

# GRC0011 Price and Revenue Regulation of Gas Services

## AEMC Final Position Rules: Amendments to the National Gas Rules

15 November 2012

### [1] Rule 3 Interpretation

In rule 3, insert the following definitions in alphabetical order:

*allowed rate of return* see rule 87(1).

*allowed rate of return objective* see rule 87(3).

*rate of return consultative procedure* means the procedure for consultative decision making laid down in rule 9B.

*rate of return guidelines* means the guidelines made under rule 87.

### [2] New Rule 9B Rate of return consultative procedure

After Rule 9A insert:

#### 9B Rate of return consultative procedure

- (1) If the Law requires a *decision* maker to comply with the *rate of return consultative procedure* in making, amending, replacing or reviewing the *rate of return guidelines*, the *decision* maker must proceed in accordance with this rule.
- (2) The *decision* maker must proceed as follows:
  - (a) the *decision* maker must publish a notice on its website and in a newspaper circulating generally throughout Australia:
    - (i) describing the proposed *rate of return guidelines*, amendments or review, and giving the address of a website on which the details of such guidelines, amendments or review, and the reasons for them, are published; and
    - (ii) inviting written submissions on the proposed *rate of return guidelines*, amendments or review within no less than 30 *business days* of the date of the notice;
  - (b) the *decision* maker may publish such issues, consultation and discussion papers, and hold such conferences and information sessions in relation to the proposed *rate of return guidelines*, amendments or review as it considers appropriate; and
  - (c) the *decision* maker must, within 80 *business days* of the date of the notice referred to in subrule (2)(a) and after considering relevant submissions made within the time allowed in the notice and other matters the *decision* maker considers relevant, make its final *decision*.
- (3) The final *decision* must:
  - (a) be in writing; and
  - (b) state the terms of the *decision* and the reasons for it; and

- (c) include a summary of each issue raised in submissions, that the *decision* maker reasonably considers to be material, together with the *decision* maker's response to each such issue.
- (4) The *decision* maker may extend the time within which it is required to make its final *decision* if:
  - (a) the consultation involves issues of unusual complexity or difficulty; or
  - (b) the extension of time has become necessary because of circumstances beyond the *decision* maker's control.
- (5) After making a final decision, the *decision* maker must, without delay:
  - (a) publish the final *decision* on the *decision* maker's website; and
  - (b) make the final *decision* available for inspection during business hours at the *decision* maker's public offices.

### **[3] Rule 72                      Specific requirements for access arrangement information relevant to price and revenue regulation**

Omit rule 72(g) and 72(h) and substitute:

- (g) the proposed return on equity, return on debt and *allowed rate of return*, for each regulatory year of the *access arrangement period*, in accordance with rule 87, including any departure from the methodologies set out in the *rate of return guidelines* and the reasons for that departure;
- (ga) the proposed formula (if any) that is to be applied in accordance with rule 87(12);
- (h) the estimated cost of corporate income tax calculated in accordance with rule 87A, including the proposed value of imputation credits referred to in that rule;

### **[4] Rule 76                      Total revenue**

Omit rule 76(c) and substitute:

- (c) the estimated cost of corporate income tax for the year (See Division 5A); and

### **[5] Rule 87                      Rate of return**

Omit rule 87 and substitute:

- (1) Subject to rule 82(3), the return on the projected capital base for each regulatory year of the *access arrangement period* is to be calculated by applying a rate of return that is determined in accordance with this rule 87 (the *allowed rate of return*).
- (2) The *allowed rate of return* is to be determined such that it achieves the *allowed rate of return objective*.
- (3) The *allowed rate of return objective* is that the rate of return for a service provider is to be 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 the provision of reference services (the *allowed rate of return objective*).
- (4) Subject to subrule (2), the *allowed rate of return* for a regulatory year is to be:

- (a) a weighted average of the return on equity for the *access arrangement period* in which that regulatory year occurs (as estimated under subrule (6)) and the return on debt for that regulatory year (as estimated under subrule (8)); and
  - (b) determined on a nominal vanilla basis that is consistent with the estimate of the value of imputation credits referred to in rule 87A.
- (5) In determining the *allowed rate of return*, regard must be had to:
- (a) relevant estimation methods, financial models, market data and other evidence;
  - (b) the desirability of using an approach that leads to the consistent application of any estimates of financial parameters that are relevant to the estimates of, and that are common to, the return on equity and the return on debt; and
  - (c) any interrelationships between estimates of financial parameters that are relevant to the estimates of the return on equity and the return on debt.

#### **Return on equity**

- (6) The return on equity for an *access arrangement period* is to be estimated such that it contributes to the achievement of the *allowed rate of return objective*.
- (7) In estimating the return on equity under subrule (6), regard must be had to the prevailing conditions in the market for equity funds.

#### **Return on debt**

- (8) The return on debt for a regulatory year is to be estimated such that it contributes to the achievement of the *allowed rate of return objective*.
- (9) The return on debt may be estimated using a methodology which results in either:
  - (a) the return on debt for each regulatory year in the *access arrangement period* being the same; or
  - (b) the return on debt (and consequently the *allowed rate of return*) being, or potentially being, different for different regulatory years in the *access arrangement period*.
- (10) Subject to subrule (8), the methodology adopted to estimate the return on debt may, without limitation, be designed to result in the return on debt reflecting:
  - (a) the return that would be required by debt investors in a benchmark efficient entity if it raised debt at the time or shortly before the time when the AER's *decision* on the access arrangement for that *access arrangement period* is made;
  - (b) the average return that would have been required by debt investors in a benchmark efficient entity if it raised debt over an historical period prior to the commencement of a regulatory year in the *access arrangement period*; or
  - (c) some combination of the returns referred to in subrules (a) and (b).
- (11) In estimating the return on debt under subrule (8), regard must be had to the following factors:

- (a) the desirability of minimising any difference between the return on debt and the return on debt of a benchmark efficient entity referred to in the *allowed rate of return objective*;
  - (b) the interrelationship between the return on equity and the return on debt;
  - (c) the incentives that the return on debt may provide in relation to capital expenditure over the *access arrangement period*, including as to the timing of any capital expenditure; and
  - (d) any impacts (including in relation to the costs of servicing debt across *access arrangement periods*) on a benchmark efficient entity referred to in the *allowed rate of return objective* that could arise as a result of changing the methodology that is used to estimate the return on debt from one *access arrangement period* to the next.
- (12) If the return on debt is to be estimated using a methodology of the type referred to in subrule (9)(b) then a resulting change to the service provider's total revenue must be effected through the automatic application of a formula that is specified in the *decision* on the access arrangement for that *access arrangement period*.

### **Rate of return guidelines**

- (13) The AER must, in accordance with the *rate of return consultative procedure*, make and publish guidelines (the *rate of return guidelines*).
- (14) The *rate of return guidelines* must set out:
- (a) the methodologies that the AER proposes to use in estimating the *allowed rate of return*, including how those methodologies are proposed to result in the determination of a return on equity and a return on debt in a way that is consistent with the *allowed rate of return objective*; and
  - (b) the estimation methods, financial models, market data and other evidence the AER proposes to take into account in estimating the return on equity, the return on debt and the value of imputation credits referred to in rule 87A.
- (15) There must be *rate of return guidelines* in force at all times after the date on which the AER first publishes the *rate of return guidelines* under these rules.
- (16) The AER must, in accordance with the *rate of return consultative procedure*, review the *rate of return guidelines*:
- (a) at intervals not exceeding three years, with the first interval starting from the date that the first *rate of return guidelines* are published under these rules; and
  - (b) at the same time as it reviews the Rate of Return Guidelines under clauses 6.5.2 and 6A.6.2 of the National Electricity Rules.
- (17) The AER may, from time to time and in accordance with the *rate of return consultative procedure*, amend or replace the *rate of return guidelines*.
- (18) The *rate of return guidelines* are not mandatory (and so do not bind the AER or anyone else) but, if the AER makes a *decision* in relation to the rate of return (including in an access arrangement draft *decision* or an access arrangement final *decision*) that is not in accordance with them, the AER must state, in its reasons for the *decision*, the reasons for departing from the guidelines.

- (19) If the *rate of return guidelines* indicate that there may be a change of regulatory approach by the *decision maker* in future *decisions*, the guidelines should also (if practicable) indicate how transitional issues are to be dealt with.

## Division 5A

### 87A Estimated cost of corporate income tax

- (1) The estimated cost of corporate income tax of a service provider for each regulatory year of an *access arrangement period* (ETC<sub>t</sub>) is to be estimated in accordance with the following formula:

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

Where

ETI<sub>t</sub> 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 reference services if such an entity, rather than the service provider, operated the business of the service provider;

r<sub>t</sub> is the expected statutory income tax rate for that regulatory year as determined by the AER; and

γ is the value of imputation credits.

**[END OF FINAL POSITION RULE]**