Contact: Leigh Mayne
Phone no: (03) 6270 3691
Our Ref: NW30195735

Your Ref: email Mark McLeish, 29 June 2011

30 June 2011

Mr Warwick Anderson
General Manager
Network Regulation Branch
Australian Energy Regulator
GPO Box 3131
CANBERRA ACT 2601

Attention: Mark McLeish

Dear Mr Anderson

EQUITY RAISING COSTS

Aurora confirms its intention to seek equity raising costs as part of its Regulatory Proposal and provides the following information in support of that claim.

In its final decision on the Victorian electricity distribution network service providers the AER has accepted that equity raising costs are a legitimate cost for a benchmark efficient firm only where equity funding is the least cost option[1]. The AER further noted in this decision that:

> *"... A DNSP should only be provided with an allowance for equity raising costs where cheaper sources of funding, such as retained earnings, are insufficient, subject to the gearing ratio and other assumptions about financing decisions being consistent with regulatory benchmarks."*

The AER considers that the best estimate of the direct costs of raising equity varies depending on the method employed:

- 0 percent of equity obtained via retained earnings;
- 1 percent of equity obtained via dividend reinvestment plans; and
- 3 percent of equity obtained via external seasoned equity offerings (placements and rights issues).

[1] AER, Final decision – appendices, Victorian electricity distribution network service providers, Distribution determination 2011-2015, October 2010, pp 504.

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The AER applies a benchmark cash flow analysis to determine the amounts that will be available from retained earnings, the amounts reinvested via dividend reinvestment plans and the amount of external equity required for the forthcoming regulatory control period from seasoned equity offerings. Each component is summed and amortised over the weighted average standard life of the DNSPs' RAB to provide the equity cost allowance associated with forecast capital expenditure in the regulatory control period.

Aurora has adopted the AER's preferred methodology and the benchmark cash flow analysis has determined that an equity raising allowance is required for the forthcoming regulatory control period. This allowance is shown in Table 1 and has been added to the RAB at the start of the regulatory control period, amortised over the weighted average standard life of Aurora's RAB. Aurora has included this allowance in its PTRM.

Aurora also notes that the inclusion of equity raising costs within the PTRM results in a slight revenue adjustment to its Regulatory Proposal and provides the AER with amended revenue and pricing tables for its Regulatory Proposal as an attachment to this letter.

If you have any questions, please contact Leigh Mayne on the above number or via email at leigh.mayne@auroraenergy.com.au.

Yours sincerely

Kim Rosinski
Commercial Manager
Aurora Energy

Table 1: Equity raising costs

Cash Flow Analysis							
	2012-13	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**Total**	
Dividends	45.3	49.2	48.4	48.7	49.2	240.8	Set to distribute imputation credits assumed in the PTRM
Dividends reinvested	13.6	14.7	14.5	14.6	14.8	72.2	30% of dividends paid
Cost of dividend reinvestment plan	0.1	0.1	0.1	0.1	0.1	0.7	Dividends reinvested multiplied by benchmark cost (1%)
Capex funding requirement	143.9	146.1	145.7	144.6	150.2	730.5	Forecast capex funding requirement
Debt component	53.4	50.6	51.5	54.6	58.1	268.2	Set to equal 60% of RAB increase (not capex)
Equity component	90.5	95.5	94.3	90.0	92.1	462.4	Residual of capex funding requirement and debt component
Retained cash flow available for reinvestment	75.1	72.2	74.2	75.1	77.2	373.8	Includes dividends reinvested
External equity requirement	15.4	23.3	20.0	14.9	14.9	88.6	Equal to equity component less retained cash flows
External equity raising costs	0.5	0.7	0.6	0.4	0.4	2.7	External equity requirement multiplied by benchmark direct cost (3%)
Total equity raising costs	0.6	0.8	0.7	0.6	0.6	3.4	Sum of dividend reinvestment plan cost and external equity raising cost
Total Equity Raising Costs ($'m, 2011-12)	0.6	0.8	0.7	0.5	0.5	3.1	To be added to the RAB at the start of the regulatory control period