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Level 18, 215 Adelaide Street
Brisbane Qld 4000

GPO Box 1450
Brisbane Qld 4001

Phone 07 3233 9100
Fax 07 3211 9339

policy@nationalseniors.com.au

Mr Warwick Anderson
General Manager
Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Dear Mr Anderson

Issues paper: Review of the rate of return guidelines

National Seniors welcomes the opportunity to make a submission in response to the rate of return guidelines issues paper released 31 October 2017.

National Seniors represents the interests of older Australians. Older Australians value affordability and reliability and recognise that network regulation plays an important role in striking a balance between them.

The sharp increase in the cost of electricity over the past decade has created significant concern among older Australians, especially those on limited fixed-incomes.

There are legitimate concerns that “gold plating” by network businesses has skewed the balance between price and reliability, leading consumers to pay more than what is required to deliver reliable sources of energy to consumers.

While generation, wholesale and retail elements of the energy market should share part of the blame for increased prices, there is clear evidence that overinvestment in network infrastructure has been a major contributor to rising electricity prices.

Most recently, for example, the Australian Competition and Consumer Commission, has stated that there has been an overinvestment in network infrastructure which has locked-in inflated prices for decades to come¹.

What is most concerning for consumers is that overinvestment in network infrastructure was facilitated by the very regulatory framework used to set the amount of revenue that monopoly network businesses can recover from consumers.

¹ Australian Competition and Consumer Commission 2017. *Retail Electricity Pricing Inquiry Preliminary report* 22 September 2017

While consumers accept that network businesses require an adequate rate of return to ensure ongoing investment in energy infrastructure in order to deliver a reliable, safe and secure supply of energy, they also expect this is done at least cost.

Overinvestment in infrastructure and the subsequent rise in costs undermines consumer's faith in the regulatory process, fuelling distrust and anger toward government and energy businesses alike.

Given the extraordinary rise in the cost of energy over the past 10 years it is unclear if consumers would agree that the current regulatory approach promotes economically efficient investment in and operation and use of electricity/gas services.

The current approach has little relationship with economic efficiency because it does not demonstrate whether consumers are paying more for the cost of energy than they need, rather it estimates an adequate return for network business as a proxy for efficiency.

Unfortunately, the guideline does not enable estimation of the economic efficiency of network businesses. While profitability analysis is currently underway this evidence will unlikely have any material impact on the rate of return guidelines review – which is disappointing.

National Seniors would like to see significantly more work done to estimate the economic efficiency of network businesses as part of the rate of the return process but this will rely on adequate resourcing of AER and consumers to counterbalance the influence of network businesses.

National Seniors is also very troubled that significant contestation will occur over elements of the rate of return guidelines as part of this review. In particular, we are concerned that data required to settle these debates is lacking and open to interpretation and bias. It is also disappointing that network businesses are not more forthcoming with reliable data to support an economically efficient rate of return.

What is most concerning is the fact that debates about the guidelines occurs within power and resource asymmetries which significantly disadvantage the regulator and consumers. Given the technical and contested nature of these debates, we believe that both the AER and consumers/consumer representatives require significantly greater resourcing.

It is particularly galling to consumers that network businesses have amassed the financial, technical and legal capacity to challenge rate of return guidelines (and decisions made by the AER when applying the guidelines) using the excessive profits generated directly as a result of the application of regulations.

Network businesses have a direct economic interest in maintaining a process which is subjective, uncertain and open to expert discretion as this opens up opportunities to challenge decisions made by the AER (as has been done through the Limited Merits Review process). While the LMR process has now been closed off through legislative change there is still the opportunity to challenge decisions through judicial review.

National Seniors believes that because network businesses participate in regulated monopoly markets and receive significant financial benefits as a result of this

regulation, there should be greater obligation and onus on demonstrating the economic efficiency of these investments.

Furthermore, we also believe that network businesses should be required to assist in the provision of relevant information required to demonstrate the economic efficiency of a network business as part of the regulatory process.

The existence of clear evidence demonstrating the economic efficiency of network businesses will give reassurance to consumers that regulations are operating effectively to deliver on the long term interests of consumers.

Yours sincerely

Brendon Radford
Senior Policy Advisor