



12 December 2016

Mr John Pierce
Chair
Australian Energy Market Commission
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Office of the
Chief Executive Officer

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Dear Mr Pierce

RE: ERC0210 – Participant derogation – NSW DNSPs revenue smoothing

Ausgrid appreciates the AEMC's commencement of the consultation process on this Rule change request. We provide these comments for further clarity of Ausgrid's views on the issues raised in the consultation paper. We hope that this submission will assist the AEMC in making a determination on our proposed Rule change.

The consultation paper raised two particular issues; namely:

1. Costs and benefits of reducing price volatility.
2. Mechanism for smoothing.

Cost and benefits of reducing price volatility

Ausgrid considers that minimising price volatility between regulatory years and between regulatory periods aligns with the intent of the regulatory framework. In making a distribution determination for a network service provider, the AER has historically sought to minimise the lumpiness of the annual building block revenue by smoothing the revenue profile between regulatory years via the setting of the X-factors. Further, the NER requires the variance between the expected revenue and annual revenue requirement of the final year of the regulatory period to be minimised as far as reasonably practical to avoid any material movement in the revenue between the last regulatory year of a period and the first regulatory year of the next period.

Given the likelihood that there may need to be revenue adjustments (either an increase or a reduction) for the current regulatory period, and the fact that the current NER framework does not allow for the smoothing of revenue between regulatory periods, we consider that the proposed participant derogation provides a means, with sufficient flexibility, for Ausgrid to propose and the AER to determine a price path that best serves the interest of customers with respect to price and aligns with the intent of the regulatory framework.

Mechanism of smoothing

The AEMC noted that the Rule change proposal did not specifically identify a discount rate to be used in the net present value calculation of smoothed revenues. We understand that the issue is about whether the discount rate should only compensate for the time value of money (i.e. inflation) or should it also compensate for the opportunity cost. The AEMC also noted that the approach to ensuring NPV neutrality is a task of the AER, consistent with approach currently embedded in the NER.

Ausgrid agrees that it is the task of the AER to ensure NPV neutrality in setting the X-factors, within the constraints imposed by the NER. We note that it has been an enduring practice of the AER in carrying out this task that the discount rate used in the NPV calculation is the rate of return set by the AER for the relevant regulatory year. This rate of return reflects both the time value of money as well as the opportunity cost.

Ausgrid considers that there are no reasons to depart from this regulatory practice in calculating the NPV of the revenue adjustments; that is the rate of return determined by the AER for the relevant regulatory year should be used as the discount rate in NPV calculation.

If you have any queries or wish to discuss this matter in further detail please contact Joseph Pizzinga, Chief Financial Officer on (02) 9269 2121 or via email jpizzinga@ausgrid.com.au.

Yours sincerely



RICHARD GROSS
Chief Executive Officer