

21 August 2012

Mr Tom Leuner
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Via email: tom.leuner@aer.gov.au

Dear Tom

AER RIT-T Cost Thresholds Review

Grid Australia provides this submission in response to the Australian Energy Regulator's (AER's) Issues Paper on the Cost Thresholds Review for the Regulatory Investment Test for Transmission, released in July 2012.

Consistent with clause 5.6.5E of the National Electricity Rules (the Rules), Grid Australia understands that the purpose of the review is to determine whether the current threshold values applicable to the RIT-T should be changed as a result of movements in input costs since 1 July 2009. Grid Australia makes the following comments in response to the issues for consideration raised by the AER.

1. Price Indices

Grid Australia agrees with the AER that the Consumer Price Index (CPI) is not representative of the costs facing the electricity transmission sector and, therefore, should not be adopted for the purposes of escalating the RIT-T thresholds. By comparison, Grid Australia considers that the Producer Price Index (PPI) is a more appropriate indicator of cost movements in the sector given that it has been constructed to measure changes in the price of inputs to, or outputs of, a particular economic sector.

For the purposes of the three yearly threshold escalation review, Grid Australia considers it would be appropriate to adopt a single (or an average of broader) PPI indicators. For example, measures such as building construction in Australia or non-residential building construction in Australia. Some of the key benefits in adopting a broader, Australia wide measure is that:

- the thresholds applied to the NEM-wide RIT-T are not unduly influenced by State specific factors for the purposes of a three-yearly review;
- for administrative simplicity, the AER can take a broad view of cost changes; and

- the measure is objective (published by the Australian Bureau of Statistics) and is readily and publicly available on a regular basis.

2. Cost Movements

Steel and aluminium represent major components of costs in the construction of electricity transmission infrastructure. In general terms, aluminium and steel each comprise of the order of 15-30% of transmission line costs.

The figures below illustrate the movements in the steel and aluminium indices sourced from CRU and the London Metals Exchange (LME).

Figure 1: CRU Steel (converted to AUD/t)

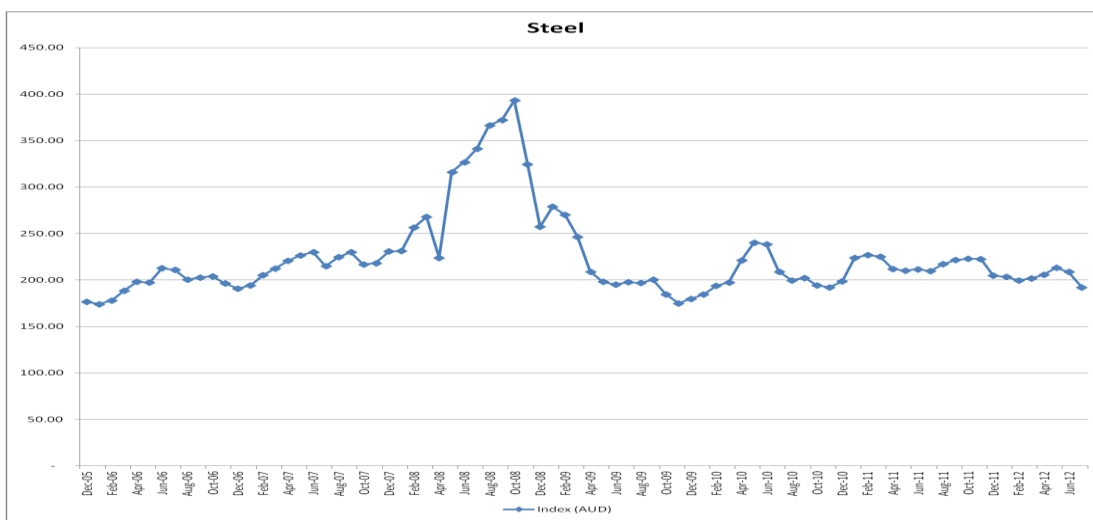
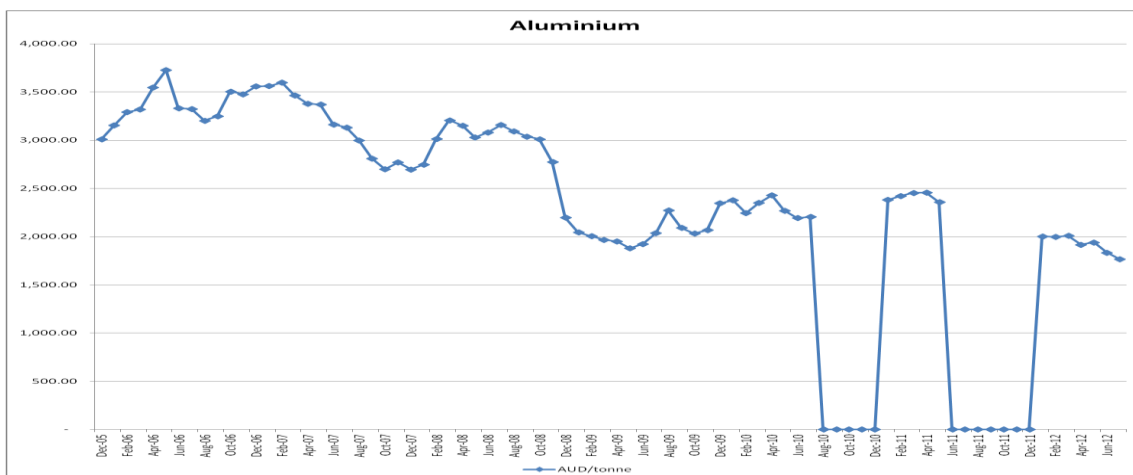


Figure 1 shows that while steel prices have ranged between approximately \$175 and \$240/t, since mid-2009, they have remained relatively stable in Australian dollar terms, trending around just over the \$220/t mark.

Figure 2: LME Aluminium Index (converted to AUD/t)



Note: Absence of data in 2010 and 2011.

Figure 2 shows that in the last three years, aluminium prices have also been relatively stable, averaging at just over \$2,000/t.

Grid Australia considers that in assessing cost movements, rather than adjusting for cost changes within a three year window (i.e. 2009–2012), the AER should consider whether there has been a material change in costs in this period relative to the base year in which the RIT T thresholds were established. Such an approach would minimise the impact of any short term volatility.

3. Approach

Grid Australia understands that the purpose of the review is to ensure that the thresholds keep pace with changes in costs over time in the event input costs vary significantly in the period under consideration. The AEMC also considered that indices could be used as the basis for escalation and that market consultation guide which is the most appropriate¹, should it be decided that the thresholds need to be changed at all.

From an overarching perspective, Grid Australia considers that the AER should take a proportionate approach to determining whether or not to change the current thresholds. In other words, to the extent that there has been no material change in costs since the current \$5m and \$35m thresholds were established, there should be no change in the thresholds.

Where the case for change of a particular threshold has been demonstrated, Grid Australia is of the view that that this figure should be rounded to the nearest \$1m for simplicity and, be consistently applied across the remaining RIT-T elements of the Rules.

If you have any questions or require clarification of any aspect of this submission, please in the first instance contact Jennifer Harris on (07) 3860 2667.

Yours sincerely



Rainer Korte
Chairman
Grid Australia Regulatory Managers Group

¹ AEMC, Final Rule Determination, National Electricity Amendment (Regulatory Investment Test for Transmission) Rule 2009, 25 June 2009, p21 and p64.