



18 November 2011

Mr John Pierce
Chairman,
Australian Energy Market Commission
PO Box A2449,
Sydney South NSW 1235

Dear Mr Pierce,

Proposed Rule Change – Clause 6A.6.4 of the National Electricity Rules: Value of Gamma

SP AusNet proposes a Rule change under section 91 of the National Electricity Law (NEL), which would effect a change to the value of γ (“gamma”) in clause 6A.6.4 of the National Electricity Rules.

The proposed Rule change adopts the value of gamma determined recently by the Australian Competition Tribunal. As you will be aware, the Tribunal found that the value of gamma determined by the AER reflected a number of errors in terms of approach and logic, which were later conceded by the AER. This important development renders clause 6A.6.4 anomalous because that clause requires the AER to continue to apply an erroneous value of gamma to future transmission revenue determinations in circumstances where the Tribunal has determined a correct value by commissioning a state of the art study.

A draft of the proposed Rule, showing the entire Rule 6A.6.4 is shown in Attachment 1. Attachment 2 includes a description of the proposed Rule, a statement of the issues concerning the existing Rules, and how the proposed Rule addresses those issues consistent with the National Electricity Objective.

SP AusNet requests that the AEMC consider the proposed rule change.

SP AusNet is aware that the AER has proposed a number of changes to the Rules relating to the economic regulation of electricity and gas networks. I should stress that the proposed Rule change set out in this letter and the Attachments is entirely unrelated to and independent of the wide-ranging issues raised by the AER’s proposed Rule change. This Rule change is confined to addressing an anomaly that has arisen from the Tribunal’s recent findings in relation to gamma. SP AusNet will be engaging separately in the AEMC’s consultation on the AER’s Rule change proposal, and is looking forward to a constructive dialogue on the issues raised by the AER.

Should any further details be required, please do not hesitate to contact Tom Hallam,
Manager Economic Regulation on (03) 9695 6617.

Yours sincerely,

A handwritten signature in blue ink, consisting of stylized initials 'AP' followed by a long horizontal line.

Alistair Parker
Director Regulation and Network Strategy

6A.6.4 Estimated cost of corporate income tax

- (a) The estimated cost of corporate income tax of a *Transmission Network Service Provider* for each *regulatory year* (**ETC_t**) must be calculated in accordance with the following formula:

$$ETC_t = (ETI_t \times r_t) (1 - \gamma)$$

where:

ETI_t is an estimate of the taxable income for that *regulatory year* that would be earned by a benchmark efficient entity as a result of the provision of *prescribed transmission services* if such an entity, rather than the *Transmission Network Service Provider*, operated the business of the *Transmission Network Service Provider*, such estimate being determined in accordance with the *post-tax revenue model*;

r_t is the expected statutory income tax rate for that *regulatory year* as determined by the *AER*; and

γ is the assumed utilisation of imputation credits, which is deemed to be 0.5.

For these purposes:

- (1) the cost of debt must be based on that of a benchmark efficient *Transmission Network Service Provider*; and
 - (2) the estimate must take into account the estimated depreciation for that *regulatory year* for tax purposes, for a benchmark efficient *Transmission Network Service Provider*, of assets where the value of those assets is included in the regulatory asset base for the relevant *transmission system* for that *regulatory year*.
- (b) The *AER* must, in accordance with the *transmission consultation procedures* and clause 6A.6.2(j), carry out reviews of the matters referred to in paragraph (d).
- (c) The *AER* must conclude the first review by 1 May 2009 and conclude subsequent reviews at intervals of five years with the first interval starting from 31 March 2009.
- (d) The *AER* may only review the value of and methodology used to calculate the assumed utilisation of imputation credits as referred to in paragraph (a) (or as subsequently revised under this clause 6A.6.4).
- (e) Where the value of the assumed utilisation of imputation credits referred to in paragraph (d) cannot be determined with certainty, the *AER* must have regard to:
- (1) the need to achieve an outcome that is consistent with the *national electricity objective*; and

- (2) the need for persuasive evidence before adopting a value that differs from the value that has previously been adopted for it.
- (f) Subject to clause, 6A.6.4(g), if, as a consequence of a review, the *AER* decides to adopt a revised value or methodology, it must use that revised value or methodology, but only for the purposes of a *Revenue Proposal* that is submitted to the *AER* under clause 6A.10.1(a) after the completion of the first review or after completion of the five yearly reviews (as the case may be).
- (g) Notwithstanding clause 6A.6.4(f), if the Australian Competition Tribunal determines that the *AER*'s most recent review of the matters referred to in clause 6A.6.4(d) resulted in an error or errors, and as a consequence of that determination, a different methodology or value is ascribed to the assumed utilisation of imputation credits, the *AER* must use that different methodology or value for the purposes of clause 6A.6.4(f).

Attachment 2

SP AusNet Rule Change Proposal - Clause 6A.6.4

1. Summary

SP AusNet proposes a Rule change under section 91 of the National Electricity Law (NEL), which would correct the errors in the current value of γ ("gamma") for forthcoming transmission revenue determinations. The correct value for gamma has been determined by the Australian Competition Tribunal (Tribunal) following appeals lodged by electricity distributors ETSA Utilities, Energex and Ergon Energy¹.

The Tribunal found errors in the AER's assessment of gamma, which is set out in the AER's Statement of Regulatory Intent (SORI)². The Tribunal commissioned a 'state of the art' study, which determined that gamma should be 0.25.

The current Rules applying to Transmission Network Service Providers (TNSPs) continue to 'lock in' the AER's value of gamma, which is 0.65. The gamma value can only be amended for Revenue Proposals that are submitted after the AER completes its scheduled review in March 2014, even though it is known now that the value of gamma is incorrect.

The Rules for TNSPs differ from those that apply to electricity distributors and gas networks, where the gamma is not 'locked in'. It is anomalous that the current Rules require a known error in relation to gamma to be perpetuated in future transmission revenue determinations until March 2014. The anomaly is exacerbated because it is confined to TNSPs while determinations for other energy networks will be able to adopt the correct gamma value. The current Rules distort incentives for efficient investment and are inconsistent with the Revenue and Pricing Principles in the NEL.

SP AusNet's Rule change proposal will contribute to the achievement of the National Electricity Objective. In particular, by ensuring that tax costs are correctly recognised, the Rule change will provide the appropriate incentives for efficient investment. The counterfactual proposition – that the existing Rules are maintained – will encourage transmission investment to be deferred until the value of gamma is corrected. It is poor regulatory practice to apply a value for gamma which is known to be incorrect, especially as the Tribunal has committed substantial resources to determine a correct estimate.

In terms of its application, it is important to note that:

- The Rule change proposal does not apply retrospectively. It will only apply to future transmission revenue determinations, where the Revenue Proposal is submitted prior to the completion of the AER's next five yearly review of the WACC and tax parameters, which is scheduled for 31 March 2014;

¹ Application by Energex Limited (Gamma) (No 5) [2011] ACompT 9 (12 May 2011).

² AER, Electricity Transmission and Distribution Network Service Providers: Review of the Weighted Average Cost of Capital (WACC) parameters, May 2009, page 466 and 467.

- The Rule change proposal does not undermine or pre-judge the outcome from the AER's scheduled review of the WACC and tax parameters. Instead, the Rule change only has the effect of correcting errors in the AER's 2009 SORI, in accordance with the Tribunal's findings; and
- The Rule change proposal involves minimal drafting changes that are unrelated to and independent of the matters raised by the AER in its recent Rule change proposal.

2. Background

2.1 Development and operation of the existing Rules

In developing the current Rules in relation to the WACC and tax parameters for TNSPs, the AEMC commented as follows:

"There has been widespread acceptance of the capital asset pricing model (CAPM) as the analytical basis for estimating the regulatory cost of capital. Although there has been ongoing debate about the parameter values used by the regulator to estimate the WACC at each revenue reset, there has been a high degree of stability in the parameter values adopted by the regulator in recent years. Considering these circumstances the Commission believes that the cost and uncertainty associated with continually reopening both the methodology and parameters at each revenue cap review is unwarranted in terms of any potential benefits and the administrative costs.

Providing short term stability regarding the WACC determination reduces an important source of potential variability in regulatory decision making thereby providing a more certain and predictable environment for investment and financing decision making. This is consistent with the approach adopted by the AER under the SRP³, however, this was an administrative document which could be departed from at any time. The provisions codified in the Revenue Rule therefore largely represent current practice. However, it is also recognised that the methodology and parameters for the cost of capital are matters that the regulator must be able to review periodically and to exercise discretion and judgement as to whether there is a case for change.

Enabling the AER to review the methodology and parameters periodically and make appropriate changes provides appropriate flexibility and discretion for the regulator to take account of changes in financial market conditions and developments in finance theory and practice. For this reason the Revenue Rule gives the AER the discretion to vary the WACC methodology or parameters at subsequent five-yearly reviews following the consultation process in the Rules."⁴

In light of the above reasoning, the AEMC firstly determined the relevant WACC and tax parameter values that should apply to TNSPs and, secondly, allowed these values to be reviewed by the AER by May 2009 (2009 SORI) and at five yearly intervals thereafter, with the next review to be concluded by 31 March 2014⁵.

³ Statement of Regulatory Principles.

⁴ AEMC, Rule Determination, National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 No.18, 16 November 2006, page 82.

⁵ National Electricity Rules, clause 6A.6.2(g).

In its 2009 SORI, the AER reached the following conclusions in relation to the value of gamma:

“Based on the evidence considered most relevant, reliable, comprehensive and theoretically appropriate, the AER considers that a reasonable estimate of gamma lies in the range 0.57 and 0.74. For clarity it is noted that:

- A payout ratio of 1.0 has been adopted, consistent with a free cash flow approach to valuation and the Officer WACC framework,
- The lower bound estimate of 0.57 is based on the AER’s best estimate of theta inferred from market prices, and
- The upper bound estimate of 0.74 is based upon the AER’s best estimate of theta from tax statistics.”⁶

The AER determined that gamma should be the midpoint between 0.57 and 0.74, being 0.65. The AER concluded its analysis in the following terms:

“In accordance with the NER, the AER considers that a gamma value of 0.65:

- is supported by the most recent available and reliable empirical evidence, which the AER considers is persuasive in support of a change to the existing value, and
- generates a forward looking rate of return that is commensurate with prevailing conditions in the market for funds and the risk involved in providing prescribed transmission services or standard control services (as the case may be).

In determining the value of imputation credits, the AER has also taken into account the revenue and pricing principles. The AER considers the value of imputation credits of 0.65 for a benchmark efficient NSP:

- together with values, methods and a credit rating for the other parameters, provides a service provider with a reasonable opportunity to recover at least the efficient costs and provides a service provider with effective incentives for efficient investment, and
- is appropriate having regard to the economic costs and risks of the potential framework in under and over investment.

On this basis, the AER considers that its proposed value achieves an outcome that is consistent with and is likely to contribute to the achievement of the NEO [National Electricity Objective].”⁷

In accordance with the Rules for the economic regulation of transmission services, the value of gamma is therefore ‘locked in’ at 0.65 until the AER reviews the value through its five yearly process, which is scheduled to be completed by March 2014. For SP AusNet, the current Rules will have the effect of applying a value of 0.65 for

⁶ AER, Electricity Transmission and Distribution Network Service Providers: Review of the Weighted Average Cost of Capital (WACC) parameters, May 2009, page 467.

⁷ Ibid, pages 468 and 469.

gamma for the duration of its next transmission revenue determination, which will expire on 30 March 2019 at the earliest.⁸

2.2 Tribunal findings in relation to the distributors' gamma appeal

The Rules relating to electricity distributors⁹ differ from those that apply to TNSPs because they allow the WACC and tax parameters to be varied in each company's price determination, providing that persuasive evidence for change can be provided. The price review submissions made by ETSA Utilities, Ergon Energy and Energex in relation to the value of gamma were rejected by the AER. Instead, the AER maintained its reasoning as set out in the 2009 SORI to conclude that the value of gamma is 0.65. The companies appealed the AER's determination to the Tribunal.

The value of gamma is determined by the product of the distribution ratio (F) and the utilisation rate (theta). In relation to the AER's conclusion that the distribution ratio should be 1, during the Tribunal process the AER conceded that it had made an error of fact:

"The AER also submits that it is open to the Tribunal to conclude that the AER made an error of fact in making the gamma constituent decision, insofar as it related to the distribution ratio, that was material to the making of each distribution determination."¹⁰

"The Tribunal accepts the AER's submissions and finds that an error of fact occurred in the making of the distribution ratio."¹¹

The AER subsequently conceded that the distribution ratio should be set at 0.7.¹²

In relation to the value of the utilisation rate (theta), the Tribunal found that the AER's approach of averaging the results from a tax study and a dividend drop-off study was based on a logical error:

"But this simple averaging adjustment has no logic to it and fails to accord each Handley and Maheswaran (2008) estimate its correct interpretation as an upper bound applying to a period. The fact that the AER chose a simple average rather than using the Handley and Maheswaran (2008) estimate for the combined period 1988-2004 is immaterial to the AER's error, since any downward adjustment to a properly derived upper bound would be inappropriate as a means of deriving an estimate of theta."¹³

It is important to note that the errors identified by the Tribunal were repeated from the AER's 2009 SORI. In particular, as noted already, the AER adopted a distribution ratio

⁸ The current determination expires on 30 March 2014 and the next determination would be subject to the 2009 SORI. The minimum regulatory period is 5 years, which means that a gamma of 0.65 will apply until 30 March 2019 at the earliest.

⁹ As an aside, the Rules for gas networks are more flexible in relation to WACC. However, it is important to note that the Rule change proposal does not seek to equilibrate the WACC arrangements between the sectors.

¹⁰ Application by Energex Limited (No 2) [2010] ACompT 7 (13 October 2010), paragraphs, paragraph 48.

¹¹ Ibid, paragraph 52.

¹² Application by Energex Limited (Gamma) (No 5) [2011] ACompT 9 (12 May 2011), paragraph 8.

¹³ Application by Energex Limited (No 2) [2010] ACompT 7 (13 October 2010), paragraph 95.

and utilisation rate of 1 and 0.65 respectively, using on the same averaging approach as described above. Therefore, the following conclusions from the Tribunal's October 2010 decision apply equally to the reasoning in the 2009 SORI:

"The Tribunal is now in the position where it has found error by the AER in its treatment of both the distribution ratio, F, and the franking credit utilisation rate, θ . However, it is not yet in a position to correct those errors. Rather, it requires a report from the AER that addresses the errors found and the further comments of the Tribunal."¹⁴

The Tribunal also rejected the AER's view that the principle of regulatory inertia justified leaving the value of gamma unchanged at 0.65:

"In its submission, the AER re-agitated one of its earlier arguments: that the Rules establish a regime of regulatory inertia whereby values of the WACC parameter set in the Statement of Regulatory Intent ('SORI') will govern the distribution determinations that are made during the following five years unless, and to the extent that, it is shown that a departure from the SORI values is justified.

The Tribunal accepts that due regard should be given to historical consistency in applying regulatory values over time. Nevertheless, the Tribunal, standing in the AER's shoes, is inescapably required to exercise regulatory judgment in determining the appropriate value of theta.

The Tribunal must determine an appropriate value for gamma on the basis of the material before it. It does not accept that its task is to determine a value of gamma that is appropriate and not too different from the previously determined value of gamma. That gives too little policy weight to the objective set out in s 7A of the NEL that a regulated DNSP should be provided with a reasonable opportunity to recover at least the efficient costs it incurs. That objective must outweigh any presumption of regulatory inertia. In any event, within the SORI framework by which the AER argues for the principle of regulatory inertia, the Tribunal has persuasive evidence justifying a departure from previously determined values of gamma."¹⁵

Following the Tribunal's decision in October 2010, a further dividend drop-off study by independent expert, SFG, was commissioned under the direction of the Tribunal. The Tribunal described this purpose of this report in the following terms:

"In respect of θ , the Tribunal seeks a report that:

- proposes an approach that correctly uses tax statistics studies and dividend drop-off studies;
- reviews dividend drop-off studies from as many sources as possible to see whether confident use can be made of any of them; and
- if possible, provides results from a newly-commissioned dividend drop-off study that is "state of the art".¹⁶

¹⁴ Ibid, paragraph 145.

¹⁵ Ibid, paragraph 146.

¹⁶ Application by Energex Limited (Gamma) (No 5) [2011] ACompT 9 (12 May 2011), paragraphs 35-37.

The Tribunal reached the following conclusion in relation to the report that was subsequently produced by the independent expert, SFG:

“The Tribunal is satisfied that SFG’s March 2011 report is the best dividend drop-off study currently available for the purpose of estimating gamma in terms of the Rules. Its estimate of a value of 0.35 for theta should be accepted as the best estimate using this approach. In particular, the Tribunal cannot accept the submission of the AER that either minor issues in the construction of the database or multicollinearity argue for giving the SFG study less weight and the Beggs and Skeels study some weight. The Beggs and Skeels study, despite not being subjected to anything like the same level scrutiny, is known to suffer by comparison with the SFG study on those and other grounds.

Moreover, the fact that in its earlier reasons the Tribunal found no error in the AER having relied on the Beggs and Skeels study is not to the point. The proceedings since then have been largely designed to render that study, along with the earlier SFG study, obsolete for the purpose of setting a value for gamma – and have done so.”¹⁷

The Tribunal concluded its findings in relation to the appropriate value of gamma as follows:

“Taking the values of the distribution ratio and of theta that the Tribunal has concluded should be used, viz 0.7 and 0.35, respectively, the Tribunal determines that the value of gamma is 0.25.”¹⁸

3. Reasons for Proposed Rule Change

3.1 General Statement of Issues

The existing Rules ‘lock in’ the value of gamma at 0.65 for TNSPs until the AER concludes its next review of the WACC and tax parameters, which is scheduled for March 2014. In particular, clause 6A.6.4(f) states:

“If, as a consequence of a review, the AER decides to adopt a revised value or methodology, it must use that revised value or methodology, but only for the purposes of a *Revenue Proposal* that is submitted to the AER under clause 6A.10.1(a) after the completion of the first review or after completion of the five yearly reviews (as the case may be).”

It is important to recall that the AEMC established the current Rules to provide TNSPs with an environment that will encourage investment:

“Providing short term stability regarding the WACC determination reduces an important source of potential variability in regulatory decision making thereby providing a more certain and predictable environment for investment and financing decision making.”¹⁹

¹⁷ Application by Energex Limited (Gamma) (No 5) [2011] ACompT 9 (12 May 2011), paragraphs 29 and 30.

¹⁸ Ibid, paragraph 42.

¹⁹ AEMC, Rule Determination, National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 No.18, 16 November 2006, page 82.

SP AusNet supports the AEMC's objectives in drafting the current Rules. Unfortunately, the intended operation of the Rules has been undermined by the following developments:

- The subsequent drafting of the electricity distribution Rules and the National Gas Rules provide more scope for the AER to vary the WACC and tax parameters from the values determined in the SORI;
- The AER's 2009 SORI increased gamma from 0.5 to 0.65, based on errors in relation to both the distribution ratio and the utilisation rate;
- The AER's value for gamma in the SORI was the subject of a successful merits review; and
- The Tribunal commissioned a 'state of the art' dividend drop-off study, which determined the value for gamma to be 0.25.

These unforeseen events have rendered clause 6A.6.4(f) anomalous. In particular:

- A gamma value of 0.65 is required to be adopted in future transmission revenue determinations, even though this value is known to be incorrect and should be 0.25; and
- Electricity distribution and gas networks will be able to adopt the correct value for gamma, whilst transmission electricity networks will be precluded from doing so.

A gamma of 0.65 is inconsistent with the Revenue and Pricing Principles in the NEL. In particular, subsection 7A(2) states that:

"A regulated network service provider should be provided with a reasonable opportunity to recover at least the efficient costs the operator incurs in—

- (a) providing direct control network services; and
- (b) complying with a regulatory obligation or requirement or making a regulatory payment."

SP AusNet proposes a Rule change that will allow the AER to adopt a gamma value of 0.25 as determined by the Tribunal, rather than continuing to apply the incorrect value of 0.65, as specified in the 2009 SORI. As explained in further detail below, correcting the value of gamma will promote the achievement of the National Electricity Objective.

3.2 Description of Rule change

It is proposed that Rule 6A.6.4(f) is qualified by a new Rule 6A.6.4(g) as set out below:

6A.6.4 Estimated cost of corporate income tax

- (f) “Subject to clause 6A.6.4 (g), if, as a consequence of a review, the AER decides to adopt a revised value or methodology, it must use that revised value or methodology, but only for the purposes of a *Revenue Proposal* that is submitted to the AER under clause 6A.10.1(a) after the completion of the first review or after completion of the five yearly reviews (as the case may be).”
- (g) Notwithstanding clause 6A.6.4(f), if the Australian Competition Tribunal determines that the AER’s most recent review of the matters referred to in clause 6A.6.4(d) resulted in an error or errors, and as a consequence of that determination, a different methodology or value is ascribed to the assumed utilisation of imputation credits, the AER must use that different methodology or value for the purposes of clause 6A.6.4(f).

The remainder of Rule 6A.6.4 would remain as presently drafted.

3.3 Implications of Change

As explained above, the effect of the proposed change is to ensure that future revenue determinations for TNSPs will not continue to apply an erroneous value for gamma in circumstances where the Tribunal has corrected the error.

The Rule change applies prospectively and does not pre-judge or encroach upon the AER’s scheduled review of the WACC and tax parameter values, which must be completed by March 2014. Specifically, the effect of the proposed clause 6A.6.4(g) is that the value of gamma determined by the Tribunal will replace the value set out in the 2009 SORI, which is known to contain errors. The value of gamma determined by the AER in subsequent five yearly reviews will not be affected by the Tribunal’s May 2011 decision.

SP AusNet is aware that the AER has proposed a number of changes to the Rules relating to the economic regulation of electricity and gas networks. The Rule change proposed herein is entirely unrelated to and independent of the wide-ranging issues raised by the AER’s proposed Rule change. The matter addressed by this Rule change is limited to addressing an anomaly that has arisen from the Tribunal’s recent findings in relation to gamma.

4 SP AusNet’s Right to Submit this Proposal

SP AusNet requests that the AEMC approve this proposed Rule in accordance with section 91 of the NEL. SP AusNet is registered as a TNSP in accordance with Section 2.5 of the NER.

Under section 91(1) of the NEL, the AEMC may make a Rule at the request of any person, the MCE or the Reliability Panel. As such, SP AusNet may request that the AEMC make or amend a Rule.

5 Power of the AEMC to Make the Proposed Rule

The subject matter about which the AEMC may make Rules is set out in section 34 of the NEL.

SP AusNet considers that the proposed Rule falls within the subject matters that the AEMC may make Rules about, as it relates to the activities of persons participating in the NEM.

6. How the Proposed Rules Contribute to the National Electricity Objective

Before the AEMC can make a Rule change, it must apply the rule making test set out in the NEL, which requires it to assess whether the proposed Rule will or is likely to contribute to the National Electricity Objective.

The National Electricity Objective is defined by section 7 of the NEL as follows:

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

SP AusNet considers that the proposed Rule change is likely to contribute to the National Electricity Objective for the following reasons:

- Efficient investment in regulated assets is not promoted by allowing an erroneous value for gamma to continue to be applied when a better value has been determined by the Tribunal. The Rule change proposal will enable the correct value of gamma to be applied in future transmission determinations.
- The Revenue and Pricing Principles in the NEL also support the adoption of a correct gamma value. In particular, to continue to apply a gamma of 0.65 would not be consistent with subsection 7A(2), which states that a regulated network service provider should be provided with a reasonable opportunity to recover at least its efficient costs. The Revenue and Pricing Principles are consistent with and support the National Electricity Objective, as noted by the AER in its 2009 SOR²⁰.
- Incentives for efficient investment will be distorted in circumstances where the value of gamma is knowingly set too low. In particular, such an outcome provides a strong incentive for a TNSP to defer capital expenditure to a later period when the value of gamma will be corrected. For SP AusNet, this future period will not commence before 1 April 2019, and therefore the distorted incentives will apply for a prolonged period. The proposed Rule change will ensure that the correct value

²⁰ AER, Electricity Transmission and Distribution Network Service Providers: Review of the Weighted Average Cost of Capital (WACC) parameters, May 2009, page 469.

of gamma is applied at the next revenue determination and thereby provide appropriate incentives for investment, consistent with the National Electricity Objective.

- A similar issue arises in relation to the choice between transmission and distribution investment. As noted above, the electricity distribution Rules allow the value of gamma to be set at 0.25. Allowing a different value for gamma between the electricity transmission and distribution sectors distorts the investment incentives between the two networks. Avoiding such a distortion is consistent with the National Electricity Objective.
- As the Rule change promotes efficient investment it is likely to benefit customers in terms of the quality, reliability and security of supply.

7. Expected Benefits and Costs of the Proposed Rule

As discussed above, the proposed Rule change will promote the achievement of the National Electricity Objective by avoiding outcomes that would be inconsistent with the Revenue and Pricing Principles and that would distort the incentives to invest. The benefits from the Rule change will be derived from appropriate transmission prices that enable TNSPs to recover their efficient costs and by providing appropriate incentives to invest.

A further benefit from the Rule change is that it makes proper use of the substantial resources committed by the Tribunal to correct the errors in the 2009 SORI and in commissioning a state of the art dividend drop-off study.

SP AusNet does not expect that there will be any changes to market systems, additional compliance, procedural or other administrative costs arising from implementing this proposed Rule change.

The drafting changes are minimal and do not require any further work to be undertaken by the AER or interested parties.

In summary, SP AusNet considers that the benefits in promoting the National Electricity Objective substantially outweigh the cost associated with the impact of the proposed Rule change.

8 Glossary

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
NEL	National Electricity Law
NEM	National Electricity Market
NER	National Electricity Rules
TNSP	Transmission Network Service Provider