



20 June 2008

By email: submissions@aemc.gov.au

Australian Energy Market Commission
Level 5, 201 Elizabeth Street
SYDNEY NSW 2001

Dear Commissioners

**Rule change proposal from Energy Users' Association of Australia
WACC Parameter Values, Equity Beta and Gamma**

Consumer Action Law Centre, Consumer Utilities Advocacy Centre and the Public Interest Advocacy Centre welcome the opportunity to provide this submission to the Australian Energy Market Commission (**AEMC**) on the rule change proposal from the Energy Users' Association of Australia (**EUAA**) regarding WACC Parameter Values, Equity Beta and Gamma (the **rule change**).

We strongly support the rule change. It is our view that the proposed amendments to the equity beta and gamma WACC parameter values are better estimates of the true value of these parameters, compared with the amounts currently fixed by the National Electricity Rules (**Rules**). The proposed amendment would ensure that the distribution and transmission businesses that are or will be subject to the current fixed parameter amounts (being the Powerlink transmission business in Queensland and the NSW and ACT distribution businesses) do not over recover compared with the relevant economic cost. Especially in relation to the NSW and ACT price review, the savings for residential consumers may be significant – up to 5% on the final consumer's electricity bill.

Problem – transitional rules allows businesses to over-recover

The new Chapter 6A of the National Electricity Rules (the **Rules**) regarding the economic regulation of transmission services and the amended Chapter 6 regarding the economic regulation of distribution services provides that the Australian Energy Regulator (**AER**) is to conduct a review of the various parameters that are used to determine the WACC. It is our understanding that these reviews will not be completed until 2009. As a transitional measure, the Rules set the WACC parameters for price distributions that are to occur before the AER's review is complete. While we understand the reason for this transitional measure, we are concerned, like the EUAA, that the amounts fixed by the Rules will enable the

network businesses subject to the fixed parameters to over-recover. This is because the values fixed by the Rules do not reflect current economic conditions.

As demonstrated by the EUAA's rule change proposal, several recent regulatory determinations have set the WACC parameter values at amounts different to those fixed by the Rules. In light of this, and the significant burden suffered by consumers of electricity if regulated businesses over-recover, we agree that the transitional WACC parameters should be fixed at the correct levels.

We are not able to provide detailed comment on the actual values being proposed by the EUAA but believe that the evidence available justifies a detailed examination by the AEMC to ensure that the values imposed are fair and efficient.

We do not, however, suggest that this rule change should necessarily pre-empt the more detailed analysis being undertaken as part of the AER WACC parameters reviews. We recognise that this would be a wasteful use of resources for two separate regulators to undertake detailed substantive reviews on the same issue. Nevertheless, considering the value to consumers of amending the fixed parameters to more appropriately reflect current economic conditions, we support the AEMC making the rule change.

We note that if the network businesses are able to over-recover pursuant to the current fixed WACC parameters, then that over-recovery will last for the duration of the regulatory period (typically 5 years, but may be longer). We would welcome the AEMC investigating the appropriateness for the WACC parameters that are set by the AER as part of its WACC parameter review to come into effect for all price determinations currently underway or already finalised from the date of the AER decision. This would potentially overcome the need for the AEMC to undertake a substantive review of WACC parameter values as part of the current rule change.

The long term interests of consumers

In the EUAA's rule change request, it states that the proposed amendment is consistent with the national electricity objective set out in section 7 of the National Electricity Law. This is because it will ensure the price of services provided by transmission and distribution businesses is not above an efficient level. The EUAA points out that if prices are above efficient levels, this can create distortions to the economy, including that household consumers of electricity will face prices above the efficient level and are therefore likely to consume less electricity and/or consume less goods and services other than electricity, than they would if prices were at the efficient level.¹

We are skeptical of this assumption. For residential consumers, the price elasticity of demand is extremely low. Much of household electricity consumption is not discretionary, but is consumed to sustain a basic standard of living. Given this, we do not believe that if prices are above efficient levels, consumers will necessarily under-consume. While some consumers may under-consume (which may lead to poor health and social outcomes, the

¹ Paragraph 80.1

costs of which will be externalised upon the state), most consumers will maintain their consumption and pay higher prices.

Despite this, we believe there are other reasons why the rule change proposal would be consistent with the national electricity objective as it impacts on residential households. The national electricity objective explicitly considers the consumer interest (emphasis added)²:

The objective of this Law is to promote efficient investment in, and efficient operation and use of, electricity services for the **long term interests of consumers** of electricity with respect to—

- (a) price, quality, safety, reliability and security of supply of electricity; and
- (b) the reliability, safety and security of the national electricity system.

In our view, the long term interests of consumers are advanced by ensuring continuous access to the affordable, reliable and safe supply of energy, in recognition that energy is an essential service to the community.³

Given the increasing pressure on household budgets and upward pressure on energy prices, it is entirely appropriate that the regulator give due consideration to measures that ensure that prices are kept to the minimum efficient level.

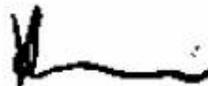
The proposed rule change is in the long term interests of consumers because it contributes to maintaining access to an affordable energy service by keeping energy prices as efficient and low as possible.

Should you have any questions, please contact Gerard Brody on 03 9670 5088.

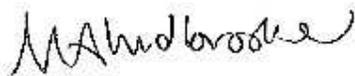
Yours sincerely



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² National Electricity Law, section 7.

³ See National Consumers Roundtable on Energy, *Charter of Principles for Energy Supply* (attached).