



Pathway to the 2022 rate of return instrument

Position paper

May 2020

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1 Background

The AER is the independent economic regulator of monopoly gas and electricity networks in each Australian State and Territory (except WA). We are guided in our role by the national electricity and gas objectives set out in the National Electricity Rules (NER) and the National Gas Rules (NGR). These objectives focus on promoting the long term interests of consumers.

In December 2018, we made our Rate of Return Instrument (2018 Instrument). This followed a process of extensive stakeholder consultation including new steps that had not been taken by us in any previous review. As a result we were keen to receive feedback on the process, including the new steps, in order to ensure each review is as effective as possible. Having heard feedback from stakeholders, we are now forming a work pathway to the 2022 rate of return review (2022 review).

This position paper is the next step towards the determination of the 2022 Rate of Return Instrument (2022 Instrument). It sets out our views on the process we will undertake to produce the 2022 Instrument, rather than the substantive rate of return issues. Our intended timelines are set out in section 4 below.

1.1 Our exercise of judgement

We develop and apply the rate of return instrument in accordance with the requirements of the NER and NGR.¹ It sets out how we will calculate the allowed return on debt, return on equity and the value of imputation credits (gamma) for the duration over which the instrument applies.

We are the decision maker in the rate of return instrument process. These decisions are made under uncertainty and therefore require the exercise of judgement when considering the evidence. The decisions must satisfy the relevant laws and rules which state:²

“The AER may make an instrument only if satisfied the instrument will, or is most likely to, contribute to the achievement of the national electricity/gas objective to the greatest degree.”

Estimation of the rate of return is complex and contentious, and the rate of return is a material driver of regulated revenue. The instrument is binding, and as such it is important that our review process provides a high degree of transparency and replicability. We will take measures to inform ourselves of relevant evidence and then review and test the available evidence when coming to a judgement. We will actively consult with stakeholders.

We will be transparent in our reasoning and provide detailed explanation. We will strive for predictability and replicability. You may not agree with our decision but you should be able to understand how we have made it.

¹ NGL, chapter 2, part 1, division 1A; NEL, part 3, division 1B.

² NGL, chapter 2, part 1, division 1A, cl. 30D(3); NEL, part 3, division 1B, cl. 18(3).

1.2 Decisions on the 2022 review process

This position paper sets out the process for the 2022 review. In deciding on this process we have been guided by:

- Legislative requirements. Certain steps and milestones in the review are required by legislation and each of these has been included. However, the legislation is not prescriptive about how these steps should be undertaken, so we have taken account of stakeholder views and our previous experience in determining the shape of these steps to maximise their value.
- Stakeholder submissions. In response to our consultation paper in late 2019 we received a number of detailed submissions from stakeholders and suggestions on how to improve the process. We also engaged The Brattle Group to interview stakeholders to obtain views on improving the process. These were all considered when designing the process.
- Our experience of the 2018 review. We have also drawn on our own perspectives on how the different stages and events of the 2018 review aided us in forming the 2018 Instrument. We have drawn on that experience as an input into our process decisions.

There is considerable diversity in the responses and suggestions we have received. That diversity has been helpful in critically evaluating the 2018 process and developing improvements. We expect the changes we are implementing will significantly improve the path to 2022 and ultimately the Instrument.

2 Pathway to 2022 Overview

2.1 What is the rate of return instrument?

The rate of return is the return expected by investors to reward them for investing their capital in a business. The rate of return provides a business with the money to pay the interest on its loans and give a return on equity to shareholders. For investors in regulated energy network businesses, the AER determines an allowed rate of return and sets regulated revenues for an upcoming period (typically every five years).

The AER's rate of return instrument specifies how we determine the allowed rate of return on capital in regulatory determinations for energy networks. It specifies the mathematical formulae we will use to calculate the rate of return, and how we will obtain inputs for those formulae. In some cases those inputs will be specified values, fixed for the life of the instrument. In other cases those inputs will be based on financial market data, which we will observe at the time of each regulatory determination. The Instrument specifies the process by which we will measure market data and incorporate it into our decision.³

The explanatory statement that accompanies the Instrument explains and sets out why we made the decisions we did, considering all the evidence before us. It is in this document that stakeholders can see how we evaluated the evidence.

The current rate of return instrument was made in December 2018 (the 2018 Instrument). It is a binding instrument and applies to all regulatory determinations made while it is in force. There is a four-yearly-cycle for us to review and replace the Instrument.

Estimating the rate of return is not a precise science. We estimate the returns required by investors in view of the risks associated with energy network companies compared to other investment opportunities. We make this judgement by examining a broad range of evidence including financial market data, models of financial returns, the latest investment knowledge and the views of all stakeholders. It is important to have a thorough process to examine the evidence so we are able to make the best decision on how to determine that rate of return.

2.2 Why does our pathway to 2022 matter?

The rate of return instrument is important because the regulated rate of return we set materially affects the amount of money energy network companies collect from consumers of electricity and gas in Australia. The rate of return is a significant driver of regulated revenue. As an approximate indicator:

- A change in the rate of return of ten basis points (one-tenth of one percentage point) results in regulated revenues—and therefore consumer bills—changing by approximately \$100 million annually, spread across all users of electricity and gas Australia wide.
- When we set the 2018 instrument, stakeholders had views on the required rate of return that were more than 400 basis points apart (four percentage points)—which translates to a difference of \$4 billion annually in regulated revenues and consumer bills.

³ The instrument also specifies contingencies to be followed when the data is missing, incomplete or not published in time.

Setting the rate of return requires a balance. On the one hand, we want to set the rate as low as possible so customers do not pay more than they need to. On the other hand, the rate of return needs to be sufficiently high to encourage energy companies and their investors to continue to operate and invest in their networks so customers receive the safe, reliable essential service they want. The Instrument should produce a rate of return that aligns with the efficient financing costs at each regulatory determination, neither too high nor too low.

In December 2022 we will publish the next rate of return instrument (the 2022 instrument). This binding instrument will determine the allowed rate of return on capital in regulatory determinations for the following four year period. Given its material impact and binding nature we need to ensure that we consider the evidence before us thoroughly and stakeholders are offered the opportunity to present their perspectives.

It is therefore important that we carefully consider the process that we will follow to arrive at the 2022 instrument.

This position paper builds upon the consultation paper published in November 2019 and sets out a pathway to the 2022 instrument. This paper:

- Has an explicit focus on the decision making process, not the content of the instrument.
- Provides explanations about the role of each of the key steps in the decision making process.
- Explains where we will make changes to the 2018 process and why.

Our position, laid out in the rest of this document, is that the active phase of the rate of return instrument review will commence in mid-2021. However, our pathway to the 2022 instrument also includes work commencing now that lays the foundation for the active phase of the review.

2.3 What aspects of the process are being evaluated in this document?

This paper and the consultation paper released in November 2019 focus on the process of reviewing the instrument. We consider it best practice to establish a clear process and to improve on the process used in the 2018 review. We have received submissions from stakeholders commenting on a range of issues that are relevant to the 2022 review. Some of these issues are outside the scope of this position paper. We will take up those issues during the active phase of the 2022 review and in working papers.

2.4 What steps are we including in the next review?

The NEL and NGL prescribe several steps and processes we must use in developing the 2022 instrument. This includes several of the innovations introduced in the 2018 review. We have reviewed these requirements and added some additional elements we think will improve the process. The key elements we will employ are:

- Annual updates of key data series informing the rate of return. We published the first update in this series at the end of 2019.

- Working papers to explore key elements of the rate of return and lay a foundation for the next instrument. We have commenced work on preparing the first set of working papers.
- A consumer reference group (CRG) to provide a strong consumer perspective in the consultation process. We see this as an important element given the challenges (such as resourcing, coordination and information asymmetry) facing individual consumers seeking to be heard in our consultation processes. We are currently recruiting for the CRG.
- An investor reference group (IRG) and retailer reference group (RRG) presenting their perspectives.
- Concurrent evidence sessions to increase sharing and testing of material. We discuss below some potential changes to the concurrent evidence sessions.
- An independent panel to review the AER's draft decision. The panel provides the benefit of an independent review, whilst promoting confidence amongst stakeholders that our findings on rate of return issues are robust and well tested.

The 2022 review will benefit from advanced planning for these elements. In the 2018 review the final legislation was only passed shortly before the publication of the 2018 instrument and we needed to anticipate the shape of these elements.

We asked The Brattle Group to collect feedback from stakeholders on the 2018 process. The findings in its report (published alongside our November 2019 consultation paper) have helped us shape and prepare for the upcoming process.⁴ In particular, we are aiming for a longer build-up process to ease time pressure in the active phase of the review.

⁴ The Brattle Group, *Stakeholder feedback on the AER's process for the 2018 rate of return instrument*, 27 June 2019; AER, *Consultation paper, Pathway to the 2022 rate of return instrument*, November 2019. Both are available on the AER website at <https://www.aer.gov.au/publications/guidelines-schemes-models/rate-of-return-instrument-2022>.

3 Summary of key elements

The below table summarises how we are proceeding with each aspect of the 2022 Review. Section 4 of the paper sets out the overall timeline of the review and section 5 explains the reasoning behind our decisions and highlights how we have responded to stakeholder feedback.

Table 3.1 Key elements of the 2022 process

Elements	Key elements
<p>Consumer Reference Group</p>	<p>Role:</p> <p>The role of the CRG is to advise the AER on our consumer engagement and to actively engage consumers themselves and provide us with their insights.</p> <p>Set up and running the CRG:</p> <p>The CRG will comprise 5 to 9 members, appointed by the AER with one position reserved for a representative from Energy Consumers Australia (ECA).</p> <p>This CRG will be active in time to comment on the working papers and the inflation review in 2020.</p> <p>Focus:</p> <p>The CRG will be set up with the intention of being able to submit consumer perspectives including on technical and procedural issues during the rate of return process. The final membership will encompass representatives with a diverse range of skills and experience.</p> <p>Consumer Challenge Panel (CCP):</p> <p>There will be no formal CCP sub-panel in place for the rate of return instrument review.</p>
<p>Concurrent Evidence Sessions</p>	<p>Role of the sessions:</p> <p>The role of the sessions is to provide insight to the AER on key rate of return topics.</p> <p>Running sessions:</p> <p>Stakeholders will be able to submit potential questions to the AER who will in turn consider which ones to put forward to the expert panel.</p> <p>We will implement an experts' conclave session, which will be a private discussion between the selected experts. This will help narrow the topics for consideration and aid in the focusing of the expert sessions.</p> <p>More stakeholders will be able to attend the sessions.</p> <p>Expert joint report:</p> <p>There will be no expert joint report published after the concurrent evidence sessions. The sessions themselves will be attended by the board, stakeholders and relevant staff to be considered as evidence. There will be a transcript of the sessions.</p>

Issues papers:

These papers will be released two to three months prior to the sessions enabling experts and stakeholders to be well prepared for the sessions.

Independent Panel

Role of the panel:

The panel will be asked two questions:

“In the panel’s view, is the draft instrument supported by evidence and reasons, taking into account competing factors such as accuracy, consistency, accessibility and transparency?”

“In the panel’s view, is the draft instrument likely to contribute to the achievement of the NEO and NGO?”

Stakeholder feedback:

We will invite stakeholders to provide brief summary submission highlighting important areas for the attention of the panel. These submissions are to be provided to us during our preparation of the draft instrument so the panel can have access to the same material we considered.

Other Stakeholder Groups

The Investor Reference Group (IRG) and Retailer Reference Group (RRG) should remain involved in the process.

4 Timeline

Taking into account the feedback around the 2018 process, we are making a number of changes to the 2022 review timeline. We have been influenced by feedback stating that too much of the work was forced into the second half of the review. We are keen to ensure that more work is undertaken earlier in the process. To this end, we are looking to bring forward some work through working papers. We also want to provide more time between key steps of the process to allow for greater review of stakeholder submissions.

Table 4.1 Dates and key steps for the 2022 Instrument process

Stage of Review	2018 Process - Actual	2022 Process - Intended
Foundational phase		
Consultation Paper - High Level		November 2019
2019 Rate of Return Annual data Update		December 2019
Position Paper - Path to 2022		May 2020
Publication of initial round of working papers		June-August 2020
2020 Rate of Return Annual data Update		November 2020
Resolution of initial round of working papers		December 2020 to May 2021
Active phase		
Consultation Paper - Detailed	31 July 2017	May 2021
Stakeholder Forum	18 September 2017	June/July 2021
Position Paper - Detailed	28 November 2017	October 2021
2021 Rate of Return Annual data Update		November 2021
Information Papers	February 2018	December 2021
Experts' Conclave		Early February 2022
Concurrent Evidence Sessions	15 March/5 April 2018	February/March 2022
<i>Expert joint report</i>	<i>21 April 2018</i>	<i>No longer required</i>
Draft Instrument	10 July 2018	June 2022

Independent Panel Report	September 2018	August 2022
Final Instrument	December 2018	December 2022

4.1 Timetable changes

Stakeholder feedback was that our timetable became too condensed in the second half of the process. We have altered our timetable in order to alleviate time pressure at various key points, while still having regard to the overall length of the review.

Throughout the timetable we have brought forward the steps that happened in the 2018 review. For example, the stakeholder forum which was held in September 2017 will be held in June/July of 2021.

The introduction of working papers, commencing well in advance of the active phase of the review is an opportunity to space out the technical work and settle some areas of discussion ahead of time. We have also significantly increased the gap between the Information papers and the Concurrent Evidence Sessions to allow experts to prepare fully.

4.2 Consultation and position papers

This paper is focused on high level elements of the review process. Subsequent working papers will address technical issues.

We will also undertake further consultation and position papers at the start of the active phase of the review process (in 2021). These papers will provide timings and discuss topics for consideration in more detail.

4.3 Information papers

The Information papers outlined in Table 4.1 are designed to guide the discussions of the concurrent evidence sessions and allow the experts to prepare adequately. We have scheduled an extra month between the release of the information papers and the first concurrent evidence session.

5 Key elements of the path to 2022

This section sets out in more detail the key elements of our pathway to 2022. These include:

- Annual data updates
- Working papers
- The Consumer Reference Group
- Concurrent expert sessions
- The Independent Panel

5.1 Annual data updates

We published the first rate of return annual data update in December 2019. It provides information on rate of return data in the years between reviews. The updates include data which informs the components of the rate of return including the risk free rate, return on equity, return on debt and value of imputation credits. We will continue this series through to the 2022 review.

5.2 Working papers

We will publish papers that discuss issues and evidence on key rate of return topics. These papers will cover a range of topics allowing us to hear from stakeholders and to provide our perspective and consideration ahead of the active phase of the review process. This will mean that there is more time during the active phase to discuss contentious and emerging issues. We have also had regard to whether topics could be constructively considered as discrete issues in advance of the active phase of the review.

Having considered the feedback from stakeholders, we are intending to undertake the working papers set out in Table 5.1. We will commence with four working papers during 2020. We have begun work on three papers now and will begin the fourth in Q4 of 2020. We are in the process of engaging consultants to provide initial reports to lay a foundation for stakeholder engagement. This will be done navigating current working restrictions and we will take steps to have a comprehensive stakeholder engagement program in all of the working papers.

Table 5.1 Program of working papers

Working Paper	Content	Dates
CAPM and alternative return on equity models	This working paper will compare and contrast return on equity models with regard to finance theory and practice. There will be a focus on any recent developments in academic literature. The working paper will consider how these models could be used within the regulatory framework to best advance the NEO/NGO.	May - December 2020

Energy network debt data - Debt term and extension of debt index	This working paper will extend previous work started in 2018 on the method used to calculate the term of debt for network businesses. Will include analysis of debt data obtained from network businesses at the end of 2019 and an update of the Energy Infrastructure Credit Spread Index, our measure of actual industry debt costs.	May - October 2020
International regulatory approaches to rate of return	This working paper will consider how prominent international regulators determine the rate of return, and identify key similarities and differences when compared to our current approach. This paper will also identify differences in the broader regulatory frameworks as well as differences in financial market conditions.	May - November 2020
Annual data update	This is our annual update of the underlying data (particularly time series data) used (a) to inform the 2018 Instrument and (b) in the estimation of the rate of return for ongoing regulatory decisions.	September - November 2020
Rate of return and cashflow in low return conditions	This working paper will consider the potential impact of low inflation, low interest rates and/or low CGS yields on (a) the regulated rate of return outcomes and (b) the required (market) rate of return.	Q4 2020 - Q2 2021

We are considering a number of potential working paper topics for commencement in 2021 including:

- Assessment of network financeability
- Equity beta analysis and relevant comparators
- Gamma and assessment of available imputation credit data
- Methods for estimating the market risk premium.

5.3 Consumer Reference Group

The consumer reference group (CRG) was a new addition to the 2018 review process and in our view helped improve the ability of consumers to effectively present their perspective to the AER as well as other stakeholders. The changes discussed below aim to build on the 2018 CRG involvement and further improve the CRG's ability to contribute constructively to the 2022 Instrument.

5.3.1 Role of the CRG

Establishing the next CRG is an important step for facilitating consumer engagement. The role of the CRG is to:

- Advise us on our consumer engagement
- Actively engage with consumers themselves and provide us with their insights.

5.3.2 Set up and running of the CRG

We are moving to set up the CRG immediately. This will allow the CRG to be a key part of the consumer response to the working papers detailed in this position paper and the 2020 inflation review. We are also running the CRG through to early 2023. This will allow a review and feedback cycle on the entire 2022 review.

The CRG will consist of between 5 to 9 members appointed by us, with one of these places reserved for a member from Energy Consumers Australia. We will provide funding for the group so they can gather information and contribute during rounds of stakeholder engagement.

When appointing members to the CRG we are seeking to form a group which blends experience from several fields:

1. Consumer advocacy, insight and engagement – research expertise or significant experience in understanding diverse consumer priorities and needs, and engaging consumers in the regulatory framework.
2. Regulatory decision-making – for example by experience in working within a regulator or similar agency, preparing submissions or reports on regulatory matters, or undertaking reviews of regulation and regulatory agencies.
3. Knowledge of the energy sector or other utilities – for example working within a relevant business or providing consultancy to it.
4. Financial and economic analysis – for example through applying financial, economic and statistical skills in the areas of corporate finance, investment analysis, economic forecasting or business analysis.

It is important that the CRG retains a core consumer focus and continues to advocate strongly for all consumers, including future ones. Nevertheless, we are seeking an increased focus on finance and economic skills so the CRG will be capable of responding to the information provided and presenting a strong consumer case. All members on the CRG will need to be able to harness their differing skillsets in order to effectively represent consumer interests.

As during the 2018 review cycle, we will work with the CRG to build their skills and capabilities in areas relevant to the rate of return. We will encourage engagement between the CRG and other key stakeholder representatives to exchange views and explore issues.

We will work with the CRG to consider how their views will be represented at the concurrent evidence sessions.

5.3.3 Stakeholder feedback on the CRG

The CRG were commended in some stakeholder submissions for enabling the discussion of topics that were important to consumers and not previously considered during the review.⁵ However there were some submissions that stated there should be more consumer engagement in the form of surveys and questionnaires by the CRG, with the end goal of ensuring that those topics consumers were most concerned about were being effectively raised.⁶ We consider it would be beneficial for the CRG to engage with both consumers and technical experts as the process progresses so they are able to represent consumer views effectively and correctly.

5.3.4 Consumer representation and the CCP

Some stakeholder submissions stated they felt there was an overlap between the role of the CRG and the already established consumer challenge panel (CCP).⁷ For the 2022 review we will not establish a CCP to participate in the review. We think that it is better to focus resources on the CRG to create a focal point for consumer representation and to try and avoid the potential confusion that some stakeholders reported during the 2018 review. This will enable a unified, effective consumer representation body that can engage both with ourselves and other stakeholder groups throughout the review.

5.4 Concurrent evidence sessions

The concurrent evidence sessions were a new addition to the 2018 review process and helped improve the ability of the AER to engage with the breadth of expert opinion and filter the evidence. In particular, the sessions were intended to draw out points of agreement and disagreement between experts, allowing for immediate exchanges back and forth rather than spread out in written reports over many months.

The concurrent evidence sessions involved expert advice on specific rate of return issues to assist in our consideration of issues. Stakeholders were positive about the introduction of the sessions, but there were areas where stakeholders wanted to see improvement.⁸

5.4.1 Role of the concurrent evidence sessions

The purpose of the sessions is to aid the AER in making decisions around a rate of return instrument that will, or is most likely to, contribute to the achievement of the NEO and NGO to the greatest degree. They will do so by allowing us to test the available information. Some submissions proposed a more determinative role for the sessions including a proposal that we should accept any majority view from the experts.⁹ We do not see the sessions being determinative of issues in their own right. Rather, we see the sessions as important for

⁵ AEC, *Submission on Rate of Return Pathway to 2022*, 17 January 2020, pp. 1–2; ENA, *Submission on Pathways to 2022 Rate of Return Instrument and Annual Update*, 20 December 2019, p. 11.

⁶ ENA, *Submission on Pathways to 2022 Rate of Return Instrument and Annual Update*, 20 December 2019, p. 11; SAPN, *Submission to AER Pathway to 2022 Rate of Return Instrument*, 17 January 2020.

⁷ AEC, *Submission on Rate of Return Pathway to 2022*, 17 January 2020, p. 1; NSG, *Submission to the 2022 Rate of Return instrument process review*, 17 January 2020, p. 5.

⁸ Brattle Group, *Stakeholder Feedback on the AERs Process for the 2018 Rate of Return Instrument*, June 2019, p. 16.

⁹ ENA, *Submission on Pathways to 2022 Rate of Return Instrument and Annual Update*, 20 December 2019, p. 14; APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 9; AGIG, *Submission to consultation on 2022 instrument process*, 17 January 2022, p. 3.

informing ourselves. Like other aspects of the process, they are designed to provide information to the AER and aid in the decision making process.

5.4.2 Running the concurrent evidence sessions

In the 2018 review process we held two concurrent evidence sessions which focused on different topics of discussion. The sessions were preceded by information papers (5.4.6) and followed by a Joint Expert Report (5.4.5) summarising the views that were discussed. Both sessions were assisted by a facilitator, who kept the discussion on track and moved through the topics for discussion.

We will retain this facilitator role in the 2022 review. The facilitator played a key part in allowing the discussion to flow. The role will be central again to sessions in the 2022 review, and we will be asking the facilitator to focus the discussion on topic and that all experts are heard.

The outline of the sessions will remain visibly similar to the process used in the 2018 sessions. The sessions were key for understanding the nuance behind arguments and submissions made by all parties.

In the recent submissions, some stakeholders stated they wanted to be able to submit questions for consideration in the sessions, to direct attention to areas deserving of the most attention.¹⁰ We consider this is a reasonable request, and will be allowing stakeholders to submit potential questions to us. We will in turn consider which questions to put forward to the expert panel in consultation with the facilitator.

Some submissions queried the balance of perspectives represented in the sessions. This is an issue we will consider closer to the sessions, but in general we agree that it is desirable to have a fair balance of perspectives represented.

There was a mixed response about the prospect of running more sessions in the 2022 review. Some stakeholders stated the concurrent evidence sessions were time constrained,¹¹ and allowing for more time may allow the experts to seek resolution of more complex issues.¹² Other submissions stated we should not undertake more sessions because this will not solve, and may in fact exacerbate, issues where experts spent time discussing topics that did not contribute meaningfully to the formation of the instrument.¹³ We will not add in an additional session, but will aim for a tighter focus through the preparation of working papers, the addition of a conclave session and through early preparation.

5.4.3 Expert conclave

¹⁰ APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 8.

¹¹ AEC, *Submission on Rate of Return Pathway to 2022*, 17 January 2020, p. 3.

¹² APA, *Submission on Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 3; NSG, *Submission to the 2022 Rate of return Instrument process review*, p. 5; APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 8;

¹³ AEC, *Submission on Rate of Return Pathway to 2022*, 17 January 2020, p. 3.

We recognise that simply extending the time spend on concurrent evidence will not necessarily improve outcomes and will add cost. After consideration of all submissions, we consider it would be most beneficial to add an initial 'expert conclave'. In this type of meeting, the experts would meet with the facilitator to discuss initial views and the topics that are likely to be of most value. This initial preparation will help focus discussion in the public sessions. We consider it is desirable to undertake this conclave session in the weeks before the concurrent evidence sessions. This will involve more engagement from the experts prior to the sessions, but should significantly aid the AER's decision making.

5.4.4 Session attendees

There was strong support for allowing more attendees to view the sessions, to allow an increase in understanding of context.¹⁴ We will open the sessions so that more stakeholder attendees will be to view the sessions. This will enable stakeholders to view the discussion first hand and not just on the transcript. We are considering whether this might be done by narrowcast or in person.

5.4.5 Expert joint report

In 2018 the expert joint report was produced after the concurrent evidence sessions and aimed to clarify and summarise the positions taken by the various experts during the discussions. Our consultation paper noted conflicting views on the usefulness of the joint report, and our proposal to require experts to commit to the production of the report before taking part in the concurrent evidence sessions.¹⁵

In response to our consultation paper, stakeholders submitted that the expert joint report:

- Needed to become substantially more formal and detailed, with majority and minority positions (as per a court judgement).¹⁶
- Should be directly written by the experts themselves (instead of the facilitator as in 2018)¹⁷
- Should be produced prior to the evidence sessions; or both before and after the sessions.¹⁸

Some stakeholders submitted that the expert joint report should be held as a directing piece of evidence for the AER and that the evidence and judgements presented in the joint report should be adhered to in the decision, or explicit reasoning given where not done so.¹⁹

¹⁴ APA, *Submission on Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 3; AGIG, *Submission to consultation on 2022 instrument process*, 17 January 2022, p. 2.

¹⁵ AER, *Pathway to the 2022 rate of return instrument, Consultation paper*, November 2019, p. 16.

¹⁶ AGIG, *Submission to consultation on 2022 instrument process*, 17 January 2022, p. 2; APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 10.

¹⁷ APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 10.

¹⁸ ENA, *Submission on Pathways to 2022 Rate of Return Instrument and Annual Update*, 20 December 2019, p. 13; SAPN, *Submission to AER Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 6.

¹⁹ ENA, *Submission on Pathways to 2022 Rate of Return Instrument and Annual Update*, 20 December 2019, p. 14; APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 9; AGIG, *Submission to consultation on 2022 instrument process*, 17 January 2022, p. 3.

After consideration of the Brattle report feedback and recent submissions, we have decided that an expert joint report will not be produced for the 2022 review. This decision reflects our experience from the 2018 process and our approach for more comprehensive preparation in advance. In the 2018 process, the aspect that was of most assistance to the AER was the discussion itself and the opportunity to test ideas and perspectives in the discussion with the experts. By contrast, the joint report was of limited assistance.

5.4.6 Information papers

As part of the sessions during the 2018 review we released a series of information papers designed to inform experts of our current positions on the topics up for discussion as well as presenting questions for discussion during the sessions. We will provide similar papers for the 2022 review. However, we think that our working papers will provide much of the foundational material.

We received strong feedback from stakeholders that the information papers were released too late in the process.²⁰ We will release these papers two to three months prior to the concurrent evidence sessions, building on our working papers.

5.5 Independent Panel

The Independent Panel was set up as part of the 2018 review in order to provide an independent review of the draft instrument and report to the AER on its findings. Testing our draft instrument in this way was a particularly important innovation in our review process in view of the contentious nature of rate of return issues, the impact of our rate of return instrument, and the depth and breadth of technical material before the AER. It comprised five Panel members drawn from diverse backgrounds and areas of expertise informed by suggestions from a range of stakeholders.

The two main purposes of the Independent Panel process were to give us the benefit of an independent review, and to promote confidence amongst stakeholders that our findings on rate of return issues were robust and had been tested.

5.5.1 Role of the panel

The Independent Panel's role is to review the draft instrument by looking at the information we had regard to in drafting the instrument. This includes submissions made as part of the process and expert reports.

Previously we asked the panel to address the following question:

“In your [the panel's] view, is the draft guideline supported by sound reasoning based on the available information such that it is capable of promoting achievement of the NEO/NGO?”

Submissions have suggested we should seek to further enhance the role of the panel and to sharpen the question it examines to support stakeholder confidence. We agree with these submissions, but we also recognise the role of the panel in assisting our decision making.

²⁰ APGA, *Submission to the AER's Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 8.

We consider it useful to split the previous question into two distinct parts and to sharpen the focus on promoting the achievement of the NEO/NGO. Therefore, we consider the following questions appropriate for guiding the role of the panel in the 2022 review:

“In the panel’s view, is the draft instrument supported by evidence and reasons, taking into account competing factors such as accuracy, consistency, accessibility and transparency?”

In the panel’s view, is the draft instrument likely to contribute to the achievement of the NEO and NGO?”

In our view, the role of the independent panel should not include duplication of our regulatory judgement or to put forward an alternative or amended Instrument. Our view is that the independent panel is best suited to a role of reviewing that we have undertaken an effective review process; engaged with the material before us with an open mind; and have reached a decision that is supported by our stated reasons and the information available to us. Its role focuses on providing its conclusions about whether our decision making is likely to contribute to the achievement of the NEO and NGO.

5.5.2 Stakeholder engagement with the panel

Some stakeholders requested to have direct contact with the panel after the draft instrument had been published so they could highlight important aspects of the review.²¹ We have considered the request and do not agree. We consider that stakeholders should be encouraged to submit all relevant material to the AER before we make a draft instrument, and the panel's review can then focus on all the evidence before the AER. However, we do accept that the panel should be clearly directed to the key issues and will include a process following the expert sessions where stakeholders provide a short summary of key issues for consideration by the AER which we would provide to the panel.

5.6 Other stakeholder reference groups

Alongside the CRG we also established two other stakeholder groups, the Investor Reference Group (IRG) and Retailer Reference Group (RRG). These were set up with the aim of establishing more consistent stakeholder feedback from these groups and ensuring all perspectives were being considered.

We received a range of feedback on the IRG and RRG. Whilst some stakeholders were unsure what these reference groups brought to the process others indicated their input enabled others to consider views and perspectives different to their own, especially at a strategic or non-technical level.²² We hold that it is important to maintain these reference groups and to set them up early.

We will initiate setup of these groups to encourage involvement on the upcoming working papers.

²¹ AGIG, *Submission to consultation on 2022 instrument process*, 17 January 2020, p. 2; SAPN, *Submission to AER Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 7.

²² APA, *Submission on Pathway to 2022 Rate of Return Instrument*, 17 January 2020, p. 3; CRG, *Submission to AER 2019 Consultation Paper*, 17 January 2020, p. 6.

6 Summary of stakeholder submissions

Table 6.1 The CRG and Consumer Representation

Stakeholder	Position	Page
AEC	The distinction between the CCP and CRG is confusing.	1
	The technical expertise of the CRG needs to improve, but it is important to understand consumer issues, such as poverty alleviation.	1 & 2
	Engagement between the CRG and the RRG is welcome, but this may not be constructive when interests are not aligned.	2
	The role of the RRG does not need to change and should remain involved in the 2022 process.	3
APA	More collaboration is required between the CRG and the CCP, but consumers should decide on how best the CRG will contribute.	2
	Investor and retailer reference groups should focus on the strategic elements of a model rather than its technicalities.	2
CRG	The CRG should be made up of a core and a wider group, where the core group undertakes intensive activities and reports back to the wider group.	3
	A project budget should be set by the AER to cover all CRG activities.	3 & 4
	There is sufficient distinction between the CCP and the CRG.	5
ENA	No one is advocating for the interests of future consumers and grid users, with the CRG focusing too much on short term issues.	10 & 11
	The CRG should have more direct consumer input and canvass opinions where possible to support their arguments.	11
	The CRG should push for joint work with industry on review issues, as well as undertaking collaborative discussions with other stakeholders	12
MEU	The CRG requires more funding.	2
	The CRG was formed too late in the 2018 review process for the AER to maximise its utility to the process.	2
NSG	The role of reference groups needs to be made clearer and eligibility requirement should be established.	5
	The AER should arrange and facilitate meetings with other reference groups.	5
SAPN	A formal role should be created for the interests of future consumers.	8

Recordings between the CCP and AER should be made available to the public. 8

Table 6.2 Independent Panel

Stakeholder	Position	Page
AGIG	The Panel should not be limited to reviewing the process used by the AER, but should also review substantive issues.	2
	The Panel should consider whether the decision best meets the NGO/NEO rather than just being capable of meeting it.	2
	Stakeholders should be able to submit a summary of key issues to the Panel for review.	2
APA	Stakeholders should not have direct contact with the Panel.	3
APGA	The Panel should focus on the outcomes rather than the process used by the AER.	10
	The use of the Panel previously by the AER was a waste of the experience of the people on the Panel.	10
	Each stakeholder should submit a summary table prior to the Draft decision, which highlights ten issues they consider the most crucial.	11
CRG	The terms of reference for the Panel should be made available for public comment early in the review process.	8
	Stakeholders should be able to make submissions to the Panel highlighting where the focus of their review should be.	8
ENA	The Panel's role should be expanded to evaluate if the decision is the most appropriate, and not just capable of promoting, the NEO and NGO, if the AER is serious about enhancing stakeholder confidence.	14
	Stakeholders should be able to submit a short summary of critical areas for review in the AER's draft instrument to the Panel.	16
	The Panel should comment on the final instrument.	16
NSG	The AER should give the Panel more guidance regarding the materiality of issues and key areas of stakeholders' views.	5
	Stakeholders should be able to submit on priority issues.	6
	The AER should develop its own position and provide an explanation for agreeing or disagreeing with the Panel's views.	6

SAPN	Stakeholders should be able to submit a small paper on the key issues to the Panel for review.	7
	The Panel should consider whether the AER's conclusions are supported by the weight of evidence, not just whether the AER had explained its reasons for a conclusion.	7
	The Panel produce a second report after the AER releases the final instrument.	7
	The Panel document the role of each member in preparing the report and identifying the information they had regarded.	8

Table 6.3 Concurrent evidence sessions & Expert joint report

Stakeholder	Position	Page
AEC	The sessions had issue with time constraints.	3
	Time spent during sessions should be focused on the disagreements of substance.	3
	A method to narrow discussion topics down earlier would help the sessions be of maximum use	3
AGIG	There needs to be more distinction between evidence and the opinions' of experts during the sessions.	1
	A report should be made available to stakeholders prior to the sessions.	1
	More formality and detail is required in the Joint Expert Report.	2
	Stakeholders should be present during the sessions.	2
	The AER should make clear the extent to which it must rely upon the Joint Expert Report.	2
APA	Hold at least 1 additional session.	3
	Allow a larger number of attendees.	3
	Continue producing the Joint Expert Report as a summary of the proceedings of the evidence sessions.	3
APGA	Too many questions, not contributing to the overall rate of return were asked.	8
	Stakeholders should come up with a long list of questions for the sessions which is then shortened by the AER board.	8

	All consultation material should be released with sufficient time (say 3 months) ahead of the sessions.	8
	An additional session should be held after the Draft decision for experts to focus on how the AER interpreted this evidence.	8
	Experts should be held accountable for their views using the Federal Court's guidelines for expert witnesses.	8
	More formalisation is required for the Joint Expert Report with the production of a majority and minority view on each question put to the experts.	10
	The Report should be detailed and grounded in evidence rather than a series of dot points.	10
	The authors of the Report should be the experts themselves and not the convenor.	10
Ausgrid	To increase independence of the experts, the AER could explain why certain experts were chosen for particular components of the review.	2
	The AER should give equal weighting to all expert opinions and their evidence.	2
CRG	All experts should be commissioned and paid for by the AER.	7
	Sessions should only focus on area of contention.	7
	AER's conclusions for the Draft (and Final) Instrument should be reconciled to experts' conclusions.	7
ENA	The experts should summarise their views in a Joint Report prior to the sessions.	13
	There should be more time prior to the sessions after the Information Papers have been published	13
	The sessions need to avoid areas of no real disagreement and areas beyond the control of the AER.	13
	Stakeholders should be able to attend the sessions to promote transparency and regulatory confidence.	14
NSG	There should be an additional session after the Draft decision.	5
	Experts should commit to these sessions and participate in developing the Joint Report.	5
SAPN	Experts prepare a Joint Report on issues to be discussed in each sessions prior to them occurring. A final report would then be prepared, updating the prior report.	6

Senior AER staff should participate in each session and a full transcript of each session should be published. 6

Table 6.4 Annual updates and working papers

Stakeholder	Position / Suggestions	Page
AGIG	Indexed corporate bonds could be used to sense-check the real return on debt that the AER is targeting.	3 & 4
	Working paper suggestions: <ol style="list-style-type: none"> 1. An update to financeability 2. An indication of the real return implied by each update 	3
APA	AER should provide periodic updates on key rate or return spreadsheets and make them available as appendices.	3
APGA	AER should provide context on the materiality of changes and how data is evolving.	12
	In each update, the real rate of return should be shown and have the financeability information updated.	12
	Working paper suggestions: <ol style="list-style-type: none"> 1. Estimating equity beta 2. Cross-checks 3. Effects of low interest rates on investors 4. AER's approach to assessing financeability 	14
Ausgrid	The AER should assess outcomes of the 2018 instrument in decisions made since its implementation to highlight any possible unintended consequences.	2
ENA	Working paper suggestions: <ol style="list-style-type: none"> 1. Review of the current status and application of the 'standard' Capital Asset Pricing Model 2. Use of samples in estimation of equity beta 3. Estimating the cost of equity in a low or zero-bond rate environment 	22
NSG	Updates on inflation and forecast methodology should be included in the annual updates and the working paper.	5