



# **Position Paper**

## **Remitted debt decisions for NSW/ACT 2014–19 electricity distribution determinations and Jemena Gas Networks 2015-20 (NSW) Access Arrangement**

December 2017

© Commonwealth of Australia 2017

This work is copyright. In addition to any use permitted under the Copyright Act 1968, all material contained within this work is provided under a Creative Commons Attributions 3.0 Australia licence, with the exception of:

- the Commonwealth Coat of Arms
- the ACCC and AER logos
- any illustration, diagram, photograph or graphic over which the Australian Competition and Consumer Commission does not hold copyright, but which may be part of or contained within this publication. The details of the relevant licence conditions are available on the Creative Commons website, as is the full legal code for the CC BY 3.0 AU licence.

Requests and inquiries concerning reproduction and rights should be addressed to the Director, Corporate Communications,  
Australian Competition and Consumer Commission,  
GPO Box 3131,  
Canberra ACT 2601  
or [publishing.unit@acc.gov.au](mailto:publishing.unit@acc.gov.au).

Inquiries about this publication should be addressed to:

Australian Energy Regulator  
GPO Box 520  
Melbourne Vic 3001

Tel: 1300 585165

# Invitation for submissions

Interested parties are invited to make submissions on this position paper by 10 February 2018.

We invited interested parties to make submissions on any issues they see with our proposed approach. This may include (but is not limited to):

- Our interpretation of the orders of the Tribunal and Full Court
- Our interpretation of the relevant rules and law
- Our proposed approach to setting the cost of debt in these remittal decisions

Submissions should be sent to: [NSWACTremittal@aer.gov.au](mailto:NSWACTremittal@aer.gov.au).

Alternatively, submissions can be sent to:

Mr Warwick Anderson  
General Manager, Network Finance and Reporting  
Australian Energy Regulator  
GPO Box 3131  
Canberra ACT 2601

Submissions should be in Microsoft Word or another text readable document format.

We prefer that all submissions be publicly available to facilitate an informed and transparent consultative process. Submissions will be treated as public documents unless otherwise requested. Parties wishing to submit confidential information should:

- clearly identify the information that is the subject of the confidentiality claim
- provide a non-confidential version of the submission in a form suitable for publication.

All non-confidential submissions will be placed on our website. For further information regarding our use and disclosure of information provided to us, see the ACCC/AER Information Policy (June 2014), which is available on our website.<sup>1</sup>

---

<sup>1</sup> <https://www.aer.gov.au/publications/corporate-documents/accc-and-aer-information-policy-collection-and-disclosure-of-information>

# Contents

Invitation for submissions .....	iii
<b>1 Executive summary .....</b>	<b>1</b>
1.1. Our remittal task .....	1
1.2. April 2015 final AER determinations .....	1
1.3. Interpretation of efficient financing costs .....	2
1.4. The remainder of this paper .....	3
<b>2 Background.....</b>	<b>5</b>
2.1. The AER’s decisions on debt in relation to the introduction of the trailing average for the NSW and ACT distributors and JGN .....	5
2.2. Merits review .....	8
2.3. Distributors' grounds for review .....	8
2.4. PIAC's grounds for review .....	9
2.5. Tribunal's decisions .....	9
2.6. Judicial review .....	10
2.7. Other relevant legal processes.....	11
<b>3 Our debt remittal task.....</b>	<b>12</b>
3.1. The legal framework .....	12
3.2. The assessment approach we have used in recent decisions in determining an approach that contributes to the ARORO .....	13
3.3. The decisions of the Australian Competition Tribunal for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd .....	16
<b>4 The approach to our remittal debt decisions we propose and consider is likely to contribute to the ARORO and best achieve the NEO and NGO19</b>	

# 1 Executive summary

## 1.1 Our remittal task

The AER's task for the remittals is to remake the return on debt decisions in relation to the introduction of the trailing average approach. In particular, we must do this having regard to a correct conceptualisation of a benchmark efficient entity as neither a regulated nor unregulated entity. We must do that in accordance with the orders of the Tribunal as clarified by the Full Federal Court. Our decision must, in all circumstances, focus on achieving the allowed rate of return objective (ARORO) and the national electricity objective (NEO) or national gas objective (NGO), as appropriate.

We note that any change in the revenue the service providers are entitled to recover following this remittal will be recovered (or returned) in future years. This will be done in a present value neutral way that adjusts for the time value of money at the regulated cost of capital. To help facilitate the adjustment of revenues in future years over the next regulatory control period for the electricity businesses the AEMC has made a rule to allow the electricity distributors to correct such differences over both the 2014–19 and subsequent regulatory control periods.<sup>2</sup> Further details on this are contained in an AER operating expenditure issues paper published as part of the remitted decision process.<sup>3</sup>

This paper invites interested parties to make submissions on issues related to the remaking of our decision on the return on debt in relation to the introduction of the trailing average approach for the electricity distribution determinations for Ausgrid, Essential Energy, Endeavour Energy and ActewAGL (the distributors) for the 2014–19 regulatory control period and for the gas access arrangement for Jemena Gas Networks (JGN) for its 2015-20 access arrangement period.

## 1.2 April 2015 final AER determinations

On 30 April 2015, we made final decisions on the determinations for the NSW and ACT electricity distributors for the 2014-19 regulatory control periods. On 3 June 2015 we made a final decision for JGN for its 2015-20 regulatory control period. As part of these decisions we did not accept each of the distributors' proposed estimates and methodology for estimating their trailing average cost of debt. Instead, we substituted our alternative trailing average cost of debt estimate based on our estimation methodology. This included a transition from the on-the-day approach to estimating debt which we had used in previous regulatory determinations to a new trailing average methodology.

---

<sup>2</sup> AEMC, *Participant derogation - NSW DNSPs revenue smoothing, Rule Determination*, 1 August 2017. AEMC, *National Electricity Amendment (Participant derogation - NSW DNSPs Revenue Smoothing) Rule 2017 No. 6*.

<sup>3</sup> AER, *Issues Paper Remitted decisions for NSW/ACT 2014-19 electricity distribution determinations Operating Expenditure*, October 2017.

When making decisions about the rate of return, our objective is to determine a rate that is commensurate with the efficient financing costs of a 'benchmark efficient entity' with a similar degree of risk to the service provider in the provision of its regulated services.

We devised a definition for a 'benchmark efficient entity' that we set out in our Rate of Return Guideline in 2013.<sup>4</sup> This followed significant rate of return related rule changes by the AEMC in 2012.<sup>5</sup> Our definition of a benchmark efficient entity included that it was a regulated entity. We applied that definition when making our decisions about an appropriate debt estimation methodology for each service provider's determination.

Our debt estimation decisions were based on our assessment of what would have been the efficient historical financing practices of our benchmark efficient entity. On this basis, we concluded that a change to the debt estimation methodology would have an impact on our benchmark efficient entity, and we would need to take that impact into account in deciding how to implement the new estimation methodology.

On 17 July 2015, the electricity distributors sought merits review of our final decisions, including our debt transition decisions, by the Australian Competition Tribunal (the Tribunal). The Public Interest Advocacy Centre (PIAC) also applied for review of our NSW final debt transition decisions. On 24 June JGN also sought review of our debt transition decision for it. These reviews were heard together in late 2015.

On 26 February 2016, the Tribunal found that the AER's decision was in error and remitted the decisions back to us.<sup>6</sup> The Tribunal's key finding was that the AER had adopted an incorrect definition of the term 'benchmark efficient entity'. It should not be defined as a regulated entity. The Tribunal also found that there would not necessarily be one benchmark for all service providers. In addition, the Tribunal found that the AER's conclusion that there would necessarily be relevant impacts on a benchmark efficient entity from a change in methodology was incorrect.

On 26 May 2017 the Full Federal Court dismissed our appeal of the decision of the Tribunal in relation to debt and found no error on the part of the Tribunal with respect to this part of its decisions.<sup>7</sup>

### 1.3 Interpretation of efficient financing costs

Following the 2012 rule amendments that proceeded our 2013 Rate of Return Guideline there has been considerable uncertainty about the meaning of 'efficient financing costs'

---

<sup>4</sup> AER, Better Regulation Rate of Return Guideline, Dec 2013.

<sup>5</sup> AEMC, Rule Determination, National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012, National Gas Amendment (Price and Revenue Regulation of Gas Services) Rule 2012, 29 October 2012.

<sup>6</sup> *Applications by Public Interest Advocacy Centre Ltd and Ausgrid* [2016] ACompT 1, p1; *Applications by Public Interest Advocacy Centre Ltd and Endeavour Energy* [2016] ACompT 2, p1; *Applications by Public Interest Advocacy Centre Ltd and Essential Energy* [2016] ACompT 3, p1; *Application by ActewAGL Distribution* [2016] ACompT 4, p1; *Application by Jemena Gas Networks (NSW) Ltd* [2016] ACompT 5, p1.

<sup>7</sup> Federal Court of Australia, *Australian Energy Regulator v Australian Competition Tribunal (No 2)* [2017] FCAFC 79, 24 May 2017; Federal Court of Australia, *Australian Energy Regulator v Australian Competition Tribunal (No 3)* [2017] FCAFC 80, 24 May 2017.

within the ARORO and what debt estimation methodology would contribute to the ARORO, achieve the NEO and NGO and achieve the Revenue and pricing principles (RPPs).

While the Tribunal found us in error and the Tribunal's decision itself was found not to be in error by the Full Court, we consider the Tribunal and Federal Court decisions provide limited clear direction on how we should remake the debt transition decision or on the interpretation of 'efficient financing costs' within the ARORO.

We re-evaluated our approach and reasoning following the original Tribunal decisions that are subject to the remittal. We again re-evaluated our approach and reasoning following the Full Court decisions handed down in May this year. This process of evolution is set out in our recent decision for APA VTS.<sup>8</sup> The Full court decision has also been considered recently by the Tribunal in decisions released in October 2017 for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd.<sup>9</sup>

Given the uncertainty in relation to the rules and law as they relate to the allowed rate of return, including with respect to the interpretation of the Full Court's decision, we have waited for the recent Tribunal decisions for ActewAGL (Gas) distribution and Jemena Electricity Networks Ltd before progressing these remittal processes as they relate to the debt orders.

We consider the recent Tribunal decisions helps to clarify for all stakeholders the interpretation of efficient financing costs within the ARORO and the scope and interpretation of the Full Court's decision.

In light of the Tribunal's recent decisions for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd, we propose to rely on the reasoning as set out in Attachment 3 of our APA VTS determination for this remittal.<sup>10</sup>

Following the reasoning in our APA VTS decisions, in making these remitted decisions we propose to move the service providers to a trailing average debt estimation methodology and to apply a revenue neutral transition in moving to this approach. As noted by the Tribunal in its recent decisions for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd, our proposed approach is effectively a combination of the on-the-day methodology and trailing average methodology.<sup>11</sup>

## 1.4 The remainder of this paper

The key purpose of this paper is to seek stakeholders' views on our proposed position and reasoning for our debt remittal decisions for the NSW/ACT 2014–19 electricity distribution determinations and for the JGN 2015-20 gas access arrangement.

While we must remake the revenue determination as a whole for each distributor taking into account interrelationships between the different contingent parts of our decision, this position

---

<sup>8</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017.

<sup>9</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017.

<sup>10</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017.

<sup>11</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p60.

paper focuses on our remitted debt decisions. Further consideration of other parts of the remittals will occur through separate processes. To date an issues paper on the opex remittal for the NSW Distributors for the 2014-19 regulator control period has been published.<sup>12</sup> The AER will also host a roundtable meeting with JGN and Consumer subpanel 10 in January 2018 on the remitted capital expenditure decision for JGN.

The remainder of this paper is set out as follows:

- Section 2 provides background on the decisions on return on debt in relation to the introduction of the trailing average we made in the final decisions, and the subsequent decisions of the Tribunal and the Court directing us to remake those decisions.
- Section 3 sets out our debt remittal task.
- Section 4 sets out our proposed approach to the remitted debt decisions.

---

<sup>12</sup> AER, Issues Paper Remitted decisions for the NSW/ACT 2014-19 electricity distribution determinations Operating Expenditure, October 2017.

## 2 Background

To contextualise our remittal task for the 2014-19 regulatory control period for the NSW and ACT electricity distributors and for the 2015-20 regulatory control period for JGN, this section presents background information on:

- our decisions on debt in relation to the introduction of the trailing average approach for NSW and ACT distributors and JGN;
- the merits review of our final decisions; and
- the judicial review of the Tribunal's decisions in respect of our final decisions.

### 2.1 The AER's decisions on debt in relation to the introduction of the trailing average for the NSW and ACT distributors and JGN

The AER is required to determine the revenue allowance for electricity distributors under the National Electricity Rules (NER) and fully regulated gas networks under the National Gas Rules (NGR).

As part of the transitional arrangements for major changes to national rules for the regulation of distributors made in November 2012, the Australian Energy Market Commission (AEMC) deferred the full regulatory determination process for NSW/ACT distributors' 2014-19 regulatory control period. On 16 April 2014, as part of the transitional arrangements, we determined a placeholder revenue allowance for the 2014-15 transitional regulatory control period. In May 2014, we received the NSW/ACT distributors' regulatory proposals for the 2014-19 regulatory control period, after which the full determination process commenced. We assessed the revenue allowances for the whole 2014-19 regulatory control period, and trued up any difference between the placeholder revenue allowance and revenue requirement for the transitional year.

On 30 April 2015, we published final decisions for the 2014–19 NSW/ACT distribution determinations. In these decisions, we did not accept the distributors' proposed return on debt estimation methodology and trailing average debt estimate, and instead substituted our own alternative return on debt estimation methodology which applied a transition path to move from the on-the-day debt estimation methodology to the trailing average methodology. On 3 June 2015 we also published the final determination for JGN's 2015-20 Access arrangement period.

The difference between our alternative starting debt estimate and methodology for updating this and the electricity distributors' proposals and JGN's proposal was due to the initial debt estimate for the first regulatory year of each regulatory control period and the method for updating the cost of debt each year.

Table 1 and Table 2 show the differences in the smoothed total revenue between the electricity distributors' and JGN's debt proposals and our final debt decisions.

**Table 1 Differences in the smoothed revenue between NSW/ACT electricity distributors' proposals and AER final decisions — debt forecast for 2014/15-18/19 regulatory period (\$m, nominal)**

	2014/15	2015/16	2016/17	2017/18	2018/19	Total (\$m, nominal)
Ausgrid Distribution debt estimates*	7.81%	7.57%	7.57%	7.57%	7.57%	
AER Final Decision debt estimate	6.51%	6.40%	6.40%	6.40%	6.40%	
Differences	1.30%	1.17%	1.17%	1.17%	1.17%	
Ausgrid Distribution smoothed revenue	2,208.75	1,836.90	1,776.20	1,766.03	1,755.94	9,343.82
AER smoothed revenue	2,208.75	1,693.22	1,637.14	1,627.73	1,618.40	8,785.24
Differences in smoothed revenue	0.00	143.67	139.06	138.30	137.54	558.58
Endeavour Distribution estimates	7.81%	7.57%	7.57%	7.57%	7.57%	
AER Final Decision	6.51%	6.40%	6.40%	6.40%	6.40%	
Differences	1.30%	1.17%	1.17%	1.17%	1.17%	
Endeavour Distribution smoothed revenue	949.45	861.38	855.43	849.51	843.64	4,359.42
AER smoothed revenue	949.45	804.01	798.45	792.93	787.45	4,132.30
Differences in smoothed revenue	0.00	57.37	56.98	56.58	56.19	227.12
Essential Distribution estimates	7.81%	7.57%	7.57%	7.57%	7.57%	
AER Final Decision	6.51%	6.40%	6.40%	6.40%	6.40%	
Differences	1.30%	1.17%	1.17%	1.17%	1.17%	

Essential Distribution smoothed revenue	1,291.72	977.26	1,005.52	1,039.75	1,080.46	5,394.71
AER smoothed revenue	1,291.72	911.31	937.66	969.58	1,007.54	5,117.81
Differences in smoothed revenue	0.00	65.95	67.86	70.17	72.92	276.90

ActewAGL Distribution estimates*	7.78%	7.45%	7.45%	7.45%	7.45%	
AER Final Decision	6.07%	5.91%	5.91%	5.91%	5.91%	
Differences	1.71%	1.54%	1.54%	1.54%	1.54%	
ActewAGL Distribution smoothed revenue	173.25	156.64	157.88	159.47	161.06	808.30
AER smoothed revenue	173.25	145.74	146.90	148.37	149.85	764.11
Differences in smoothed revenue	0.00	10.89	10.98	11.10	11.21	44.18

Source: AER analysis.

Note: The final decision PTRMs were used in the AER smoothed revenue calculations. The differences in the estimated unsmoothed revenues for the 2014/15 year are reflected in the revenues for the following four years in the regulatory period. The businesses' cost of debt estimates and the proposed smoothed total revenue numbers were calculated for the Tribunal hearing. Therefore, only the cost of debt numbers for 2015/16 were available for annual updating. The five year total revenue numbers were submitted to the Tribunal in the Limited Merits Review process.

\* Ausgrid Distribution and ActewAGL Distribution have both distribution and transmission assets. These numbers include the revenue from both types of assets and has been calculated in the two final decision PTRMs for these businesses.

**Table 2 Differences in the smoothed revenue between JGN's proposal and AER final decision — debt forecast for 2015/16-2019/20 regulatory period (\$m, nominal)**

	2015/16	2016/17	2017/18	2018/19	2019/20	Total (\$m, nominal)
JGN Distribution estimates	5.19%	5.19%	5.19%	5.19%	5.19%	
AER Final Decision	4.28%	4.28%	4.28%	4.28%	4.28%	
Differences	0.91%	0.91%	0.91%	0.91%	0.91%	

JGN Distribution smoothed revenue	497.37	474.27	452.44	441.87	455.14	2,321.10
AER smoothed revenue	497.37	450.33	429.60	419.57	432.17	2,229.04
Differences in smoothed revenue	0.00	23.94	22.84	22.30	22.98	92.07

Source: AER analysis.

Note: The final decision PTRM was used in the AER smoothed revenue calculation. The difference in the estimated unsmoothed revenues for the 2015/16 year is reflected in the revenues for the following four years in the regulatory period. JGN's cost of debt estimates and the proposed smoothed total revenue numbers were calculated for the Tribunal hearing. The five year total revenue numbers were submitted to the Tribunal in the Limited Merits Review process.

## 2.2 Merits review

On 17 June 2015, the electricity distributors and PIAC sought merits review of our final electricity determinations. On 24 June JGN sought merits review of our final determination for its access arrangement. This included in relation to each determinations' constituent decision on the return on debt in relation to the introduction of the trailing average.<sup>13</sup> The Commonwealth Minister for Industry and Science also intervened.

## 2.3 Distributors' grounds for review

The distributors essentially argued that our allowed estimated return on debt was too low and would not achieve the ARORO and was inconsistent with the NEO/NGO and revenue and pricing principles. Specifically, each distributor raised issue with our use of a transition to the trailing average that started with a current 'on-the-day' based return on debt number. This was estimated from data close to but prior to the commencement of the 2014/15 regulatory control year for the electricity distributors and close to but prior to the 2015 regulator year for JGN.

The NSW electricity distributors' overarching ground of review on debt transition was 'the AER erred in concluding that the adoption of its transition from the on-the-day approach to the trailing average was consistent with the Rules, the NEO, and the revenue and pricing principles.'<sup>14</sup> This was based on a number of alleged errors set out in the businesses submissions.<sup>15</sup>

<sup>13</sup> The electricity distributors had also sought merits review on other elements of our decision including the return on equity, operating expenditure, the value of imputation credit (gamma), and the efficiency benefit sharing scheme. JGN also sought review in relation to ME Capex.

<sup>14</sup> Networks NSW submissions of Ausgrid, Endeavour Energy and Essential Energy on leave to apply for review, 18 Jun 2015, p 143.

<sup>15</sup> Networks NSW submissions of Ausgrid, Endeavour Energy and Essential Energy on leave to apply for review, 18 Jun 2015, pp 143 - 172.

ActewAGL Electricity Distribution's grounds of review were similar to those of the NSW electricity distributors, its overarching ground of review being 'in relation to the decision on estimating the return on debt, the AER erred in concluding that the adoption of its transition from the on-the-day approach to the trailing average approach was consistent with the NER, the NEO and the RPPs.'<sup>16</sup> This was also based on a number of alleged errors set out in its submissions.<sup>17</sup>

JGN's overarching ground of review was 'the Return on Debt Decision involved an error or errors of fact, or alternatively an incorrect exercise of discretion or was unreasonable, in that the AER erred in determining that the return on debt in the Final Decision (4.28% for the first year of the 2015-20 AA period, and thereafter in accordance with the AER's return on debt methodology) was commensurate with the efficient financing cost of a benchmark efficient entity with a similar degree of risk to that faced by JGN.'<sup>18</sup> This was also based on a number of alleged errors related to the AER's debt transition decision.<sup>19</sup>

## 2.4 PIAC's grounds for review

PIAC, on the other hand, argued that our starting debt allowance was too high. It specifically raised issue with our use of prevailing debt rates before the commencement of the 2014/15 'transitional' regulatory year for the commencement of the trailing average. It argued we should have used prevailing rates closer to the commencement of the 2015/16 regulatory year.<sup>20</sup>

## 2.5 Tribunal's decisions

On 26 February 2016, the Tribunal handed down its decisions.<sup>21</sup> The Tribunal remitted our decisions back to us to be remade, in accordance with its orders on:

- the return on debt (for all of the businesses);
- the value of imputation credits (gamma) (for all of the businesses);
- opex (for all of the businesses except Jemena Gas Networks);
- capex (only for Jemena Gas Networks); and
- the implications of this for the Service Target Performance Incentive Scheme (only for ActewAGL Distribution)

---

<sup>16</sup> ActewAGL Distribution, Submissions in support of application for leave to apply, 18 June 2015, p 122.

<sup>17</sup> ActewAGL Distribution, Submissions in support of application for leave to apply, 18 June 2015, pp122-146.

<sup>18</sup> Jemena Gas Networks (NS) Limited, Application for leave and application for review by the Australian Competition Tribunal, 24 June 2015, p 31.

<sup>19</sup> Jemena Gas Networks (NS) Limited, Application for leave and application for review by the Australian Competition Tribunal, 24 June 2015, pp 32-41.

<sup>20</sup> Public Interest Advocacy Centre Ltd, Application for leave to review and application for review, 21 May 2015, pp 14-20.

<sup>21</sup> *Applications by Public Interest Advocacy Centre Ltd and Ausgrid* [2016] ACompT 1; *Applications by Public Interest Advocacy Centre Ltd and Endeavour Energy* [2016] ACompT 2; *Applications by Public Interest Advocacy Centre Ltd and Essential Energy* [2016] ACompT 3; *Application by ActewAGL Distribution* [2016] ACompT 4.

On the return on debt the Tribunal instructed us to remake the constituent decision on return on debt in relation to the introduction of the trailing average in accordance with the Tribunal's reasons for its decisions without giving a clear clarification of the directions for the remittal.<sup>22</sup>

The Tribunal found us in error in our definition of a benchmark efficient entity as a 'regulated' entity.

The Tribunal also found us in error in our construction of rule 6.5.2(k)(4).

## 2.6 Judicial review

On 24 March 2016, we applied to the Full Federal Court for judicial review of the Tribunal's decisions on the value of imputation credits (gamma), the return on debt and opex.

On 24 May 2017, the Full Court dismissed our appeals on debt and opex and upheld the Tribunal's decisions in relation to these issues. It upheld the AER's appeal in relation to gamma.<sup>23</sup>

The AER has carefully considered the full reasoning of the Full Federal Court in considering what to do to achieve the ARORO, NEO and RPPs in these remittal decisions. Of relevance, in relation to the Full Court's decision:

- The Full Court clarified that a benchmark efficient entity is not necessarily either regulated or unregulated.
- The important characteristic of a benchmark efficient entity is that it has a similar degree of risk to the service provider with respect to the provision of its regulated services.
- A change in debt estimation methodology does not necessarily result in any impacts for a benchmark efficient entity.

In relation to both the decisions of the Tribunal and the Full Court we also make the following observations:

- the decisions of the Court and Tribunal were not focussed on the interpretation of 'efficient financing costs' in the Allowed rate of return objective. We consider this to be an important factor (and which we discuss in further detail under section 3.3).
- neither decision removes the requirement to apply a debt methodology that we consider will achieve the relevant legislative objectives for each of the respective service providers.
- neither decision requires the use of a trailing average methodology for determining the cost of debt in these remittals.

---

<sup>22</sup> *Applications by Public Interest Advocacy Centre Ltd and Ausgrid* [2016] ACompT 1, p1; *Applications by Public Interest Advocacy Centre Ltd and Endeavour Energy* [2016] ACompT 2, p1; *Applications by Public Interest Advocacy Centre Ltd and Essential Energy* [2016] ACompT 3, p1; *Application by ActewAGL Distribution* [2016] ACompT 4, p1; *Application by Jemena Gas Networks (NSW) Ltd* [2016] ACompT 5, p1.

<sup>23</sup> Federal Court of Australia, *Australian Energy Regulator v Australian Competition Tribunal (No 2)* [2017] FCAFC 79, 24 May 2017; Federal Court of Australia, *Australian Energy Regulator v Australian Competition Tribunal (No 3)* [2017] FCAFC 80, 24 May 2017.

## 2.7 Other relevant legal processes

We note that there are other legal decisions that we have had regard to in preparing this paper and considering our proposed approach for these remittal processes:

- The decision of the Australian Competition Tribunal for South Australia Power Networks (currently under review by the Full Federal Court).<sup>24</sup>
- The decisions of the Australian Competition Tribunal for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd.<sup>25</sup>

The decisions of the Tribunal for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd are particularly important. After the Tribunal handed down its decisions in Ausgrid and others, the AER reconsidered its approach to debt estimation methodology. The new approach, which we adopted in our decisions for ActewAGL (Gas) Distribution and Jemena Electricity Networks, does not rely upon a conceptualisation of a benchmark efficient entity as a regulated entity. It recognises that different service providers may have a different benchmark efficient entity. The new approach also does not rely on a change in methodology impacting a benchmark efficient entity to justify our revenue neutral transition. Our new approach does not rely upon an assessment of historical financing practices. Instead, it considers the efficient financing costs (being the costs of equity and debt) in a forward looking manner. Our new approach was subject to review by the Tribunal.

The Tribunal upheld our new approach. It explained more clearly how each of the Tribunal and Court decisions should be read together consistently. It provided clarification for the earlier Tribunal's decision on the directions of the Tribunal for the remittal that were previously unclear to us. We consider these decisions support a revenue neutral transition when moving to a trailing average methodology based on our new approach, or the continuance of an on-the-day methodology for determining the cost of debt.

An important aspect of the decisions for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd is the consideration in those decisions of the interpretation of the 'allowed rate of return objective' and the meaning of 'efficient financing costs'.<sup>26</sup> We consider these decisions support our ex ante interpretation of efficient financing costs. These decisions are covered in further detail below.

Finally, we note that South Australia Power Networks (SAPN) sought judicial review of the decision of the Australian Competition Tribunal decision that affirmed our determination for SAPN's 2015/16-2019/20 regulatory control period.<sup>27</sup> The Full Federal Court heard this appeal in early May 2017 and the decision is currently reserved. The decision of the Full Court for SAPN may be relevant to what debt methodology approach (or approaches) will be legally permissible in these remittal decisions. In making these remittals we will consider the Full Court's decision for SAPN when this is handed down.

---

<sup>24</sup> Australian Competition Tribunal, Application by SA Power Networks [2016] ACompT 11, October 2016.

<sup>25</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017.

<sup>26</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017.

<sup>27</sup> SA Power Networks, Originating Application for review, SA Power Networks v Australian Competition Tribunal & Anor, 25 Nov 2016.

## 3 Our debt remittal task

In this section, we outline the key factors relevant to the remaking of the debt decisions, namely:

- the legal framework in which we must remake the debt decisions;
- the assessment approach we have used in recent decisions in determining an approach that achieves the ARORO; and
- the decisions of the Australian Competition Tribunal for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd.

### 3.1 The legal framework

#### 3.1.1 The Tribunal's directions

The Tribunal provided us with the following direction in relation to debt for Ausgrid:<sup>28</sup>

the AER is to make the constituent decision on return on debt in relation to the introduction of the trailing average approach in accordance with these reasons for decision

The Tribunal also provided corresponding directions for Endeavour Energy, Essential Energy, and ActewAGL.<sup>29</sup>

The Tribunal provided us with the following direction in relation to debt for JGN:<sup>30</sup>

the AER is to make the constituent decision on debt having regard to the position of Jemena Gas Networks (NSW) Ltd in its Revised Regulatory Proposal concerning the trailing average approach in accordance with the reasons for this determination

#### 3.1.2 The NER/NGR and NEL/NGL requirements

The rules in the NER and NGR and provisions in the National Electricity Law (NEL) and National Gas Law (NGL) that govern our assessment of debt remain unchanged on remittal.

We must determine a rate of return such that it achieves the allowed rate of return objective.<sup>31</sup> The allowed rate of return objective is that the rate of return is to commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as that which applies to the service provider in respect of its regulated services (its standard control service in the case of electricity distributors and its reference services in the case of

---

<sup>28</sup> Australian Competition Tribunal, *Applications by Public Interest Advocacy Centre Ltd and Ausgrid* [2016] ACompT 1, direction 1(b).

<sup>29</sup> Australian Competition Tribunal, *Applications by Public Interest Advocacy Centre Ltd and Endeavour Energy* [2016] ACompT 2, direction (1)(b); *Applications by Public Interest Advocacy Centre Ltd and Essential Energy* [2016] ACompT 3, direction (1)(b); *Application by ActewAGL Distribution* [2016] ACompT 4, direction (1)(b);

<sup>30</sup> Australian Competition Tribunal, *Applications by Jemena Gas Networks (NSW) Ltd* ACompT 5, direction 1(a).

<sup>31</sup> NER ss 6.5.2(b), 6A.6.2(b) and NGR s87(2).

JGN).<sup>32</sup> Therefore, each remade debt decision must contribute to achieving the allowed rate of return objective.

Other legislative requirements relevant to remaking our debt decision include the NEO/NGO, the RPPs and any interrelationships with other related components of a distribution determination. The NEO/NGO are relevant because we are required to make a distribution determination that will or is likely to contribute to the achievement of the NEO/NGO to the greatest degree.<sup>33</sup> The RPPs are relevant because we must take them into account in exercising discretion, as is the case in remaking our debt decisions.<sup>34</sup> We must also take into account any interrelationships between our remade debt decision and any other related component of a distribution determination.<sup>35</sup>

Much of the relevant legislation is set out in our recent determination for APA VTS.<sup>36</sup> However, all relevant legislation is available online on the Australian Energy Market Commission website.<sup>37</sup>

## 3.2 The assessment approach we have used in recent decisions in determining an approach that contributes to the ARORO

Our assessment approach we have used in recent determinations is set out in our recent final determination for APA VTS.<sup>38</sup> This is available on the AER website.<sup>39</sup>

We note the APA VTS determination was made in full consideration of the following legal decisions:

- the Tribunal decisions that have led to these remittals<sup>40</sup>
- The Full Federal Court decisions on our appeals of the above Tribunal decisions<sup>41</sup>
- The Tribunal decision for SAPN<sup>42</sup>

---

<sup>32</sup> NER ss 6.5.2(c), 6A.6.2(c) and NGR s87(3).

<sup>33</sup> NEL, ss. 7 and 16(1)(d); NGL ss 23 and 28(1)(iii)

<sup>34</sup> The RPP that are directly relevant to remaking our debt decision are set out at NEL, ss. 7A(2), 7A(3), 7A(5), 7A(6) and 16(2) and NGL, ss 24(2), 24(3), 24(5), 24(6) and 28(2).

<sup>35</sup> NEL, s. 16(1)(c); NGL, s. 28(1)(ii)

<sup>36</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017.

<sup>37</sup> <http://www.aemc.gov.au/Australias-Energy-Market/Market-Legislation>

<sup>38</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017.

<sup>39</sup> <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/apa-victorian-transmission-system-access-arrangement-2018-22/final-decision>

<sup>40</sup> *Applications by Public Interest Advocacy Centre Ltd and Ausgrid* [2016] ACompT; *Applications by Public Interest Advocacy Centre Ltd and Endeavour Energy* [2016] ACompT 2; *Applications by Public Interest Advocacy Centre Ltd and Essential Energy* [2016] ACompT 3; *Application by ActewAGL Distribution* [2016] ACompT 4; *Application by Jemena Gas Networks (NSW) Ltd* [2016] ACompT 5

<sup>41</sup> *Australian Energy Regulator v Australian Competition Tribunal (No 2)* [2017] FCAFC 79, May 2017; *Australian Energy Regulator v Australian Competition Tribunal (No 3)* [2017] FCAFC 80, May 2017.

<sup>42</sup> *Australian Competition Tribunal, Application by SA Power Networks* [2016] ACompT 11, October 2016.

- The Tribunal decisions for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd<sup>43</sup>

As noted earlier, following the Tribunal decisions handed down in February 2016 we reconsidered our approach afresh, and in particular what debt methodology would contribute to achieving the ARORO, the NEO/NGO and the RPPs. This included reconsideration of the appropriate transition if we were to continue to move to a trailing average methodology for estimating the cost of debt. We again reconsidered our debt methodology decisions and reasoning (including whether to continue to move to a trailing average methodology and whether to apply a transition) following the Full Court's decisions handed down in May 2017 and have followed the Full Court decision in all of our determinations released post May 2017.

Of note our APA VTS decision:

- Does not define a benchmark efficient entity as 'regulated'. Rather, it defines a benchmark efficient entity as neither regulated nor unregulated. A benchmark efficient entity for a service provider is an entity that has a risk commensurate with the provision of that service provider's regulated services. In the case of APA VTS, the appropriate benchmark efficient entity is an entity with a similar degree of risk to APA VTS in the provision of its reference services.<sup>44</sup>
- Interprets 'efficient financing costs' as an ex-ante concept as approved by the Tribunal in the ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd appeals of our May 2016 determinations.<sup>45</sup>
- As an ex-ante approach, does not rely on a consideration of the impacts on past financial practices under 6.5.2(k)(4) of the Rules to justify a revenue neutral transition to the trailing average.<sup>46</sup> We note for all decisions released since May 2016 we have applied this type of transition to contribute to achieving the ARORO, the NEO and the RPPs.
- Indicates that if we could not apply an approximately revenue neutral transition we would continue to apply the on-the day methodology to determine the cost of debt.<sup>47</sup> This is on the basis that a rate of return that meets the ARORO must provide for efficient financing costs and this is an ex ante concept.<sup>48</sup> We note that the Tribunal in its decisions for

---

<sup>43</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017.

<sup>44</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017, p 3 - 10. It is also worth noting on this point that while our decisions released between May 2016 and pre the release of the Full Court decision in May 2017 did define a benchmark efficient entity as regulated, they also noted this was not material to the decisions (i.e. we would have applied the same decision regardless of this position) and the Tribunal accepted this in upholding our May 2016 determinations for ActewAGL (Gas) Distribution and Jemena Electricity Distribution Ltd:

Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p 35..

<sup>45</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017, pp 3-17. We have applied this reasoning in all decision released since May 2016.

<sup>46</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017, pp 31-32, 317-319.

<sup>47</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017, pp 31-32, 103.

<sup>48</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017, p 35.

ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd concluded that an on-the-day approach could be lawfully applied in those cases and also that an immediate trailing average would not achieve the ARORO or reflect efficient financing costs.<sup>49</sup>

As noted above, in our APA VTS determination we consider a rate of return that meets the ARORO must provide ex-ante compensation for efficient financing costs and we consider that this is equally applicable in these remittals. This return would give a benchmark efficient entity a reasonable opportunity to recover at least its efficient financing costs. This is a zero net present value (NPV) investment condition.

SFG Consulting advice to the AEMC during the rule change process also supports the position that setting an allowed return that results in a zero NPV investment outcome is important to achieving efficient investment incentives.<sup>50</sup>

Under our regulatory framework, a benchmark efficient entity's assets are captured in its RAB. The return on capital building block allows a benchmark efficient entity to finance (through debt and equity) investment in its network.<sup>51</sup> Because investments usually carry a degree of risk, to satisfy the zero NPV condition the allowed rate of return must be sufficient to compensate a benchmark efficient entity's debt and equity investors for the risk of their investment.<sup>52</sup>

We see the NPV=0 concept given effect in the Revenue and Pricing Principles and this has been a particularly important factor in developing our new approach following the decisions of the Tribunal and the Federal Court. That is, the service provider should be given a reasonable opportunity to recover its efficient costs. It should be provided with effective incentives to promote efficient investment in, provision and use of, services. A return should be commensurate with the regulatory and commercial risks involved in providing the standard control, prescribed transmission, or reference services. We should have regard to the economic costs and risks of the potential for under and over investment by a service provider and to the economic costs and risks of the potential for under and over utilisation of regulated services.

We consider this to be an essential concept that underlies the regulatory scheme that is given expression in the NEO/NGO and the RPPs and the ARORO should be understood in this important context.

We consider a change in methodology is only likely to result in an outcome that meets the ARORO if it results in ex-ante compensation for efficient financing costs and is approximately revenue neutral in a present value sense so that it does not affect the present value of future cash flows through the PTRM or relevant model (avoiding windfall gains or losses to the service providers and consumers). A change in methodology is also only likely to achieve the NEO/NGO if it does not result in a material distortion of investment incentives.

---

<sup>49</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, pp 59-60.

<sup>50</sup> SFG Consulting, Rule change proposals relating to the debt component of the regulatory rate of return, 21 August 2012, pp 63-64.

<sup>51</sup> This includes both new and existing investment.

<sup>52</sup> This risk is based on the risk of the underlying assets (that is, the RAB). See Partington, G., Satchell, S., Report to the AER: Discussion of the allowed cost of debt, 5 May 2016, pp. 18, 22.

In our view a change to the trailing average without a revenue neutral transition will result in an allowed rate of return either above or below the efficient financing costs of a benchmark efficient entity due to the immediate change to the new methodology and not achieve the ARORO. We consider a rate of return materially above or below efficient financing costs due to the change in methodology will create material investment distortions and not achieve the NEO/NGO. A change in methodology that results in a material wealth transfer may also increase regulatory risk and as a consequence the overall financing costs of a benchmark efficient entity.

By combining a trailing average approach with the on the day approach, investment distortions can be limited, but only if the combination involves a revenue neutral transition between the two methodologies. The revenue neutral transition also limits the realisation of financial risk from the change in methodology. This reduction in risk should assist to achieve the lowest cost financing over the life of the assets.

In this sense, we consider the ability to use a trailing average in a manner that will meet the ARORO and NGO is contingent upon the use of a revenue neutral transition.

### **3.3 The decisions of the Australian Competition Tribunal for ActewAGL (Gas) Distribution and Jemena Electricity Networks Ltd**

Following the Tribunal and Federal Court decisions that lead to these remittals, there remained some uncertainty about what methodology for estimating the return on debt would best achieve the ARORO in a manner that contributed to the achievement of the NEO and NGO. This has been recently clarified by the Tribunal.

On 17 October 2017 the Tribunal handed down its decisions for ActewAGL (Gas) Distribution (ActewAGL Gas) and Jemena Electricity Networks Ltd (Jemena Electricity).<sup>53</sup>

The Tribunal in these decisions upheld the AER's new approach which was developed in response to the previous decisions of the Tribunal and Federal Court. That is, it upheld an approach of applying a revenue neutral transition when moving from an on the day approach to a trailing average methodology for estimating the return on debt.<sup>54</sup>

In forming our proposed position on debt transition for these remittals we have carefully considered this Tribunal decision and encourage interested stakeholders to read the full decision available on the Federal Court website.<sup>55</sup>

Of significance, the Tribunal highlighted that the Rules expressly provide for 3 types of methodologies that the AER can adopt when estimating the return on debt. Those 3 methodologies can be generally described as the on-the-day methodology, the trailing average methodology or a combination of the two (such as a transition from the on-the-day

---

<sup>53</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017.

<sup>54</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p i.

<sup>55</sup> <http://www.judgments.fedcourt.gov.au/judgments/Judgments/tribunals/acompt/2017/2017acompt0002>

methodology to a trailing average methodology). It also noted the AER's choice between these methodologies have to be resolved in accordance with s 16(1)(d) of the NEL. That is, we must make the decision that will or is likely to contribute to the achievement of the objective to the greatest degree.<sup>56</sup> This requirement also applies to our gas decisions under s28(1)(iii) of the NGL.

The Tribunal accepted our ex-ante construction of the term 'efficient financing costs' in the ARORO.<sup>57</sup>

The Tribunal noted that the Full Court's reasoning had to be seen 'in the context of the question it was considering' and noted it considered 'that the construction of "efficient financing costs" needs to be considered in the context of what is required by r 6.5.2 as a whole, in the context of the NEO and NGO, and in light of the specific claims by the applicants about how the return on debt should be estimated.'<sup>58</sup>

The Tribunal also noted that the rate of return in a workably competitive market should be seen as an ex ante concept where the rate of return 'will be just sufficient to give the investment's stream of cash flows a net present value of zero.'<sup>59</sup>

The Tribunal noted that '[t]he Rules, as now amended, guide the regulator towards the estimate of the required rate of return through the ARORO. It is obvious, then, that the phrase "efficient financing costs" must be construed consistently with the efficiency thrust of the NEO and NGO, ie in terms of accepted notions of economic efficiency.'<sup>60</sup>

With respect to the Full Court's decision, the Tribunal noted that it considered its construction of 'efficient financing costs' in the ARORO was consistent with the Full Court's decision, stating '[t]he Tribunal sees no tension between this view and the statements by the Full Court, set out at [102] above. In particular, the term "efficient financing costs" embodies the *ex ante*, forward-looking, expectations-based framework briefly described above. This does not seem to be in contention when expressed in those broad terms.'<sup>61</sup>

The Tribunal also accepted that the new approach adopted by the AER did not rely on a definition of a benchmark efficient entity as a regulated entity. It accepted that the AER's new approach was consistent with what it had said about efficient financing costs of a benchmark efficient entity with a similar degree of risk to the particular service provider in the provision of its regulated services.<sup>62</sup>

We have applied this new conceptualisation of a benchmark entity, of a benchmark efficient entity having a similar degree of risk as the service provider in the provision of its regulated services, in all of our recent decisions including in our APA VTS determination and we would propose to adopt a similar approach in these remittals.

---

<sup>56</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p37.

<sup>57</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, pp 40 - 44.

<sup>58</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p40.

<sup>59</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p40.

<sup>60</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p42.

<sup>61</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, pp 43-44.

<sup>62</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p48.

With respect to the use of past interest rates to set the cost of debt the Tribunal stated 'the Tribunal considers that the Full Court's reasons in respect of the construction of r 6.5.2(k)(4) are not relevant to that part of the AER's reasoning.'<sup>63</sup> For the reasons outlined by the Tribunal, we consider the Full Court's comments on the construction of r 6.5.2(k)(4) are appropriately accounted for in the approach we would propose to adopt in these remitted decisions.

In relation to our conclusions that both the on-the-day methodology and a full transition could contribute to the ARORO, the Tribunal noted 'there is ample support for the AER's conclusion that the on-the-day approach to estimating the return on debt can contribute to the ARORO' and 'the AER was correct, the Tribunal finds, to take the view that the on-the-day approach could contribute to the achievement of the ARORO'.<sup>64</sup>

The Tribunal went on to state that 'the clear option is a combination of the on-the-day approach and a fully implemented HTA. The transition that the AER decided upon is such a combination. Both the on-the-day approach and the transition are specifically provided for in the Rules and it is clear that the AEMC considered that both could contribute to the ARORO in certain circumstances. It is not clear what the AEMC considered those circumstances would be, or how they would differ from each other, or even if they would differ. Rather, it considered that it was a matter for the AER in each particular case. No compelling argument was ever put why, if the fully implemented HTA approach can contribute to achievement of the ARORO, the transition to that outcome could not also contribute to the ARORO'.<sup>65</sup>

We consider the reasoning in this Tribunal decision supports our interpretation of the rules and law and economic reasoning we have applied in our recent decisions, modified in light of the decisions of the Tribunal and Federal Court, and that this new approach would be appropriate to adopt for these remittals.<sup>66</sup>

---

<sup>63</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p 49.

<sup>64</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, pp 59- 60.

<sup>65</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, pp 59- 60.

<sup>66</sup> We consider this Tribunal decision also supports a position that if we were to not use a revenue neutral transition it would be appropriate for us to continue to apply the on-the-day methodology to determine the allowed return on debt.

## 4 The approach to our remittal debt decisions we propose and consider is likely to contribute to the ARORO and best achieve the NEO and NGO

We propose to rely on the reasoning as set out in our APA VTS determination for our remitted debt decisions.<sup>67</sup> As such, we propose to move the service providers to a trailing average and apply revenue neutral transitions in moving them to this methodology. As noted by the Tribunal in its decisions for ActewAGL (Gas) distribution and Jemena Electricity Networks Ltd, our proposed approach is effectively a combination of the on-the-day methodology and trailing average methodology.<sup>68</sup>

We note that we propose to rely on our entire reasoning in our APA VTS decision in making these remittal decisions. Interested stakeholders are directed to read Attachment 3 of our APA VTS determination for further information and our full proposed reasoning.<sup>69</sup>

In the event a revenue neutral transition was precluded by the law or orders of the Tribunal or Federal Court, something we do not consider to be the case, we may apply an on-the-day approach to setting the allowed return on debt in our debt remittal decisions. We consider the use of the on-the-day methodology to set the return on debt would better achieve the ARORO, the NEO and NGO and the RPPs, than a change to a trailing average methodology without a relatively revenue neutral transition.

With respect to debt data to estimate the return on debt, we propose to use the most up to debt data from the RBA and Bloomberg for estimating the cost of debt over the relevant averaging periods. We note that the RBA has updated its cost of debt data and back cast this twice since our original determinations made in April and May 2015. Bloomberg has also removed some data from publication.

Finally, in relation to the timing of the initial debt averaging period (for the commencement of the trailing average), we propose to use the initial averaging period set out in our final determination for the introduction of the trailing average. As such, we do not propose to adopt PIAC's submission to use prevailing rates closer to the commencement of the 2015/16 regulatory year when estimating the return on debt for the NSW electricity distributors.

---

<sup>67</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017.

<sup>68</sup> Australian Competition Tribunal, Application by ActewAGL Distribution [2017] ACompT 2, October 2017, p60.

<sup>69</sup> AER, Final Decision APA VTS gas access arrangement 2018 to 2022 Attachment 3 - Rate of return, November 2017; <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/apa-victorian-transmission-system-access-arrangement-2018-22/final-decision>