20 October 2006

Dr J. Tamblyn
Chairman, Australian Energy Market Commission
Level 16
1 Margaret Street
Sydney NSW 2000

By email – submissions@aemc.gov.au

Dear John

ETSA Utilities' Comments on the AEMC Review of the Electricity Transmission Revenue and Pricing Rules Assessment of forecast Expenditure (October 2006)

ETSA Utilities would like to make some brief comments on the AEMC's request for further views on the decision-making requirements of the Draft Revenue Rule in relation to the regulator's assessment of forecast expenditures. Our comments are split into remarks on Process, Content of legal Advice and AEMC Issues.

Regulatory Process

The AEMC's public consultation process on the electricity transmission revenue rules has been underway for about eight months, with submissions and debate from many parties covering TNSP's, other networks, customers, government agencies and regulators. The submissions and arguments have been disclosed in a public and transparent manner.

It appears that the Department of Industry, Tourism and Resources has sourced legal advice for the purpose of the Distribution Rules that relates to the decision-criteria on regulators being required to accept reasonable estimates of expenditure provided by network service provider's. This advice has been forwarded to the AEMC.

ETSA Utilities values the publication of this advice, albeit at such a late stage of the decision-making process. This is far preferable to not having had such advice published if the advice is to have any standing at all in this debate. Having the advice subject to a single week of review when all other aspects have been open for some months should limit the amount of weight that the AEMC can assign to this advice.

ETSA Utilities notes that the AEMC proposes to obtain and publish a Senior Counsel's legal opinion on some key issues as part of the final rule determination.

<u>Content of Legal Advice</u>

The scope of the legal advice is principally on the potential to narrow the decision-criteria of reasonable estimates for possible electricity distribution revenue rules. It does not appear to consider the implications that such an alternate decision criterion would create. The AEMC paper explores a range of reasonable outcomes and recognises the absence of a single correct answer in these matters – regulation is perhaps better described as an art than a science. However, the legal advice implies that the regulator should be empowered to make the final, best estimate no matter what the network service provider has submitted.

Such arrangements would result in the elimination of 'propose/respond' completely, with the revenue reset process remaining a 'consider/decide' (with the degree of 'consider' to be applied determined unilaterally by the regulator). The AEMC paper and proposals went to some length in identifying why the 'propose/respond' model would be a better method, including:

- an expectation of better forecasts incorporating more robust substantiation of proposals by network service providers,
- less gaming by network service providers (because of the fear that forecasts considered to be unreasonable by the regulator could be rejected and replaced by the regulator's sole opinion), and
- more information would be available to customers during the consultation process. ETSA Utilities would expect that the regulator would have a better public review of the expenditure proposals under the propose/respond arrangement than has existed in other revenue determinations over recent years, enabling a more informed regulatory decision.

ETSA Utilities considers that the legal advice provided by the Department of Industry, Tourism and Resources does not consider appropriately the revised framework for revenue resets incorporated in the AEMC's draft rule. If adopted, the recommendation would introduce a new uncertainty about how 'best estimates arrived at on a reasonable basis' should be interpreted. In contrast, the interpretation of 'reasonable estimate' is relatively familiar for all parties involved.

AEMC Issues

The AEMC explicitly asked ‘*should the rules provide that:*

a. a TNSP's proposal must be accepted if the AER is satisfied that the proposal for forecast expenditure satisfies the criteria in the Rules; or

b. the AER should have a residual discretion to substitute its own reasonable estimate of forecast expenditure in those circumstances?’

ETSA Utilities believes that option A should be included in the rules. Without that, the expenditure forecast process falls back to consider/decide, and the benefits and expectations of the AEMC as outlined in the draft rule discussion paper may be lost, depending on the level of ‘consider’ applied by the regulator and the relationship between the regulator and network service provider.

ETSA Utilities would also expect that under option A, following the public consultation procedure on the expenditure forecasts, the regulator would accept the TNSP's proposed forecast expenditure if (and only if) satisfied that the proposal met the criteria contained in the revenue rules. If the regulator formed a view that the forecast expenditure was unreasonable, then those forecasts would be rejected and replaced by the regulator’s reasonable forecast. In such circumstances, ETSA Utilities would expect the regulator to disclose why the TNSP’s forecasts were not reasonable.

Please contact James Bennett (Manager Regulation, ph 08 8404 5261) if you wish to discuss this response.

Lew Owens
Chief Executive Officer, ETSA Utilities

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