



# SETTING THE OPENING CAPITAL BASE

Response to AEMC Consultation Paper – GRC0025

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## OVERVIEW

The Energy Networks Association (ENA) welcomes the Australian Energy Market Commission's (AEMC) Consultation Paper on the *National Gas Amendment (Setting the Opening Capital Base)* rule change request (Consultation Paper).

The rule change request seeks to modify the *National Gas Rules* to require a regulator to remove any benefit or penalty associated with the difference between estimated and actual capital expenditure in the final year of the regulatory period when setting the opening capital base for a subsequent access arrangement period.

The AEMC Consultation Paper also raises the potential for an alternative amendment to be made to both the *National Electricity Rules* and *National Gas Rules* to the same effect, but with greater specification around defining the 'benefit or penalty'. This submission addresses the regulatory policy issues involved in making equivalent amendments to both sets of Rules.

The ENA supports the basis of the rule change proposal as providing improved clarity over the legal basis of decision-making under the National Gas Rules. In principle, ENA support the potential alternative amendment applying across both electricity and gas raised by the AEMC as providing added clarity to the capital base roll-forward process. This support is subject to the examination of a detailed draft rule and the impact of such a rule being limited to codifying current regulatory practice under the *National Electricity Rules*.

## BACKGROUND

The Energy Networks Association is the national industry association representing the businesses operating Australia's electricity transmission and distribution and gas distribution networks. Member businesses provide energy to virtually every household and business in Australia. ENA members own assets valued at over \$100 billion in energy network infrastructure.

This submission provides an initial perspective of network businesses on the rule change proposal ahead of the AEMC draft rule determination. The Consultation Paper also poses a number of threshold questions on the scope and benefits of the rule change proposal. These are addressed in Annex A to this submission.

## IMPROVED PREDICTABILITY

The ENA considers that the rule change proposal has the potential to materially improve predictability in the operation of the capital base provisions of the *National Gas Rules*. This is because the proposed change clarifies the powers of the AER and WA Economic Regulation Authority to make adjustments to remove benefits and penalties associated with variations between forecast and actual expenditure in the final year of an access arrangement.

This clarification would follow two Australian Competition Tribunal rulings which made materially different findings on the power of the AER to make such adjustments. These adjustments are explicitly provided for under the existing *National Electricity Rules* for both electricity transmission and distribution businesses.

In ENA's view improved transparency and predictability would benefit consumers through avoiding unnecessary ambiguity over the future power to make such adjustments in respect of gas distribution networks. This has the potential to marginally reduce the potential for costly disputes, and ensure that the regulatory regime operates in a predictable manner.

The option raised to extend the rule change to clarifying under both the National Electricity and Gas Rules that the adjustments should be confined to the return on capital component would also represent a modest but desirable increase in the predictability of the regulatory regime.

## ANALYSIS OF INCENTIVE IMPACTS

ENA recognises that the operation of roll forward and capital base establishment approaches present significant complexities where these involve interactions with forecasts or estimated costs.

For this reason, ENA strongly encourages AEMC to include in the pending draft rule determination full and systematic analysis of the incentives under the current Gas Rules, and any potential rule amendments.

This is important to ensure that all parties can have confidence that divergences in forecasts and estimates from actual outturn results are treated in a consistent and symmetrical way that supports efficient, predictable, and time consistent incentives.

## ANNEX A - RESPONSE TO QUESTIONS FOR CONSULTATION

### The issue as proposed

*1. Do stakeholders agree that the issue identified by the AER in this rule change request needs to be addressed through a rule change and, if so, why? If not, please explain why the issue, as characterised by the AER, does not need to be addressed through a rule change or may be addressed in some other way.*

ENA agrees that clarity and predictability would be enhanced by a rule change to address the issues identified.

### The proposed solution

*1. Do you consider the proposed solution is a proportionate response to the issue identified by the AER?*

The AER's proposed solution of making clarifying amendments to the *National Gas Rules* is a proportionate response to the issues raised by the two Australian Competition Tribunal rulings in the APA and Jemena matters.

*2. Do you consider the wording of the proposed rule is sufficiently clear and accurately captures the intended adjustment to the accumulated return on capital in the circumstances noted?*

ENA agrees that the AER's proposed rule change may benefit from further clarification to ensure clarity about the scope of regulatory discretion around the scope of benefits or penalties associated with differences between actual and estimated capital expenditure.

*3. On the basis of the issue as raised by the AER, do you consider there is a more preferable solution(s) to this issue?*

ENA supports the position put in the AEMC Consultation Paper to more precisely define the nature of the benefit of penalty to be addressed. This option should be developed further as part of the draft rule determination process.

### The impacts of the proposed rule change

*1. In what way do you consider the proposed rule change may or may not affect efficiency in providing gas pipeline services and the long term interests of consumers?*

By providing increased predictability over the scope of adjustments that could be made in the establishing of an opening regulatory asset base the rule change would enhance predictability and transparency, to the benefit of consumers (i.e. through lower potential dispute costs). A stable and predictable roll forward approach also decreases regulatory risk for network investors, enabling benefits

through better access to efficient financing through debt and equity markets.

*2. Would implementation of the proposed rule improve consistency of regulatory processes and promote process certainty among pipeline users?*

Yes, subject to any unintended impacts of the interaction of forecasts, estimation approaches and incentives which should be fully scoped as a matter of priority in further stages of the rule change.

*3. How would the rule as proposed impact upon service provider efficiency incentives that underpin the regulatory regime?*

As proposed, the rule should essentially codify typical regulatory practice under the *National Electricity Rules*, at the margins modestly reinforcing the incentive qualities of the regime.

### The costs and benefits

*1. Is the proposed approach likely to improve and/or promote administrative efficiency and minimise undue regulatory burden?*

As above, by codifying existing practice and providing modestly enhanced predictability around the scope of benefits or penalties that can apply in establishing an opening capital base, the approach should marginally improve administrative efficiency and minimise costs..

*2. Would the proposed rule impose any material costs on consumers or service providers? Please estimate, describe and characterise any costs and their impacts.*

As above, at this stage ENA can identify no significant cost imposition on service providers or consumers.