Submission to the AER

Draft position paper: Profitability measures for electricity and gas network businesses

30/05/2018

INTRODUCTION

The Australian Pipelines and Gas Association (APGA) welcomes the opportunity to comment on the Australian Energy Regulator's (AER) Draft position paper on Profitability measures for electricity and gas network businesses.

APGA is the peak body representing Australasia's pipeline infrastructure, with a focus on gas transmission, but also including transportation of other products. Our members include owners, operators, constructors, advisers, engineering companies and suppliers of pipeline products and services. APGA's members build, own and operate the gas transmission infrastructure connecting the disparate gas supply basins and demand centres of Australia, offering a wide range of services to gas producers, retailers and users. The replacement value of Australia's gas transmission infrastructure is estimated to be $50 billion.

A stable and internally consistent regulatory framework is vital to maintaining the attractiveness of the Australian energy sector as a destination for investment. APGA considers that an ability to capture performance against regulatory determinations could play a role in maintaining the attractiveness of the Australian energy sector as a destination for investment by providing confidence that levels of out or under-performance against regulatory benchmarks remain within reasonable bounds given the incentive regulation framework. However, in order to perform this role, the measures need to be clear, meaningful and relevant to the regulatory task. From this perspective, whilst broadly supportive of the approach the AER appears to be following, we have two concerns:

- The mixing of information from statutory and regulatory perspectives when the two are very different.
- A residual lack of clarity about the framework of use of the measures.

We discuss these two issues below.

KEY ISSUES

Common Basis for Regulatory Inputs

One of the AER's objectives, which is set out in section 2.5 of the draft position paper, is to "identify measures that will allow comparison of the profit outcomes of the service providers [i.e. firms that are subject to regulatory revenue determination] with other businesses in the broader economy". One of APGA's key concerns with the set of measures currently proposed by the AER is that they rely on figures from both "statutory" accounting and "regulatory" frameworks.

These two frameworks are fundamentally different, and it is not a simple matter of adjusting numbers from one framework to another. For example, the asset base (RAB in a regulatory context) which forms the denominator in any returns percentage is formed via the interaction of competitive forces for statutory accounts in the wider economy, whilst the regulatory RAB is formed on the basis of a specific set of rules developed by the regulator.

The effect of using "mixed" figures is that it can leave stakeholders unable to meaningfully compare the profit outcomes of regulated and unregulated companies due to the use of fundamentally different concepts. Such differences will mean that any comparisons with the broader economy need to be treated with considerable caution.

There may be some scope for the development of interim or indicative numbers in the short term, provided all parties are aware of the limitations of such numbers, but, in the long-term, a robust solution to this problem is for AER to develop a full set of regulatory accounts to underpin the profitability measures. We consider that these accounts should be developed jointly with consumers, the AER and businesses.

Use of the measures

The AER has responded to calls from stakeholders concerning more clarity in respect of how the measures are likely to be used. While it is helpful to have some further guidance on what the information will not be used for, for there to be certainty and stability in the decision-making process we consider that it would be useful to take this further and develop some principles of use, so that stakeholders can understand how the information might be used and be assured that the information would not be used in an arbitrary or unpredictable manner. The obvious basis for such principles of use would be the incentive regulation framework, and based upon that, we propose two principles:

- If profit out-performance is due to out-performance of benchmarks set in the incentive framework, e.g. out-performance of operating expenditure allowances, then there is nothing further for the AER to consider. Such out-performance is consistent with the incentive-based framework, and the framework already contains means for these benefits to be shared with consumers.
- If profit out-performance is due to factors outside of the incentive framework, e.g. changes in interest rates, then the AER could take that out-performance into account in a contextual way in its regulatory determination process. However, this consideration would need to be symmetrical, so that any under-performance also needs to be taken into account by the AER in considering the overall context of its decision.

The reasons for any over or under-performance of a service provider against its regulatory benchmarks should be easy to identify. We would encourage the AER to provide examples on how it might use information associated with the second principle with its final position paper to provide greater clarity for stakeholders.