



# **Electricity transmission and distribution network service providers**

## **Statement of the revised WACC parameters (transmission)**

## **Statement of regulatory intent on the revised WACC parameters (distribution)**

May 2009

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### **Amendment record**

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<b>Version</b>	<b>Date</b>	<b>Pages</b>
1	11 December 2008 (proposed)	7
2	1 May 2009 (final)	7

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## Shortened forms

AER	Australian Energy Regulator
DNSP	distribution network service provider
NEL	National Electricity Law
NER	National Electricity Rules
TNSP	transmission network service provider
WACC	weighted average cost of capital

# 1 Nature and authority

## 1.1 Introduction

This document contains the Australian Energy Regulator's (AER):

- *Statement of the revised WACC parameters* (the transmission statement), and
- *Statement of regulatory intent on the revised WACC parameters* (the distribution statement),

which respectively set out the revised weighted average cost of capital (WACC) values, methods and credit rating levels to be applied by the AER in making a transmission network service provider's (TNSP) revenue determination under chapter 6A of the National Electricity Rules (NER) and a distribution network service provider's (DNSP) building block determination under chapter 6 of the NER. The revised WACC parameter values, methods and credit rating levels set out in the statements are the outcomes of the AER's first review of the WACC parameters under the NER.<sup>1</sup>

The WACC parameters are relevant to the return on capital and estimated cost of corporate income tax building blocks.

The statements apply to transmission revenue determinations and distribution building block determinations where the NER require the respective revenue proposal or regulatory proposal to be submitted to the AER between 1 May 2009 and 1 April 2014. The values, methods and credit rating levels are 'locked-in' for transmission revenue determinations, in that under chapter 6A a departure from these parameters is not permissible at the time of the determination. For distribution building block determinations under chapter 6, a departure is only permissible where there is persuasive evidence to do so.

These statements and the accompanying final decision, and all references to relevant provisions contained therein, refer to and have been made in accordance with version 28 of the NER dated 16 April 2009.

## 1.2 Authority

The NER require the AER to review the following matters:

- the nominal risk free rate, including the maturity period and bond rates
- the equity beta
- the market risk premium

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<sup>1</sup> NER, cls. 6.5.4, 6A.6.2 and 6A.6.4.

- the ratio of the value of debt to the value of equity and debt<sup>2</sup>
- the credit rating level, and
- the assumed utilisation of imputation credits.<sup>3</sup>

### **1.3 Role of the statement—transmission determinations**

The WACC parameter values, methods and credit rating levels contained in the transmission statement in this document are to apply to transmission determinations where the revenue proposal is submitted to the AER between 1 May 2009 and 1 April 2014 in accordance with clauses 6A.6.2 and 6A.6.4 of the NER.

The revised values, methods and credit rating levels adopted in the transmission statement supersedes the equivalent values, methods and credit levels prescribed in clauses 6A.6.2 and 6A.6.4 of the NER.

### **1.4 Role of the statement of regulatory intent—distribution determinations**

The WACC parameter values, methods and credit rating levels contained in the the distribution statement are to apply to distribution determinations where the regulatory proposal is submitted to the AER between 1 May 2009 and 1 April 2014 in accordance with clause 6.5.4 of the NER.

The revised values, methods and credit rating levels adopted in the transmission statement supersedes the equivalent values, methods and credit rating levels (where appropriate):

- prescribed in clause 6.5.2 of the NER
- prescribed in clauses 6.5.2 and 6.5.3 in appendix 1 of chapter 11 of the NER, or
- set out in the current jurisdictional determinations for DNSPs in Queensland, Victoria, Tasmania and South Australia.

### **1.5 Confidentiality**

The AER's obligations regarding confidentiality and the use and disclosure of information provided to it by a TNSP or DNSP are governed by the *Trade Practices Act 1974* (Cth), the National Electricity Law (NEL) and the NER. For further information regarding the AER's use and disclosure of information provided to it, see the *ACCC/AER Information Policy*, October 2008, available on the AER's website.

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<sup>2</sup> Clause 6A.6.2(i)(1)(v) of the NER refers to the market value of debt to the market value of equity and debt.

<sup>3</sup> NER, cls. 6.5.4(a), 6A.6.2(f) and 6A.6.4(b).

## **1.6 Processes for revision**

The AER must complete its second review of the WACC parameters for transmission determinations at an interval after the completion of this first review of five years.<sup>4</sup>

The AER must complete its second review of the WACC parameters for distribution determinations at an interval after the completion of this first review not exceeding five years.<sup>5</sup>

## **1.7 Definitions**

Terms italicised in the statements are given their meaning in chapter 10 of the NER unless otherwise specified.

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<sup>4</sup> NER, cls. 6A.6.2(g) and 6A.6.4(c).

<sup>5</sup> NER, cl. 6.5.4(b).

## 2 Statement of the revised WACC parameters—transmission

- 2.1 Paragraphs 2.2–2.8 set out the revised values, methods or credit rating levels adopted by the *AER* in accordance with clause 6A.6.2(h) of the *NER* to apply to a *Transmission Network Service Provider’s revenue determination* where the relevant *revenue proposal* is submitted to the *AER* between 1 May 2009 and 1 April 2014.
- 2.2 In relation to the method to calculate the nominal risk free rate ( $r_f$ ):
- (a) it is to be on a moving average basis from the annualised yield on Commonwealth Government bonds with a maturity of 10 years,
  - (b) the period of time in which it is to be calculated is either:
    - (i) a period (‘the agreed period’), being one which is as close as practically possible to the commencement of the *regulatory control period*, proposed by the relevant *Transmission Network Service Provider*, and agreed by the *AER* (such agreement is not to be unreasonably withheld), or
    - (ii) a period specified by the *AER*, and notified to the provider within a reasonable time prior to the commencement of that period, if the period proposed by the provider is not agreed by the *AER* under paragraph 2.2(b)(i),
- and is also to be calculated in accordance with clauses 6A.6.2(c)(1), 6A.6.2(c)(2)(iii) and 6A.6.2(c)(2)(iv) of the *NER*.
- 2.3 In relation to clause 6A.6.2(d) of the *NER*:
- (a) the maturity period is a maturity of 10 years, and
  - (b) the bond rate is the annualised yield on Commonwealth Government bonds.
- 2.4 The equity beta ( $\beta_e$ ) is 0.80.
- 2.5 The market risk premium (MRP) is 6.5 per cent.
- 2.6 The market value of debt as a proportion of the market value of equity and debt ( $D/V$ ) is 0.60.
- 2.7 The credit rating level is BBB+.
- 2.8 The assumed utilisation of imputation credits ( $\gamma$ ) is 0.65.

### 3 Statement of regulatory intent on the revised WACC parameters—distribution

- 3.1 Paragraphs 3.2–3.8 set out the revised values, methods and credit rating levels adopted by the *AER* in accordance with clause 6.5.4(c) of the *NER* to apply to a *Distribution Network Service Provider’s building block determination* where the relevant *regulatory proposal* is submitted to the *AER* between 1 May 2009 and 1 April 2014.
- 3.2 In relation to the method to calculate the nominal risk free rate ( $r_f$ ):
- (a) it is to be on a moving average basis from the annualised yield on Commonwealth Government bonds with a maturity of 10 years,
  - (b) the period of time in which it is to be calculated is either:
    - (i) a period (‘the agreed period’), being one which is as close as practically possible to the commencement of the *regulatory control period*, proposed by the relevant *Distribution Network Service Provider*, and agreed by the *AER* (such agreement is not to be unreasonably withheld), or
    - (ii) a period specified by the *AER*, and notified to the provider within a reasonable time prior to the commencement of that period, if the period proposed by the provider is not agreed by the *AER* under paragraph 3.2(b)(i),
- and is also to be calculated in accordance with clauses 6.5.2(c)(1), 6.5.2(c)(2)(iii) and 6.5.2(c)(2)(iv) of the *NER*.
- 3.3 In relation to clause 6.5.2(d) of the *NER*:
- (a) the maturity period is a maturity of 10 years, and
  - (b) the bond rate is the annualised yield on Commonwealth Government bonds.
- 3.4 The equity beta ( $\beta_e$ ) is 0.80.
- 3.5 The market risk premium (MRP) is 6.5 per cent.
- 3.6 The value of debt as a proportion of the value of equity and debt (D/V) is 0.60.
- 3.7 The credit rating level is BBB+.
- 3.8 The assumed utilisation of imputation credits ( $\gamma$ ) is 0.65.