

Profitability measures for energy network businesses

Public Forum

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Outline

1. Opportunities and support for profitability metrics
2. Use of profitability measures
3. Observations on measure comparability issues
4. Suggested approach

Networks support development of profitability measures

- » Network business support development and implementation of profitability measures
- » We recognise consumers need for meaningful measures able to be used in a timely way
- » Potential opportunities of getting this process right
 - Increased transparency around outcomes of AER regulatory determinations over the medium term
 - Enabling better stakeholder participation in regulatory and policy processes, promoting NEO and NGO consistent outcomes
 - Promoting improved confidence and stability of the regulatory framework

Use of profitability information

- » Position Paper positively clarifies that a mechanistic approach will not be adopted
- » Use of profitability information considered in AER Rate of Return Joint Experts Report

“It was agreed that this data should be collected by AER to assist with achieving its other non-rate of return regulatory objectives

View expressed by most experts was that historic profitability analysis was a function of expectations at time price control set, provides no information on appropriate rate of return, and an ex post review would be fundamentally inconsistent with an incentive based regulation framework.” (p.35)

- » Value in achieving clarity and alignment of expectations of stakeholders about how such information will be used before data publication begins

Observations on measure comparability issues

- » Potential for a 'half-way' house of adjusting statutory accounts towards regulatory accounts holds risks for complexity, transparency and acceptance of measures
- » Potential for stakeholder confusion in a dual reporting of regulatory and adjusted statutory accounts
- » More work required to allow for 'apples to apples' comparison
 - e.g. if tracking actual EBIT and NPAT, PTRM needs to have a similar benchmark
- » Earnings per customer measure still has comparability issues between diverse distribution network types and densities
 - Excluding transmission positive move that recognises this, but issue remains

Observations on measure comparability issues (II)

- » Unclear limitations in RAB multiples will be overcome under suggested approach
 - Will RAB multiples be ‘decomposed’ into regulated/unregulated revenues?
- » Impact of operation of incentive schemes should be transparent in each reporting measure
 - to support the objectives of informing debate on the overall regulatory framework

Suggested approach

- » Consider potential implementation costs and build in a “review step”
- » Test with stakeholders in further discussions their likely confidence in ‘mixed’ statutory/regulatory measures sought from networks
- » Ensure upfront stakeholder alignment on how profitability measures will be used
- » Build performance reporting framework to recognise that incentive-based regulation means high profitability can be sign of successful delivery of NEO/NGO outcomes
- » Potential two stage approach
 1. Focus on the clearly achievable set of regulatory accounting based metrics initially
 2. Involve all stakeholders in more detailed development work on any statutory account reliant measures, to ensure community wide confidence in results