Energy Action Group

Presentation to ACCC TransEnd Predetermination Conference

Hobart 17th October 2003

Regulated Entities are Unique

- Minimal risk of non payment.
- Far lower risks than almost all listed companies in a competitive market.
- A relative high degree of freedom of action once a determination is made. “The light hand.”
- Indexed against inflation and have a real asset base. Unlike all other companies who use DAC.
- Generous Regulatory Determinations fail to deliver competitive outcomes to consumers

Competitive Outcomes

- One of the important objectives for the ACCC is to emulate competitive outcomes in Determinations.
- A Determination can be seen as a benchmark.
- Performance by a monopoly business that provides results better than the benchmark get rewarded while worse results get penalised over the regulatory cycle.

Some simple issues

- EAG agrees that if ACCC is going to use 5 year regulatory resets then all of CAPM should be reviewed at the time. This approach justifies using the 5 year bond rate.
- The Transco’s have been honing and refining their regulatory approach and incrementally creeping the revenue upwards raising their revenue requests, determination after determination. The ACCC should be trying to minimise the process of regulatory revenue creep.

Consistency

- ACCC needs to co-ordinate its Gas and Electricity Determinations along with its submissions to the Australian Competition Tribunal.
- Why suggest that you may have erred on the side of generosity and then write a Determination that repeats a generous outcome.
- The ACCC Statement of Facts Issues and Contentions filed with the Australian Competition Tribunal on the 11th June 2003 suggests that a lower equity beta number could have been appropriate in the GasNet Determination. P 123 Para 334,

Weighted Average Cost of Capital

The ACCC draft determination fails to address the following:

- Market risk premium of 6% has been ACCC’s mantra. In the UK and US regulators have set the MRP at 3.5%. Why are Australian customers paying a higher MRP when there is no evidence that the Australian financial market is less efficient than the UK and US market.
- Equity Beta of 1 means a risk profile similar to the general market. With 99% of revenues guaranteed, TE market risk is no where near that of the market.
- The ACCC commissioned Allen Consulting report indicated an Equity Beta of around 0.5.

Weighted Average Cost of Capital

The ACCC draft determination fails to address the following:

- Why is the ACCC exploring beta options as low as 0.35 in the current discussions on the draft SRP? Yet is still using a unity beta!
- Customer groups have put in representations since June 2002 in both gas and electricity determinations yet there has been no ACCC response. How much notice does the ACCC take of customer group's input?

Why ?

Transparency

- Poor/no justification in the Draft Determination as to why an aging network similar to PowerNet, TransGrid and ElectraNet with minimal load growth has such a significant capex expenditure and increase in the Regulated Asset Base other than to trade energy over Bass Link.
- Why does Aurora have a lower Capex than TransEnd
- Particularly given the role of Tasmanian Treasury in asset revaluations

Performance Standards

- Need for TNSPs to be provided with positive and negative incentives especially for service standards that relate to the impact on the energy market, eg due to outages for scheduled maintenance given the potentially large impact, relative to transmission costs, that the actions of transmission companies can have on regional energy prices.
- We note that ACCC is moving (too slowly) to introduce some service standards for TNSPs and suggest that they apply these to TE, or at least put TE on notice that they will once they are finalised
- Performance incentives would be more effective if applied uniformly across the NEM.
- Undertaking revenue reviews for all regulated TNSPs at the same time would facilitate this. Current arrangement of piecemeal review of individual TNSPs at different times is costly, inefficient and reduces the benefit to end users of regulation.

Efficiency

- There appear to be minimal /no incentives in the Draft Determination to encourage TransEnd to make any efficiency gains.
- No alternatives like DM embedded generation and inter-fuel substitution were promoted or considered in the TransEnd Application nor the Determination.
- Another failure for alternatives like Demand Management and embedded generation.

Performance Incentives

- In previous regulatory decisions as well as in this draft decision, the ACCC has only placed a maximum of 1% of the allowed revenue at risk for under performance.
- We submit that is insufficient incentive for improved performance with 99% of revenue guaranteed regardless of the level of performance.
- We applaud the ACCC’s finding that Transend’s proposed service standard benchmarks are insufficiently challenging and have suggested alternative targets.
- Failure to reach these more challenging targets however will only reduce Trensend’s return on equity by between 0.2% - 0.3% (based on the AR of $95M).

Regulatory Asset Base – (Why We Are) RAB(id)

- Asset base on 1 July 1998 was $333.25M, forecast by OTTER to rise to 468.71M by 30 June 2002, including a forecast period capex of $202.7M.
- Transend's 2002 Annual Report states that actual capex between 1999 and 2002 amounted to just $151.4M. Yet RAB has increased to $542.2M.
- Regulatory Asset Base has been unreasonably revalued from level accepted by OTTER.
- Increase in RAB represents over 10% of TUoS (from WACC)
- An unacceptable conflict of interest exist with the Tasmanian Government's role in approving the revaluation.
- ACCC has failed customers by meekly accepting this unreasonable revaluation.