

# Response to the AER's "*Pathway to the 2022 rate of return instrument Consultation Paper*"

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Prepared and submitted by former members of the Consumer Reference Group (CRG) established as part of the AER's 2018 Rate of Return guideline Review:

Former CRG member	Organisational affiliation'
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## **General Comments**

We (former CRG members) welcome the AER taking the initiative to outline a complete process at this early stage for the development of the next guideline.

We question the value of any form of consultation (other than this initial consultation) being undertaken before a new CRG is created.

We are concerned that the proposed approach for the 2022 review seems to be presuming a simple continuation of the foundation model approach (incremental) and not considering other alternatives such as how to inform the decision from profitability analysis or investment records.

It is our view that the 2022 review should be broadened to consider such alternatives, particularly given the paucity of available data to calculate elements of the CAPM model, and the rapidly changing nature of the national energy markets, in particular electricity networks.

Consideration of such alternatives should be a key focus for the AER's Position Paper - High Level, to be published in early 2020.

A particular feature of the 2018 CRG process was the employment of a consultant to provide the drafts of the CRG's first submission, given resourcing and timing constraints. The CRG response to the draft decision was written by CRG members. We believe the CRG has the ability to write its own submissions and that the use of an independent "author" is not required provided sufficient funding is available to resource the CRG. Further, it is important that funding is sufficient to enable the CRG to access a suitably qualified consultant to advise it on technical issues when required.

A part of the AER's 2018 Rate of Return guideline Review CRG process was that CRG members represented a diverse range of consumer perspectives. Members were however appointed in their individual capacity and not as representatives of organisations they were associated with.

We recommend that approach be continued in the 2022 review process.

## Consultation paper questions – detailed responses

Former CRG members responses.

### *1. How could the CRG be adapted to improve their contribution to the review?*

The functioning of the CRG during the 2018 review involved a significant element of “learning as we go”, by the AER and by the CRG membership. Governance arrangements; the decision to provide submissions; the process for the development of submissions; the CRG’s role in evidence sessions and the focus areas for the CRG in general were but a limited number of the matters which were developed during the course of the review.

The recommendations which follow are based on what we observed worked and what did not work so well during that “learn as we go” process:

- An interim CRG team, comprising a Chair, Deputy Chair and (say) four other members be appointed by the AER as soon as possible ahead of the release of the AER’s high level position paper, scheduled for early 2020. The members of that team could be drawn from the previous CRG so there is sufficient initial understanding of the issues and the technical aspects to provide informed input.
- The role of the interim CRG be clearly defined ahead of the release of those appointments, to include provision of high level input to the foundation phase, including responding to the high level position paper; assisting the AER in the establishment of the new CRG, which would occur ahead of the active phase of the review and would include identifying the detailed role of the new CRG (as noted below); and formulation of a skills development program.
- The detailed role of the new CRG and the expected project timetable, reflecting the contents of and responses to the AER’s high level position paper, including CRG outputs, be refined ahead of the appointment of the new CRG and include objectives and deliverables.
- The new CRG to comprise a core group and a wider group. The core group would undertake more intensive activities and report back to the wider group on a less frequent but regular basis to ensure that the overall direction taken by the core group is reflective of consumer interests.
- The total number of CRG members should not be constrained but the previous membership of 15 is possibly at the upper limit of what might be considered a productive and manageable group.
- Members of the wider, non-core CRG with limited technical knowledge be provided with a comprehensive skills development program to ensure they have an appropriate understanding of regulatory processes relevant to the Rate of Return review; the RoR review process itself and the role of the CRG within that process.
- All core CRG members be subject to performance reviews at least every six months. Those members would have clear expectations set around their role and their performance would be assessed against those expectations, potentially by a selection panel as described in the response to question 2.
- Given the nature of the RoR review, being that of a project, it is important that the CRG Chair also assume the role of Project Manager for CRG activities, and develop and manage a CRG RoR project plan accordingly, in conjunction with the AER.
- A project budget be established by the AER and agreed with the CRG Chair. It is important that the budget be sufficient to fund all CRG activities, including payment of sitting fees, preparation time, review and writing time and reimbursement (or payment) of travel and

accommodation. It is also important that the budget be subject to regular review, contain sufficient contingency to avoid the need to formally seek increases, and be managed by the CRG Chair/Project Manager with the assistance of the AER.

- Funding and compensation arrangements for the CRG Chair be commensurate with this degree of responsibility.
- Development of submissions responding to AER requests and other inputs requiring CRG contributions be prepared by core CRG representatives with the necessary skills, coordinated by the Chair/Project Manager, and be finalised following review and endorsement by the full CRG.
- The CRG be supported by access to a suitably qualified technical resource from the AER and when necessary one suitably qualified consultant, preferably of its choosing, to advise on technical issues.
- The AER assign management level resources to work with the CRG, in particular the CRG Chair, and to be accountable for the AER's management of the CRG's involvement in the 2022 review, including the budget, as was the case in the 2018 review.

### *2. Is there anything that needs to change about the CRG nomination process?*

CRG members need to work collaboratively in the best interests of all consumers, not just the particular cohort that they may 'represent'. To that end we recommend that, as with the 2018 CRG, appointments of suitably qualified applicants be made in an individual capacity, not as representatives of organisations.

The nomination (recruitment) process for the new CRG should be sufficiently broad to create competition for the available positions and should reflect a strong consumer bias with easy access to informed consumer input.

As a group, the CRG must have sufficient technical understanding (not only of the rate of return issues but also of the way the market operates and the role of consumers in its operation) as well as a strong understanding of consumers' long term interests.

Active engagement by the AER with relevant consumer representative bodies, at national and state level, seeking nominations for positions as outlined in a suitable role description, is one means by which this might be achieved.

The call for nominations should be explicit about the competencies required (noting our response to question 3), the time commitment expected and the reimbursement arrangements.

If the recommendation in response to question 1 on the early appointment of the Chair and Deputy Chair is adopted the AER might develop an explicit selection panel that would include the relevant AER General Manager Consumers and Markets, the General Manager Networks Financing and Reporting, and the Chair of the CRG. It could be expected that selections would be made based on written submissions and AER research and would not involve interviews by the panel.

### *3. What characteristics should be sought for CRG members?*

There should be no minimum requirement of technical knowledge for membership, rather the demonstrated ability to deal with complex issues in a constructive way should be a mandatory requirement.

A first hand, intimate knowledge of consumer experiences with the delivery of essential services, especially electricity and gas, and the impacts of price, reliability and quality of service reflected in

that experience should be considered equally important as an understanding of the technical dimensions of RoR and how that flows through to prices, noting the skills development suggested at point 1 above.

*4. What should the CRG's main role be when in the 2022 process? Should the CRG's main role be to provide technical submissions or more customer focused submissions to the review process?*

Noting that we believe it is appropriate to consider alternatives to the foundation model approach, the role of the CRG should include the provision of both technical submissions and customer focussed submissions.

The role of the consumer in the functioning of Australia's energy markets is changing. As noted by the AEMC in its overview of *Designing the Grid of the Future* – “The way customers are using the grid is changing. That means we must also change the way we regulate and operate the grid and the way consumers access, pay for and are rewarded for the services they provide to the grid”, and the emerging role of the “prosumer” – producing and consuming energy - mean that active and informed consumer involvement in all aspects of the energy market is critical to the ongoing success of that market”.

The RoR paid for by consumers and received by network investors will have a major bearing on how energy networks are developed in the changing market, and consumers can be considered to have a shared and ongoing investment interest. The changing nature of the energy market will require investment in assets different to those which make up a traditional energy network, and now involves direct investment in the market by many consumers who may have a different view to consumers that are more passive.

We believe that there is considerable merit in continuing the dialogue between consumers, network owners and operators, investor groups and retailers, guided by a clear and agreed set of objectives. It is important that the budget noted at point 1 above provide for such engagement.

We also recognise that no matter how detailed the RoR process is, the AER will be left with the need to exercise judgement. An explicit benefit the CRG provided in the last review was the clarity that consumers were prepared to take a risk on reduced reliability in exchange for lower prices and that this informed the AER's judgement about what point choice to make in the ranges for various parameters.

Combining technical analysis with consumer experience, CRG submissions added a new perspective that helped inform and improve the AER's decision.

*5. What scope is there for the CRG and CCP to work collaboratively to jointly contribute to the 2022 process?*

The role of the CCP is to provide input and challenge the AER on key consumer issues during a network determination, to help improve the AER's decisions. We note there is a review of the CCP currently in progress.

The role of the CRG is to provide direct and ongoing feedback to the AER during the RoR instrument development, and to facilitate broader consumer participation and engagement. That role needs to be clearly defined, as noted in section 1 above.

The two roles of CCP and CRG are both valuable, but distinct. The CRG should operate independently of the CCP, but be able to draw on the work and experience of CCP members as appropriate.

We believe the broad membership of the CRG should be drawn from non-CCP members, however we believe there is a case for CCP members not involved in the CCP subgroup addressing the RoR instrument taking up key roles on the CRG, utilising the skills and experience gained in their CCP activities and being cognisant of the separate role they would perform as part of the CRG.

*6. Does the AER's support of the CRG need to change ahead of the 2022 review? If so, how should that support change?*

The level of support provided by the AER for the 2018 was appropriate and valued by the CRG, noting that the CRG was established later in the process than ideal, and both the AER and the CRG grew into their respective roles in making the CRG work effectively.

Funding and the allocation of an appropriate technical resource are discussed at section 1. Access to broader AER specialist resources, as was the case in the 2018 review, should continue. As noted, it is important that funding be sufficient to enable the effective operation of the CRG, including the engagement of independent expertise when required.

*7. Do the IRG and RRG need to be altered to enable them to be able to more effectively contribute to the development of the Instrument? If so, what changes should be made to the groups?*

We are of the view, as noted in section 1 above, that continuation of the dialogue between consumers and investors (via the CRG and IRG) based on an agreed set of objectives and outcomes would be valuable.

The roles of each of those groups should be more accurately defined, beyond the current requirement "to provide direct and ongoing feedback to the AER during the guideline development", along with the expected outcomes from interactions with the CRG and with Networks.

*8. How could the concurrent evidence sessions be adapted to improve discussion on topics?*

Our understanding of the concurrent evidence process is as follows:

- When expert evidence is tendered in contested proceedings, traditionally each party will call one or more expert witnesses whose evidence mostly supports that party's case, and the relevant arbiter must evaluate the expert evidence (usually conflicting) provided.
- Concurrent evidence is a means of securing expert evidence with more input and assistance from the experts themselves in lieu of their perceived role as being inherently, even if not consciously, biased to the case of the party calling them.
- After each expert has prepared his or her evidence, there is a conference with the objective of the production of a joint report on the matters about which they agree and those on which they disagree, giving short reasons as to why they disagree.
- Ideally, this process will identify that the experts agree on everything that each has said in his or her reports, on the basis that the opposing expert accepts the assumptions which the other has used.
- Identifying the right questions to put to the experts is a key part of the process, and one in which the parties to the proceedings (in this case the RoR review) should play a role in jointly determining.

As detailed in the Brattle interviews, application of the concurrent evidence process as executed in the 2018 review was flawed on a number of fronts.

To address those flaws for the 2022 review we recommend that all experts be commissioned and paid for by the AER. We expect implementation of this recommendation would be accompanied by numerous changes at a detailed level. We recognise the experts may have consulted for parties prior to the concurrent sessions and may provide advice after the sessions.

For the sessions, it is important that the experts provide technical advice on the issues at hand and not be advocates for particular stakeholder positions. Reflecting this expectation, the experts' preparation and participation should be funded by the AER.

Nominations for the role of experts to participate in the concurrent sessions should come from the ENA, CRG, IRG, RRG and AER. We recommend the AER select from these nominations to ensure a broad breadth of views including those that might not come from the "prevailing paradigm".

*9. At what points in the process would the concurrent evidence sessions aid the most?*

We believe the proposed timing is appropriate, subject to our responses to questions 10 and 11 below.

*10. What could be done to better assist the concurrent evidence sessions to fulfil their role? Do the number of rounds be increased?*

As noted in our response to question 8 above, we expect there will be numerous changes at a detailed level to the concurrent evidence process as executed in the 2018 review, however at a high level we recommend the process adopted for the 2022 review reflect the process outlined in our response to question 8.

To assist in focusing on the important issues, the experts should be tasked with responding to a set of issues/questions developed by the AER which cover the major elements needed to be examined to develop the RoR instrument. Where the experts agree, these aspects need not be further debated so that the concurrent evidence sessions only focus on those aspects where there is disagreement. Every attempt should be made to allow the experts to reach agreement where there is conflict.

In particular, the value of the final report from the concurrent expert evidence sessions should be that the conclusions outlined in that report are capable of being considered by the AER when exercising its judgement, in such a manner that the AER's conclusions in its Draft (and Final) instruments can be directly reconciled to the experts' conclusions.

*11. Do stakeholders consider the Joint Expert Report was useful to the process? How could it be improved?*

We refer to the feedback provided to the Brattle interviews. In particular we agree with the suggestion that a joint report be written prior to the concurrent expert sessions, based on written submissions provided by the experts responding to the questions posed, identifying the main areas of agreement and disagreement, which would then more efficiently allocate time to the issues of disagreement while everyone was present at the sessions.

On conclusion of the concurrent evidence sessions it is important that a final report be produced which highlights aspects where there is agreement and where there is residual disagreement, and reasons for the source of the disagreement, for consideration by the AER in formulating its Draft (and Final) Instruments.

One reason for ensuring that the AER contracts for the experts in the concurrent evidence component of the RoR review process is to ensure that experts are available and funded for the end-to-end concurrent evidence process, including time to review and comment on the final report.

*12. Are there any adjustments that could be made to the Independent Panel that would assist it in undertaking its role?*

We note the detailed responses to the Brattle interviews. Our view is that the primary role of the Independent Panel should be that of a probity review, confirming that the interests of all stakeholders have been well represented and considered in the RoR review process.

The terms of reference for the Independent Panel should be made available for comment early in the review process – for instance as part of the May 2021 Consultation Paper.

The opportunity should be available for parties to the proceedings to make submissions to the Independent Panel, highlighting aspects of the reasoning in the Draft which the parties would particularly like the Independent Panel to include in its review.

Consistent with many court practices these submissions should be constrained in length (such as no more than four pages) and should not seek to introduce any new evidence.