Public forum

Review into the use of total factor productivity for the determination of prices and revenues

Monday, 1 February 2010
Melbourne Airport Hilton

Agenda

10.15 am	Opening remarks Dr John Tamblyn, AEMC Chairman
10.30 am	Overview of preliminary findings 1 (economic) Eamonn Corrigan, AEMC
10.45 am	Overview of preliminary findings 2 (practical) Meredith Mayes, AEMC
11.00 am	Comments from interested parties: • presentations from DPI, APIA, EUAA • open discussion on preliminary findings
12.00 pm	Break
12.15 pm	Way forward for the review and concluding comments Eamonn Corrigan, AEMC
12.30 pm	Open discussion on way forward
1.00 pm	Lunch

Summary of discussion

On 1 February, the Australian Energy Market Commission (AEMC) held a public forum to present the key issues from the Preliminary Findings for the AEMC's review into the use of total factor productivity (TFP) for the determination of prices and revenues (TFP Review). The AEMC also sought to obtain views and opinions from stakeholders on the Preliminary Findings (as published on 17 December 2009) and related issues at the forum. The AEMC was represented by Dr John Tamblyn (Chairman), Anne Pearson, Charles Hoang, Colin Sausman, Eamonn Corrigan and Meredith Mayes.

Dr John Tamblyn opened the forum and welcomed all participants and presenters. In a brief presentation, he outlined the purpose of the AEMC's TFP Review, the considerations in the Preliminary Findings, and the timetable for the Review (submissions on the Preliminary Findings are due 26 February 2010).

The second presentation was given by AEMC staff on the economic assessment in the Preliminary Findings. This focused on the efficiency properties of a TFP methodology, using the current building block approach as the counterfactual. The assessment also assumed that the necessary data-set will be available and the TFP index can be calculated.

The AEMC staff then provided a presentation on the practical assessment in the Preliminary Findings. Here, the assumptions made in the previous presentation relating to the availability of the data-set and the calculability of a TFP index were relaxed. This allowed an assessment of the pre-conditions for practical application of a TFP methodology, its potential impact on the regulatory framework, and its potential application to the energy sectors. The current building block approach was used as the counterfactual in this assessment.

Following the brief presentations from the AEMC staff, key interested parties provided presentations:

- Raif Sarcich, representing the Victorian Department of Primary Industries (DPI), presented its position on TFP and some comments on the Preliminary Findings:
    - The current building block approach is complex and that TFP would simplify the process and be a dynamic incentive for innovation.
    - The Victorian distribution electricity and gas industry is now stable and TFP can be implemented now.
    - DPI expressed two areas of concern on the Preliminary Findings:
        - Although it agreed that an accurate and robust data-set would be required for a TFP methodology to work, it considered that this has already been achieved via the ESC-PEG work. DPI does not consider it necessary to restart a data collection process nor that eight years of data is required as proposed. Therefore, in DPI's view TFP could be commenced immediately.
        - The analysis appears to be based on a 'transitional' TFP methodology. It should be based on an 'end-game' design with off-ramps rather than scheduled price resets as this is the design that delivers significant benefits.
- Chris Harvey provided a presentation on behalf of the Australian Pipeline Industry Association (APIA) and made the following comments:

- APIA supports the time in which the AEMC has taken for this Review and sees it as indicative of the time required to consider and develop a TFP methodology.

- APIA has not changed its position since the previous AEMC TFP Public Forum in February 2009 – that TFP is not appropriate for the gas transmission sector.

- APIA agrees with the AEMC view that a TFP methodology would be less appropriate for the energy transmission sector. It considers that it would be possible to confirm this view and conclude consideration of TFP for transmission now (rather than waiting for eight years of data). In particular, the APIA considers that the gas transmission sector can be excluded from a TFP methodology and explained the reasons for this view.

- Some questions APIA raised with the AEMC were whether the assumptions used to assess a TFP methodology were appropriate and whether the information asymmetry issue has been overstated.

- Roman Domanski from the Energy Users Association of Australia (EUAA) presented EUAA's views, including:

    - Compared to the UK, NSW electricity distributors performed worse in terms of productivity. Victoria, on the other hand, showed better performance, but EUAA would be concerned if the AER accepted the Victorian service providers' proposals on expenditure assessments.

    - EUAA considered that there are fundamental issues which would not be addressed by the TFP Review such as flaws in Chapters 6 and 6A of the NER, the lack of political independence of the AER, privatisation of energy companies, and institutional design and relationships.

    - EUAA suggested ways forward including the consideration of a full range of comparative techniques such as TFP, the removal of the propose-respond model, the removal of the appeals process, a single review of both transmission and distribution as done in the UK, and encourage for customer engagement.

A copy of all presentations can be found on the AEMC's website.

The following issues were raised in the open discussion:

- ENA questioned what counterfactual would be used for comparison to a TFP methodology given that the building block approach is evolving over time. Further, if eight years of data is required before TFP can be used as a revenue determination method then it is possible that the building block approach may improve over that time.

- Grid Australia indicated it would not support providing data for the electricity transmission sector, noting that adequately reporting is another thing.

- SP AusNet also considered that the Preliminary Findings was proposing for a transitional TFP methodology and should aim for a final TFP methodology. It was also of the view that there should only be one P_0 regulatory reset over a long regulatory period (with possibility of off ramps).

- Energex noted that the Preliminary Findings refers to data being audited. However, at present auditing is only done for financial data and not engineering data. This means more work would be required to audit engineering data under a data reporting regime that supports TFP.

- APIA questioned how different would a P_0 assessment under the building block approach would be compared to a TFP methodology.

- Jemena suggested that the uncertainty in setting P_0 is in the determination of what would be defined as efficient cost and that this is still an issue under the suggested TFP methodology.

- Paul Fearon suggested that a TFP methodology provides the opportunity to move regulation toward a better mimic of competitive market forces for the service providers instead of focusing on a static framework that tries to determine future efficient costs. The DPI added that a TFP methodology would incentivise service providers to compete against the productivity trend for that industry over the long term. This is something that in DPI's view the building block approach does not provide.

- The AER asked how a TFP methodology, or any such form of economic regulation, would provide for stronger incentives for lower costs, pass cost savings to consumers, and be less costly to administer. The AER suggested that such a thing does not exist. The selection of any regulatory method requires a trade-off of these things.

- EUAA was concerned that a TFP methodology would not have a good starting point (that is, initial price). It considered that this is because service providers have not been operating at efficient costs. This is because of problems with the operation of the current regulatory regime, data collection, inconsistent jurisdictional decisions, and government ownership.

- The EUAA also noted the concerns of service providers about the costs relating to providing data to the regulator. In the EUAA's opinion, this cost is something that service providers would have to bear as a result of being monopoly businesses.

Dr John Tamblyn thanked all for participating in the Public Forum and reminded interested parties to provide any submissions to the AEMC on the Preliminary Findings and the accompanying consultant reports by 26 February 2010.

Participants

The AEMC invited all industry stakeholders to attend the Public Forum. The following attended the forum.

Name	Surname	Company
Alan	Smith	Parsons Brinkerhoff
Alex	McPherson	Energex
Andrew	Ley	Australian Energy Regulator
Anh	Mai	SP AusNet
Anne	Pearson	Australian Energy Market Commission
Charles	Hoang	Australian Energy Market Commission
Chris	Harvey	Chris Harvey Consulting
Colin	Sausman	Australian Energy Market Commission
Darryl	Biggar	Australian Energy Regulator
Dennis	Lawrence	Economic Insights
Eamonn	Corrigan	Australian Energy Market Commission
Garth	Crawford	Energy Networks Association
Isaac	Katz	Harding Katz Pty Ltd
Jason	Cooke	Country Energy
Jeremy	Rothfield	United Energy Distribution and Multinet Gas
Jim	Bain	Energy Networks Association
Jodi	Smith	Department of Resources, Energy and Tourism (Cth)
John	Tamblyn	Australian Energy Market Commission
Jon	Hocking	Integral Energy
Joseph	Caruana	Energy Branch - Industry and Investment NSW
Lindsay	Gamble	AEMO
Luke	Reedman	CSIRO
Mark	McLeish	Australian Energy Regulator
Mark	Pedler	Dept for Transport, Energy and Infrastructure (SA)
Meredith	Mayes	Australian Energy Market Commission
Mick	Ryan	Energex
Natalie	Lindsay	Country Energy
Paul	Fearon	Energy Safe Victoria
Paul	Callander	APA Group
Peter	Dobson	Department of Primary Industries (Victoria)
Peter	Walshe	Parsons Brinkerhoff
Raif	Sarcich	Department of Primary Industries (Victoria)
Roman	Domanski	EUAA
Son	Truong Vu	EnergyAustralia
Stephanie	McDougall	CitiPower / Powercor Australia
Warwick	Tudehope	Jemena Limited