



INDEPENDENT PRICING AND REGULATORY TRIBUNAL
OF NEW SOUTH WALES

Our Reference :

Contact: Fiona Towers
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22 March 2006

Dr John Tamblyn
Chairman
Australian Energy Market Commission
Level 16
1 Margaret St
SYDNEY 2000

RECEIVED
27 MAR 2006

Dear Dr Tamblyn,

Review of the electricity transmission revenue and pricing Rules

The Independent Pricing and Regulatory Tribunal (the Tribunal) is currently the jurisdictional regulator of electricity and gas distribution businesses in NSW, regulating the energy businesses under the National Electricity Rules (the Electricity Rules) and the National Third Party Access Code for Natural Gas Pipeline Systems (the Gas Code).

The Tribunal considers that the AEMC's approach to the electricity transmission revenue Rules could, where appropriate, be translated into the Rules governing electricity and gas distribution. Therefore, the Tribunal is making some high-level comments relating to the Commission electricity transmission revenue Rule proposal.

In its experience in regulating businesses, the Tribunal considers that a price determination is a 'regulatory package' that involves balancing competing objectives. In each review that the Tribunal has undertaken it has been faced with circumstances specific to each business. While it is possible to achieve a level of consistency in the regulatory approach, regard must be had to the individual circumstances of each business. It is, therefore, necessary that the regulator have a level of discretion to ensure that the 'regulatory package' that it delivers is appropriate.

More specifically, the Tribunal notes that the AEMC is reducing the regulator's discretion in relation to the weighted average cost of capital (WACC). In its experience, the Tribunal has found that appropriate discretion around the WACC can assist in delivering a balanced outcome. Further, prescribing the WACC approach together with the required financial outcomes (through requiring BBB credit rating) could leave the regulator with unachievable requirements.

It is important that economic regulation in Australia continues to evolve to ensure that the regulatory package is best practice. Making the Rules highly prescriptive will require changes to the regulatory package to be done through a formal Rule making process. Because the AEMC cannot initiate Rule changes (after the initial process), interested persons will need to propose Rule changes. Future Rule change proposals may not be as comprehensive as the current Rule change process that the AEMC is undertaking, with interested persons proposing changes to only part of the 'regulatory package'. It is unclear

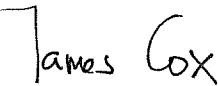
whether the AEMC will be able to address other matters that may, in best practice, change as a result of the proposed Rule change.

Arguably, a prescriptive set of Rules will attract more Rule change proposals. A large number of Rule change proposals could lead to greater uncertainty for stakeholders.

The Tribunal notes that, subsequent to the AEMC releasing its Rule proposal, the Expert Panel on Energy Access Pricing has released its draft report. It is unclear how the Expert Panel's advice on a common approach to revenue and network pricing across the energy market will relate to the AEMC's Rule change process. The Tribunal is supportive of the findings of the Expert Panel. In particular, the Tribunal supports the Expert Panel's view on the propose-respond model. The Tribunal has experience under both the Gas Code 'propose-respond' model and the 'regulator determines' model under the Electricity Rules. The Tribunal considers that it can deliver a more appropriate package under the 'regulator determines' model and has tried to adopt this approach to the greatest extent possible under the Gas Code. The Tribunal notes that the AEMC, in its proposed Rules, has improved upon the current model under the Gas Code, but reiterates its view that the 'regulator determines' model is preferable.

If you would like to discuss our views, we will be available to meet with you.

Yours sincerely,

A handwritten signature in black ink that reads "James Cox". The signature is written in a cursive style with a large, stylized 'J' and 'C'.

Mr James Cox
Chief Executive Officer
Full Time Member