AUSTRALIAN ENERGY REGULATOR

MINUTES

Minutes of the predetermination conference on the AER's draft decision on Powerlink's transmission revenue proposal—1 July 2012 to 30 June 2017

Location: Mercure Hotel, Brisbane

Date: Wednesday 14 December 2011 (9.30 am to 11.30 am)

Forum Chair: Warwick Anderson, General Manager, Network Regulation, Australian Energy Regulator

Attendees: the meeting commenced with 36 registered attendees and 6 AER staff. The attendance list is available at www.aer.gov.au.

Summary of forum

A summary of the discussions that occurred at the forum is under each agenda item.

1. Opening remarks by the Chair

Warwick Anderson (Chair) opened the forum.

- Introduction, outline of agenda and procedural issues of the forum.
- The purpose of the forum is for the AER to explain its draft decision on Powerlink's revenue proposal for the regulatory control period 1 July 2012 to 30 June 2017.

2. Presentation by Andrew Reeves, Chairman, AER

The Chair invited Andrew Reeves (Chairman) to present the AER's draft decision. The presentation slides can be found at www.aer.gov.au.

Andrew Reeves

- Provided an outline of the regulatory framework within which the AER's draft decision is made.
- Noted consultants engaged by AER to assist with review of technical and economic matter contained in Powerlink's revenue proposal.
- Set out the impact of the AER's draft decision on indicative transmission charges and potential retail price impacts.
- The AER has not accepted all of Powerlink's revenue proposal and has determined a revenue allowance 23 per cent below Powerlink's proposal. The main drivers for the

difference between the proposal and draft decision are the lower cost of capital parameters together with reduced capital expenditure (capex) and operating expenditure (opex).

- The AER's draft decision included a lower regulatory asset base, driven by the reduced forecast capex, depreciation and lower inflation rates used by AER.

- The AER's draft decision included a lower capex allowance than Powerlink's proposal, driven by the reduced demand forecast, 500 kV projects and cost estimation risk factors.

- The AER's reduced demand forecast is driven by the different assumptions used by the AER to arrive at its alternative demand forecast, which included different population, electricity price and energy trends assumptions as well as different temperature correction methodology. Andrew acknowledged the difficulties involved with producing demand forecasts.

- The AER's draft decision included a lower cost of capital (WACC). This was influenced by the parameters prescribed in the 2009 WACC review (which are therefore fixed), the averaging period and fluctuations within financial markets and the availability of long term bonds in the Australian market.

- The opex allowance in the AER' draft decision focused on revealed costs and incentives to provide starting point assessment. Powerlink's proposed opex allowance was reduced because of network growth and real cost escalation.

- Transmission Network Service Providers have responded well to the Service Target Performance Incentive Scheme incentives.

- The AER approved Powerlink's proposed pricing methodology and the AER amended Powerlink's negotiated services criteria.

- Powerlink may submit a revised proposal in response to draft decision by 16 January 2012. Submissions on the AER's draft decision and Powerlink's revised proposal are due by 20 February 2012. The AER is required to publish a final decision by 30 April 2012.

3. Presentation by David Headberry, Energy Consumers Group operating in Queensland (9.55 am to 10.20 am)

The Chair invited David Headberry, Energy Consumers Group operating in Queensland ("the Group") to present the group's views on the AER's draft decision. The presentation slides can be found at www.aer.gov.au.

David discussed concerns held by the Group on the AER's draft decision. David reported that in the Group's opinion, the draft decision allows Powerlink:

- more revenue than Powerlink has demonstrated it has historically required

- greater allowances for the cost of debt and opex than Powerlink has shown it needs

- to meet its future service performance targets, given its current performance

David also considered that the draft decision does not allow for the impact on consumption and demand that the higher prices permitted Powerlink would result in.

Overall David noted that the AER draft decision gave a better outcome for consumers than the Powerlink proposal, but still resulted in higher costs than were warranted based on Powerlink's past performance.

4. Question and comments from attendees

Roman Domanski (Energy Users Association of Australia (EUAA)): welcomed draft decision; noted incentive on TNSPs to over forecast expenditure requirements; acknowledged Powerlink's assistance in explaining to EUAA their revenue proposal; recommended AER maintain a rigorous assessment for the revised proposal before publishing final decision.

Mate' Ataata (EUAA): How was the $1.40 increase in transmission charges calculated?

Andrew Reeves (AER): Responded that the $1.40 increase in charges is indicative only and is based on assumed energy growth taken from Powerlink annual planning report and pro-rated on AER's peak demand reductions. Noted revenue cap control mechanism leads to "under and overs" account.

Brian Carrick (QTC): How did AER satisfy itself that data used for cost of capital was robust. Did AER consider putting out issues paper to explain its new approach to setting WACC?

Andrew Reeves (AER): Noted general industry and investor concerns about WACC. The AER's approach to assessing WACC is based on available financial market information and there will be a difference between the draft and final report because of changes in the financial market information in the intervening period. AER has been on record in the past discussing possible changes to the approach to assessing financial instruments.

Merryn York (Powerlink): How would the AER like Powerlink to test easements? For instance, should the test involve going out to the community to foreshadow potential easements acquisition?

Andrew Reeves (AER): Recognised this is a difficult issue for which there is no hard and fast answer, but the effort that goes in should be commensurate with the size of the project/program. Andrew clarified that the AER is not advocating the running of a "dummy" process but that assessment of corridors and community concerns is important. The AER did not see evidence that appropriate non-network solutions had been canvassed with the 500kV projects. Andrew noted that the interaction of TNSPs' requirement to meet planning laws and the role of the economic regulator in approving major projects expenditure was discussed at the recent Standing Council on Energy and Resources Meeting.

Roman Domanski (EUAA): EUAA members were frustrated with elements of the WACC, such as the Tasmanian distributor, Aurora Energy, receiving a market risk premium (MRP) of 6 per cent in its draft decision, while the MRP for the Powerlink decision was 6.5 per cent.

Andrew Reeves (AER): Noted that the WACC review two years ago locked in certain parameters for the ensuing five years. The AER made the decision to move to an MRP of 6.5 per cent back then on the basis of instability in global financial markets at the time.