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12 July 2012

Australian Energy Market Commission
Via online submission at www.aemc.gov.au

ERC0134 – Cost of Debt Issues

APA Group welcomes the opportunity to make a submission to the AEMC's additional consultation paper on Cost of Debt issues and the proposal raised by Queensland Treasury Corporation (QTC).

In general, APA Group understands the motivation behind the QTC proposal, and would support a Rule that provides optionality which enables the regulated entity to choose a cost of debt approach relevant to it business. This optionality would include enabling the business to elect to have its cost of debt calculated by reference to its debt portfolio hedging activities.

Optionality is important

APA Group submits that it is important to allow the regulated business to choose a cost of debt approach relevant to its business. This need for optionality arises because the structures of the regulated businesses differ across the sector.

In the case of a government owned business, or a single asset business, the scope to hedge the debt portfolio against regulatory determinations may be important for the prudent financial management of the business. In this circumstance, it would be sensible to allow the business to choose this option.

However, in the case of a publicly traded business, the regulator's decisions on cost of capital can carry significant financial market information. To the extent that financial market participants are not across the detail of how the "historical rolling average" cost of debt has been calculated in regulatory determinations, there is scope for the regulator's cost of capital decisions to send inappropriate signals to the market which may impact the business' ability to compete for capital.

It is critical, from a market information perspective, that the regulatory cost of capital be consistent with the cost of funds prevailing in the marketplace at the time the regulatory decision is reached.

It is of paramount importance, therefore, that the business should be able to elect the cost of debt approach to be applied – it would be inappropriate to impose a particular cost of debt approach through inflexible Rules.

We would be pleased to discuss this in more detail at your convenience. Please contact Scott Young on (02) 9275 0031 or scott.young@apa.com.au.

Yours Faithfully

Scott Young

for Peter Bolding
General Manager Regulatory and Strategy