

4 May 2012

Mr Moston Neck
Director Network Regulation
Australian Energy Regulator
PO Box 12241, George Street Post Shop,
Brisbane Qld 4003

Dear Mr Neck

FORM OF REGULATION TO APPLY FOR THE 2014 TO 2019 REGULATORY PERIOD

Endeavour Energy is pleased to provide you with its comments on the AER's *Discussion paper – Control mechanisms for standard control electricity distribution services in the ACT and NSW*. The discussion paper has sought views on a range of questions to assist the AER in developing the Framework and Approach paper required to be under the National Electricity Rules (NER).

Endeavour Energy has considered the available forms of regulation under the NER that may be applied to standard control distribution services, and the AER's initial preference for a revenue cap.

However, Endeavour Energy believes that the focus of the form of regulation should be on efficient and predictable prices for consumers. Indeed, Endeavour Energy has publically committed to controlling network price increases to around CPI for the next seven years. As set out below, Endeavour Energy is of the view that the Weighted Average Price Cap (WAPC) form of regulation is the form of regulation most likely to achieve pricing stability for customers over the 2014 to 2019 regulatory period.

There are two primary forms of regulation or control mechanisms that are applied in the National Electricity Market (NEM) being revenue caps and WAPCs.

Revenue caps were last applied in NSW between 1999 and 2004. This form of control ensures that the DNSPs recover exactly the revenue determined by the regulator at the time of the determination, no more and no less in NPV terms. Any under or over recovered revenues are recovered or returned back to customers in subsequent years by adjusting the revenue targets. Some of the primary reasons for abandoning the revenue cap form of regulation in 2004 was the failure to deliver pricing stability and the inability of the form of regulation to adjust revenues/prices that reflected the underlying drivers of costs to the DNSPs at that time.

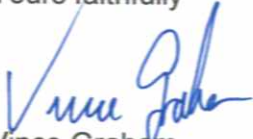
The WAPC form of regulation does not provide any guarantee of revenues, and to the degree that volume changes differ to those forecast by the regulator the DNSP will bear the revenue volatility, however customers do not face pricing volatility. The move to the WAPC form of regulation was accepted by IPART in 2004, in part because the revenues were expected to move in a direction consistent with the underlying cost movements of the DNSPs, using energy throughput changes as a proxy measure of cost changes.

As set out in Table 4.1 of the AER discussion paper, the WAPC has increased incentives to set efficient prices, the DNSP bears the risks of volume variances which are directly linked to the high level of pricing certainty provided to customers.

Endeavour Energy also notes that continued application of the WAPC would minimise transitional issues between regulatory periods. In addition the WAPC is the most prevalent form of regulation applied to distribution networks in the NEM, and therefore continued application would serve to maintain the current levels of national consistency in economic regulation.

If you would like to discuss these comments further, please contact our acting Manager Network Regulation, Mr. Frank Nevill on 02 9853 6598.

Yours faithfully



Vince Graham

Chief Executive Officer