diligence framework to check all information in the Regulatory Proposal and obtain appropriate sign offs from key officers. This process is lengthy and involves a large number of Ergon Energy's officers and employees.

In addition to settling the content of the Regulatory Proposal and obtaining all of the necessary sign-offs, Ergon Energy must also comply with its reporting requirements under the GOC Act and brief its shareholding Ministers in accordance with the GOC Act and particularly, in relation to any matters that may involve significant changes to commitments, projections or assumptions underpinning its Statement of Corporate Intent and Corporate Plan for periods covered by the Regulatory Proposal.

It is only after all of these steps have been completed in turn that Ergon Energy will be able to finalise, organise publication and lodge its Regulatory Proposal with the AER.

If the SORI is not finalised until 1 May 2009, Ergon Energy will not be able to meet its planned timelines and processes and submit the Regulatory Proposal by 31 May 2009.

1.5 Subsequent Statements of Regulatory Intent

The AER's justification for the Rule change proposal is that it will not have time to finalise its review by 31 March 2009.

However, the impact of the AER's proposed change to clause 6.5.4(b) of the Rules is that the additional one month time period will apply not only to the current review, but also all subsequent reviews.

By way of example, the AER must conduct reviews by 31 March 2009, 31 March 2014 and 31 March 2019. Ergon Energy must lodge Regulatory Proposals by 31 May 2009, 31 May 2014 and 31 May 2019.

If the change to clause 6.5.4 of the Rules was made (with no corresponding change to clause 6.8.2 (b)) Ergon Energy may have less than one month after receipt of the relevant SORI to finalise and submit its Regulatory Proposals for not only the next regulatory control period but all subsequent regulatory control periods

1.6 Suggested Amended Rule Change

Having regard to the AER Rule Change proposal and the ETSA Submission, Ergon Energy does not support the changes to the Rules proposed by the AER. Ergon Energy is of the view that if the AEMC agrees to extend the date for issuing the SORI, the National Electricity Rules should be changed in the way shown in our Annexure.

In summary, Ergon Energy's approach to a Rule change would:

- (a) enable the AER to finalise its review of the matters referred to in clause 6.5.4(d) of the Rules by 31 May 2009;
- (b) ensure that the extension of time only applied in relation to the review currently being undertaken by the AER; and
- (c) extend the time that Ergon Energy and other relevant distribution entities have to submit their regulatory proposals, so that they are not disadvantaged by the extension of time under clause 6.5.4(d).

Under Ergon Energy's approach to a Rule change, any extension of time for the AER and the relevant distribution entities does not impact on the commencement and length of the regulatory control period for each of the relevant distribution entities. For Ergon Energy, the regulatory control period will continue to run on a financial year basis, and the next regulatory control period would commence on 1 July 2010.

2. ETSA SUBMISSION

Ergon Energy gives qualified support to the ETSA Submission.

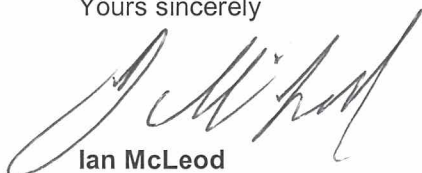
Ergon Energy agrees with most of the arguments and issues raised by ETSA, particularly as discussed in section 1.4 above.

However, despite agreeing with the intent of the ETSA Submission, Ergon Energy does not support the changes to the Rules proposed by ETSA. The changes proposed by ETSA only grant an extension of time to ETSA. The extensions of time should also be granted to Ergon Energy and other relevant distribution entities.

Ergon Energy believes that the most appropriate changes to the Rules are those set out in our Annexure.

Please do not hesitate to contact me or Tony Pfeiffer, General Manager Regulatory Affairs on (07) 3228 7711 if you wish to discuss this submission.

Yours sincerely



Ian McLeod
Chief Executive

ANNEXURE

Proposed Changes to the National Electricity Rules

Ergon Energy proposes that the National Electricity Rules be amended in accordance with the changes marked up below.

6.5.4 Review of rate of return

- (a) ...
- (b) The first review is to be concluded by ~~31 March 2009~~ 1 May 2009. The second review is to be concluded by 31 March 2014 and further reviews are to follow at intervals not exceeding, in any case, 5 years.
- (c) ...

6.8.2 Submission of regulatory proposal

- (a) ...
- (b) A Subject to paragraph (g), a regulatory proposal must be submitted:
 - (1) at least 13 months before the expiry of a distribution determination that applies to the service provider; or
 - (2) if no distribution determination applies to the service provider, within 3 months after being required to do so by the AER.
- (c) ...
- (d) ...
- (e) ...
- (f) ...
- (g) Despite paragraph (b), a Distribution Network Service Provider does not have to submit a regulatory proposal before the date which is 60 days after the AER has:
 - (i) _____ concluded its most recent review under clause 6.5.4(b); and
 - (ii) _____ issued a statement of regulatory intent under clause 6.5.4(c) in consequence of that review.