

Utility Regulation in New Zealand

John Small*

As a result of legislative amendments in 2008, New Zealand is now starting on a third distinct and innovative approach to the economic regulation of basic infrastructure assets. Compared to previous versions, the new regime is expected to make the regulator's analysis more transparent, consistent and predictable. It does this by requiring that detailed 'input methodologies' for regulatory cost modelling are determined before being used to set constraints. There is also greater flexibility for the regulator, with new forms of oversight and control being made available. The new regime is best understood as evolving from New Zealand's regulatory history and the broader history of official economic thought in the country. This paper reviews New Zealand's recent regulatory history and describes the new regime that lies ahead.

Current Situation

The Commerce Commission ('Commission') regulates the prices of network services in the electricity and gas industries. Each also has a separate regulator of trading activities: the Electricity Commission and the Gas Industry Company respectively, the latter being a co-regulatory body. The Commission also regulates access to raw milk (where one national co-operative has a degree of market power) and the

telecommunications industry.

This situation was maintained by legislative amendments in 2008, at which time airports fell within the Commission's scope and additional forms of regulation were enabled, including a negotiate/arbitrate process and a more flexible default/customised structure for setting price and quality paths. Perhaps more significantly, the process of regulation also changed. The Commission is now required to describe its regulatory methodologies in detail before applying them, and to survive a robust appeals process available to firms. There is an interesting history of thought behind these moves.

Light-Handed Regulation 1984-1999

The widespread liberalisation of the New Zealand economy that began in the mid 1980s was predicated on the view that regulation was far too pervasive. There was indeed a sound economic basis for that position in many parts of the economy, including in the government sector.

Policy reforms opened markets to competitive entry and reduced the compliance cost of starting a business. However the official antipathy towards regulation was sufficiently strong that it extended to situations in which it is difficult to imagine markets delivering workable competition, such as bottleneck facilities in network industries. The reformers were aware of the way utility regulation was evolving in comparable jurisdictions such as the USA, the UK and Australia, but eschewed those methods in favour of a unique model known as light-handed regulation.

This regime was based on information disclosure combined with the threat of actual regulation (Bollard and Pickford, 1997). Its application in the electricity sector illustrates its main features. The government agency responsible for policy in network industries (now known as the Ministry of Economic Development or MED) developed and administered information disclosure rules for electricity distribution firms which

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* John Small is an economist and a Director of Covec (www.covec.co.nz). He advises regulators throughout the Asia Pacific region.

owned networks and retailed power. This process began in 1994. The disclosure rules mandated the use of optimised deprival value (ODV) for asset valuation,¹ and required that asset revaluations be booked as income for the purpose of reporting profits.

Although ODV is a replacement cost concept, the MED did not increase the physical asset values in the valuation handbook over time, thereby placing some constraint on valuation uplifts. However the information disclosure rules did allow firms considerable latitude in their implementation of ODV, and the disclosed data suggest that price-cost margins grew significantly between 1994 and 2003 (Bertram and Twaddle, 2005).

Differences in reporting conventions also made comparisons between firms difficult, reducing the opportunity to develop indicators of the type used in yardstick regulation (Shleifer, 1985). Credibility of the threat of regulation was thereby weakened, because there was no clear description of the conduct that would trigger it. It is difficult to maintain a strong threat when ones requirements are opaque. Reinforcing and also contributing to this situation was a lack of institutional capacity to either clarify or deliver on the threat of regulation (Haucap, Heimeshoff and Uhde, 2006).

Regulation of other network industries was similarly light. Telecom was privatised into this model and thereby had the upper hand in interconnection negotiations. Airports were free to charge as they pleased once they had 'consulted' with airlines. Gas pipelines were in a similar situation to electricity lines.

Eventually, the poor quality of disclosed information in the electricity lines sector made it impossible to dispel concerns about the leverage of market power from non-contestable distribution services into contestable markets for the generation and retailing of power. However rather than modify this regulatory model to make it more effective, with regulation still politically unpalatable, a structural split of the electricity distribution sector was preferred. This was mandated through the *Electricity Industry Reform Act 1998*, which required distribution companies to divest either their 'lines' business or their electricity retailing business. Most chose the latter option and electricity generators

¹ Strictly speaking (Clarke, 1998), ODV is equal to the lesser of optimised replacement cost (ORC) and economic value (which is the greater of scrap value or the willingness to pay of users). However, in practice in New Zealand, the ORC has typically been depreciated to become ODRC. Moreover, since willingness to pay generally exceeds this amount, ODV in New Zealand is usually equivalent to ODRC.

were eager buyers for the retailing businesses. In a short time, vertical integration in the industry shifted from being within a set of local integrated distributor-retailers to being within a set of five integrated generator-retailers ('gentailers').

First Attempts at Actual Regulation 1999-2008

Following the change of government in 1999, the idea that regulation could be beneficial became more acceptable in official circles. Ministerial inquiries were convened into the telecommunications and electricity industries and a set of new regulatory measures was introduced in response to their findings.

In telecommunications, a separate *Telecommunications Act* was passed in 2001 and a Commissioner was appointed to regulate wholesale interactions for the purpose of promoting competition. The Act placed several services under regulation and provided a process by which other services could be regulated. The Commissioner was located within the Commerce Commission and deliberated with two other Commerce Commissioners.

Also in 2001, the *Commerce Act* was amended to pass responsibility for information disclosure rules for electricity lines networks (including asset valuation methodologies) to the Commerce Commission, and to create a 'thresholds' regulatory regime. In that regime, the Commission was required to set thresholds for lines companies and empowered to control prices or revenues for firms which breached those thresholds.

The thresholds were intended to be a screening device that allowed the Commission the flexibility to avoid regulation for those firms within the threshold. Some means of targeting is particularly helpful in the electricity lines sector due to the large number of firms (twenty eight) and the fact that many are small and community owned. The process following a threshold breach was that the Commission would investigate and may or may not decide to impose direct regulation, which could be done without recourse to Ministerial approval.

These changes made the threat of regulation much more credible. The thresholds were at least an indication as to the boundaries of acceptable conduct. Moreover, the act of designing and setting thresholds gave the Commission an enhanced regulatory capacity relative to the situation of the 1990s.

Electricity lines business began to confront the reality of more effective regulation. There were many threshold breaches, and even though many were quite minor, the Commission was required to at least consider the possibility of more intrusive actions for each of them.

This focused attention on the Commission's decisions regarding the prioritisation and management of the breaches. It also revealed a cost of building post-breach flexibility into the thresholds regime itself.

Indeed, the regulated industry complained that the consequences of breaching the thresholds were uncertain, which created difficulties for their management decision-making. They were unsure of precisely which type and severity of breaches would trigger direct regulation. There were also other complaints. Vector, a large electricity and gas network owner, had a rather public dispute with the Commission over pricing of electricity network services in Wellington. Vector is controlled by a trust of Auckland consumers, who enjoyed cheaper connections than Vector's Wellington customers and an annual dividend from Vector. It was claimed that the Commission used a relatively minor breach of its overall thresholds to pressure Vector to change this pricing structure.

Concerns about the pricing of gas pipeline services also emerged over this period. This sector had been subject to information disclosure but without explicit guidance on asset valuation. It had adopted ODV and begun to revalue its assets in line with replacement costs. Following a Ministerial request in April 2003, the Commission inquired into the case for regulatory control, advising the Minister at the end of 2004 that control should be imposed on two suppliers of gas pipeline services (Powerco and Vector) under Part 4 of the *Commerce Act* which deals with regulation. This recommendation was accepted in May 2005 and provisional price cuts of around 9 per cent were ordered by the Commission soon after (Commerce Commission, 2009).

Powerco and Vector sought Judicial Review of the Commission's 2004 recommendation for control and the Minister's acceptance of that recommendation. While their complaints included technical matters such as the treatment of taxation and cost allocation, this action was also a direct legal challenge to the legitimacy of counting wealth transfers as a benefit of regulation. Demand for the services of gas pipelines is quite inelastic, so price regulation delivers limited efficiency benefits in the form of additional uptake of services (that is, allocative efficiency gains). However in the context of ongoing revaluations in line with the increasing cost of building gas pipelines there are significant wealth effects associated with the decision of whether to regulate or not.

At this time, the sole purpose of the *Commerce Act* (s 1A) was 'to promote competition in markets for the long-term benefit of consumers within New Zealand'. Powerco and Vector argued that transferring a monopoly rent to the customers of the monopolist did

not promote competition and could therefore not be counted as a benefit of regulation under the Act. The High Court dismissed all causes of action in December 2007, concluding that the (s1A) purpose statement could not apply to situations in which there was no prospect of competition. Powerco pursued this at the Court of Appeal which ruled against it in August 2008.

Meanwhile, the Commission had been concluding its authorisation of gas pipeline pricing, its decisions being published in October 2008. These decisions marked the end of replacement cost valuation concepts for gas pipelines. In effect, the Commission reasoned that replacement cost valuations were excessively generous in this industry, that they were not needed, and that they delivered windfall gains to firms that were unrelated to cost-reduction efforts. It set asset valuations at the ODV levels applying in 2002, those valuations being approximately consistent between firms and the timing reflecting a trade-off between the legitimate expectations of investors and interests of consumers.

The advantages of legislative amendment had by now become apparent and MED had in 2006 begun working on a review of the regulatory provisions in *Commerce Act*. This review and the subsequent legislative amendment laid the platform for the next version of utility regulation in New Zealand.

The New Model 2009-

The *Commerce Act* was amended in September 2008. A key provision was to include a separate purpose statement for regulation, squarely addressing the complaint of Vector and Powerco in their Judicial Review of gas pipeline regulation. The regulatory purpose statement applies to markets where there is 'little or no competition and little or no likelihood of a substantial increase in competition'. In such markets, the purpose of Part 4 of the Act is stated in s52A as being to

promote the long-term benefit of consumers...by promoting outcomes that are consistent with outcomes produced in competitive markets such that suppliers of regulated goods or services

- a. have incentives to innovate and to invest, including in replacement, upgraded, and new assets; and
- b. have incentives to improve efficiency and provide services at a quality that reflects consumer demands; and
- c. share with consumers the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices; and

- d. are limited in their ability to extract excessive profits.

As the purpose statement shows, a key concern cited by government was that regulated firms must have sufficient incentive and ability to invest in infrastructure. This responds to complaints from regulated firms that regulation was deterring investment. However the statement also points clearly towards the objective of constraining market power (sections c and d). The amendment also created a new test for when regulation may be imposed (s52G) which sets the following hurdles

- a. the goods or services are supplied in a market where there is little or no competition; and little or no likelihood of a substantial increase in competition; and
- b. there is scope for the exercise of substantial market power in relation to the goods or services, taking into account the effectiveness of existing regulation or arrangements (including ownership arrangements); and
- c. the benefits of regulating the goods or services in meeting the purpose of this Part materially exceed the costs of regulation.

A full inquiry by the Commerce Commission is required as a first step before new goods or services may be regulated. Decisions on whether and how to regulate rest with the Minister of Commerce in consultation with the sector Minister.

Input Methodologies

This much is largely a clarification of the positions adopted in the previous version of the Act. However a wholly new approach to regulatory processes is also included, under the heading of 'input methodologies'. These are detailed rules covering matters such as how to calculate the cost of capital, value assets and allocate common costs. The Commission is required to set input methodologies for electricity lines, gas pipelines and airports by 30 June 2010. (The Minister may grant one extension of six months). The methodologies are binding on the Commission and regulated suppliers.

Interested parties have a right of appeal against the input methodologies to the High Court sitting with lay members. The Court may only allow an appeal if it is satisfied that 'the amended or substituted input methodology is or will be... materially better in meeting' one or both of two purposes. Those two purposes are the overall purpose of Part 4 as described above (s52A) and a separate purpose of input methodologies described in s52R as being to 'promote certainty for suppliers and consumers in relation to the rules, requirements, and processes applying to the

regulation, or proposed regulation, of goods or services under this Part.'

The appeal provisions are interesting for two reasons. One is that the legal standard clearly involves a comparison between two methodologies rather than consideration of the Commission's decision alone. Secondly, it is somewhat ironic that the amendment has replaced a regulatory statute lacking any clear purpose with one that has two somewhat conflicting purpose statements. It remains to be seen whether this duality of purpose will cause difficulties.

Input methodologies are required for three sectors initially and are also required as part of the process leading to regulation of other services. While they are intended to create greater certainty over the outcomes of regulation, they are only required in situations where regulation is to be used. In this sense, they do not significantly advance the idea of threat-based regulation. Indeed, the thresholds regime applying to electricity lines businesses has been abandoned through repeal of the relevant sections of the Act.

The new model provides for several forms of regulation, each of which has its own purpose statement. The options and their purposes are shown in Table 1

Table 1 Forms of Regulation under part 4 of the Commerce Act and their Purposes

| Method | Purpose |
|---------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Information Disclosure | to ensure that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met. |
| Negotiate/Arbitrate | to encourage a supplier and its customers to reach agreement, through negotiation, on the supplier's prices and quality standards during a specified regulatory period, and to provide for binding arbitration if negotiation is unsuccessful |
| Default/Customised price-quality regulation | to provide a relatively low-cost way of setting price-quality paths for suppliers of regulated goods or services, while allowing the opportunity for individual regulated suppliers to have alternative price-quality paths that better meet their particular circumstances. |

Information disclosure will apply to consumer-owned electricity lines businesses, comprising 16 of the 28 firms in the sector. However, consumers will be able to petition the Commission if they consider a firm should be put on the default/customised regime.

The international airports at Auckland, Wellington and Christchurch will also be subject to information disclosure with the Commission being required to monitor disclosed information and report to Ministers after 2012 as to the effectiveness of this regime.

The information disclosure regimes retain an element of threat-based regulation. This is the first time that Airports have been subject to oversight by the Commission. Following an investigation, the Commission had in 2002 recommended regulation of Auckland Airport to the Minister, who rejected it. Airports have since been operating under the 1990s version of light-handed regulation.

The negotiate/arbitrate model will be familiar to Australian regulators and is also the basic structure of telecommunications regulation in New Zealand. It is expected to be most useful in situations where there is a relatively small number of customers such as airports.

Default/customised regulation replaces the former thresholds regime and will apply to electricity lines businesses that are not consumer-owned, and to gas pipelines. Under it, the Commission sets a default price-quality path for regulated suppliers for (normally) five-year periods. There may be a P_0 adjustment, and a CPI-X structure is envisaged for prices with X being

linked to expected long-run productivity improvement rates for the sector. Suppliers may propose an alternative customised price-quality path to the Commission once in each regulatory period. The Commission must normally decide such applications within 150 working days. The Commission is also empowered to set quality standards (including to reduce energy losses) and to incentivise meeting or exceeding those standards. Interested parties have a right of appeal to the High Court against final decisions taken by the Commission on customised price paths.

It is worth noting that the discipline of input methodologies is required for all three forms of regulation, though there will be variation across those forms. This should lead to greater rigor in the design of information disclosure regimes in particular.

Where to from here?

These regulatory changes are underway at a time of heightened uncertainty over global economic conditions and over critical policy decisions over carbon emissions. Although legislation is in place mandating a reasonably pure emissions trading scheme, which would cover the industrial sector by January 2010, the legislation was the work of the previous government and a select committee is currently considering changes. More generally, though its banking system appears sound, New Zealand is braced for tough economic conditions for some time to come, and there is very limited scope for counter-cyclical government spending.

These are both expected to be transitional issues, albeit somewhat painful. One of the largest regulated firms, Powerco, was fully owned by Babcock and Brown until 58 per cent was sold in February 2009 to

Queensland Investment Corporation, slightly before Babcock and Brown went into voluntary administration. From a regulatory standpoint, the ability of firms to meet their cash obligations is distinct from the usual focus on overall cost recovery. Cash-flow issues have received some attention from the Commission recently, particularly in respect of the treatment of asset revaluations as income if replacement cost valuation concepts are used. It is not always feasible for firms to rebate capital asset revaluations to their customers in a single year while also meeting other cash commitments.

At present, the Commission is preparing consultation documents setting out its views on input methodologies. The consultation and appeal processes provide regulated firms with opportunities to challenge virtually every part of the regulatory model, so wide-ranging and robust debate can be expected. It is not clear that regulated gas pipeline owners have yet abandoned their preference for asset values to track replacement costs, so further arguments may arise as to the merits of regulatory models predicated on the costs of a hypothetical new entrant.

The input methodologies initiative was motivated in part by complaints from electricity lines companies that they were confused as to the consequences of breaching thresholds. It was hoped that by front-loading most of the analysis and publishing the rules, firms would be able to predict the impact of regulation on their business with greater certainty. That does not make such impacts any more welcome of course, and regulated firms may also regret weakening the discretion the Commission previously had over its responses to threshold breaches.

On the other hand, the new model does include robust rights of appeal and greater clarification of Parliament's intentions through the use of more specific purpose statements. While it remains to be seen how this new innovation in New Zealand's processes for utility regulation will work in practice, it is undoubtedly the most rigorous regulatory structure that has been used in recent times.

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Critical Issues in Regulation – From the Journals

‘Capital structure and regulation: Do ownership and regulatory independence matter?’, B Bortolotti, C Cambini, L Rondi and Y Spiegel, Discussion Paper No. 7100, Centre for Economic Policy Research, London England, December 2008.

The authors study the potential for a utility to increase the level of debt as a result of regulation. The authors examine whether a relationship exists between capital structure, regulated prices, ownership structure and regulatory independence.

Regulators set prices taking into account the capital structure. If the firm issues more debt, then the regulator is inclined to award higher prices to reduce the probability that the firm is placed in financial stress. The firm can therefore have an incentive to increase gearing if this causes the regulator to grant higher prices. This is based on the assumption that the firm is privately owned and regulated independently.

The authors test the following three hypotheses. Firstly, that regulated firms have a higher leverage if they are privately controlled and subject to regulation by an independent regulatory agency. Secondly, whether an increase in leverage leads to an increase in regulated prices. Finally, the authors test whether an increase in leverage will lead to an increase in the market value of the (privately owned) firm. The last two hypotheses stem from the fact that firms receiving a higher price will earn greater revenue and are valued higher in the market.

Using panel data on 92 publicly traded utility companies based in the EU over the period 1994 to 2005, the authors run a series of regressions to test all three hypotheses. Controls were introduced in the equations for country and firm-specific effects, along with dummy variables to signify if regulation is independent or not. The results indicate the above hypotheses can not be rejected. This suggests that increased leverage is associated with higher prices and therefore a higher market value for the firms studied.

The study is of particular interest because it suggests the observed capital structure of privately owned firms could be more highly geared than government-owned utilities. [Paper](#)

‘Competition schemes and investment in network infrastructure under uncertainty’, K Hori and K Mizuno, *Journal of Regulatory Economics*, Vol.35, 2009, pp. 179-200.

This paper compares two specific types of competition scheme – services-based and facilities-based – in terms of the incumbent firm’s incentive to invest in network infrastructure. Services-based competition is where entrants can utilise the existing network investment of an incumbent, whereas facilities-based competition requires entrants to make investments in network infrastructure in order to compete in the downstream market.

The authors favour a real options approach for focusing on a regulated firm’s incentives to make irreversible investments under future demand uncertainty. However, the applicability of this approach to regulated industries is currently subject to substantial debate.

Hori and Mizuno find that under services-based competition, entrants have a greater propensity to enter the market sooner than under facilities-based competition, because they avoid the need to incur the large costs, which are fixed and irreversible. Services-based competition can thereby create a competitive environment earlier, which the authors note was a partial rationale for the move to unbundle telecommunications services in the US in 1996.

On the other hand, their model also suggests that having gained access to the incumbent’s infrastructure, new entrants invest in bypass facilities later than under facilities-based competition. In addition, the model suggests that services-based competition could deter the initial construction of network infrastructure, depending on the environment surrounding the firms. The authors claim that the welfare losses from services-based competition suggested by their model led the U.S. Federal Communications Commission to alter its unbundling rules in 2003.

In circumstances where monopoly rent is large, Hori and Mizuno’s model suggests that the initial introduction of infrastructure occurs earlier under facilities-based competition than under services-based competition. On the other hand when monopoly rent is small *and* the degree of demand uncertainty is small, services-based competition can bring about the earlier introduction of infrastructure than facilities-based competition.

'The diversification discount puzzle: Evidence for a transaction-cost resolution', R Aggarwal and S Zhao, *The Financial Review*, Vol.44, 2009, pp.113-135.

This article analyses the corporate diversification discount puzzle. Although some studies show a significant diversification discount, others contend that there is no such discount and that prior studies suffer from measurement problems, with the discount disappearing when errors are corrected. The question the article sought to raise was whether diversified firms were valued more or less than their stand-alone (less diversified) counterparts. This can have implications for the recent debate regarding equity raising costs.

Transaction-cost economics seeks to explain why certain transactions are directed by managers within the firm, as opposed to taking place in an open market. In the case of financing, transactions costs can impact on the efficiency of using internal versus external sources of capital.

According to this perspective, diversified firms should outperform single segment firms in industries with higher external transaction costs. In particular, agency costs tend to be lower, especially in more mature industries, where it can be expected that information asymmetries are lower. Agency costs relate to investors being unable to perfectly control the actions of managers. By contrast, the authors suggest that such costs tend to be higher in less diversified and emergent industries, which requires those firms to offer greater compensation to investors.

The ACCC/AER has questioned whether to allow equity raising costs as an expense, with internal financing favoured as a more efficient source of capital. Aggarwal and Zhao's paper suggests that transaction costs associated with external financing are greater due to the greater degree of information asymmetry. This asymmetry can be mitigated to an extent with the diversification of business activities and firms operating in more mature industries. This might imply a lesser cost of raising external equity for regulated utilities, if such businesses can be considered 'diversified' and 'mature'

A contention of the article was that diversification can be value enhancing if external capital markets face large transaction costs relative to internal costs of allocating capital and vice versa.

'CAPM for estimating the cost of equity capital: Interpreting the empirical evidence', Zhi Da, Re-Jin Guo and Ravi Jagannathan, NBER Working Paper Series, Working Paper 14889, April 2009.

The Capital Asset Pricing Model (CAPM), as developed by Sharp and Lintner, is widely used by regulators to estimate the cost of equity component of the weighted average cost of capital (WACC). For instance, its use by the AER in regulating electricity transmission and distribution is mandated in the National Electricity Rules.

The CAPM can be used to estimate the cost of capital for an asset or individual project, as well as for a firm's overall equity. The CAPM specifies a relationship between the expected return of an individual project or business and the level of systematic (or non-diversifiable) risk. Despite its popularity, the use of the CAPM is controversial due to several empirical studies noting anomalies in its predictive power. For instance, empirical studies have found that average returns on stocks are related to other factors beyond non-diversifiable risk, such as firm size, book-to-market ratio (BM), and earnings-to-price ratio.

In this article, the authors focus on the CAPM's use in estimating the cost of capital for a project. Specifically, they examine whether these empirical anomalies which mostly apply to the equity value of the firm, are sufficient to warrant the use of an alternative to the CAPM to estimate the cost of capital for a project. The authors specifically examine the BM effect, which they describe as being the most prominent empirical challenge to the CAPM.

Da, Guo and Ragannathan proceed by examining the related literature and providing new empirical evidence in relation to the anomalies. First they examine the impact 'real options' on stock values, which are firms' options to turn down, undertake or defer new projects, as well as options to modify or terminate and existing projects. They agree that the firm size and BM effects found in some empirical studies might be the result of real options associated with some firms' projects. With some firms having greater levels of real options than others, the CAPM might therefore do a poor job of explaining the cross-section of stock returns.

The authors then present the findings of empirical work based on a sample of firms over the period 1932-2007. The authors compare the performance of the standard CAPM and the Fama-French three-factor model in pricing the average returns on portfolios of stocks grouped according to their betas.

The authors find that use of the Fama-French model does not substantially reduce the average pricing error associated with the CAPM.

To specifically examine the BM effect, the authors consider the potential for within-industry BM effects and cross-industry effects, using portfolios categorised by industry. The authors find that within-industry variation in BM is related to financial leverage and Capex which, they say, are measures of real options available to a firm. The authors find that once these two firm characteristics are controlled for, the BM effect is significantly reduced. The within-industry BM effect is also weakened when the authors measure the expected return using the forward-looking Implied Cost of Capital rather than the actual realised return.

Using these observations, the authors suggest that the BM effect is likely to be driven by firm-specific characteristics, not the characteristics of underlying projects. The authors conclude that the existence of real options may be an important reason for the poor performance of the CAPM in explaining returns on cross-sections of stocks. However, the empirical evidence is not sufficient to abandon the use of the CAPM for providing a reasonable estimate of the required return on individual projects. [Paper](#)

‘Real estate, factory outlets and bricks: A note on non-aeronautical activities at commercial airports’, William G Morrison, *Journal of Air Transport Management*, Vol. 15, 2009, pp. 112-115.

This paper analyses price subsidisation of air transport businesses by airports using their non-air transport businesses. The authors suggest that airports may be able to offer air transport services at below marginal cost prices.

Australian airports are private businesses that operate on land leased from the federal government. All airport land development is subject to direct federal government approval and not to local council constraints. According to the authors, during the bidding process for airports, the government encouraged development of airport land into commercial properties, with commercial owners assured that no price cap would apply to these services. The authors suggest this has led to an increase in the value of commercial airports and the development of non-air transport businesses in airports.

The authors note that the complementarity between air transport services and non-air transport services decreases the profit maximising price for air transport services, relative to the air-transport prices being set

independently. They find that the lost revenue is more than made up for by the additional revenue of non-air transport sales.

If the airport is under ‘single till’ price regulation, which takes account of non-air transport revenues, the authors argue that the price for air transport services will be lower than unregulated airports. This is due to single till regulation taking account of all airport revenue, resulting in lower regulated prices for air transport services. They note that this outcome is also likely for non-profit airports. Such airports seek to maximise profits on all non air transport services to subsidise air transport services.

The authors conclude that specifications for airport service-levels are required, because the relative profitability of non air transport services can otherwise induce the airports to shift their focus away from providing air transport services. They suggest that airport security may be sacrificed if too many non air transport services result in greater access to the airport. On the other hand, for non-profit airports, there can be incentive to ‘gold plate’ the provision of air transport services, because the accumulated profits from non air transport services cannot be distributed to shareholders.

The authors conclude that the attractiveness of non air transport services varies according to the business opportunities defined by land, location and assets. The degree of competition between airports encourages the development of complementary non-air transport businesses, but can also affect the businesses that don’t complement air transport services. The development of non-air transport business can have different impacts on air transport prices and infrastructure investing.

‘Capital market response to emission rights returns: Evidence from the European power sector’, Stefan Veith, Jorg R. Werner and Jochen Zimmermann, *Energy Economics* Vol. 31(4), July 2009.

This paper investigates the distributional impacts of the Emission Trading Scheme (ETS) introduced by the European Union (EU) in 2005, among the regulated firms, and also among other market participants including the firms’ customers. This is investigated by examining the empirical links between the share returns of electricity generators and the market for carbon emission rights under the EU’s ETS.

Veith et al. estimate a multifactor market model of share returns for a sample of the European energy production sector, with the purpose of capturing the

incremental economic influence of the ETS regulatory scheme. They posit that if capital markets consider the ETS to be relevant to the value of energy producer shares, then this will be reflected in the relationship between share returns and the price of emissions permits. The estimation method allows for either positive or negative economic consequences of the ETS on energy producers.

The authors find that there is a positive correlation between share prices of the sampled energy producers and prices of carbon dioxide emission permits. Veith et al. surmise that this indicates the introduction by the EU of its ETS altered the cost structures of firms in the power sector, but that investors perceived that increased consumer energy price would overcompensate for the increased costs under the ETS.

However, the authors also note that this positive correlation did not hold for utilities with higher proportions of fossil fuel electricity generation. The correlation for higher fossil fuel generators in the sample was instead negative with respect to carbon prices. The implication is that for high-carbon generators, share returns decreased as the price of carbon emissions permits increased. This is an important qualification to the applicability of the overall results to Australia, where a significantly higher proportion of fossil fuels (coal, gas, etc) are used in electricity generation compared to the EU.

International Round-Up of Regulatory Decisions

This section contains a sample of recent regulatory decisions in leading OECD countries and the European Union, with emphasis on energy, telecommunications, posts, water and wastewater, rail, airports and ports.

Canada: NEB Releases Canadian Energy Overview 2008

The Canadian energy regulator, the National Energy Board (NEB) released its Canadian Energy Overview 2008 report on 21 May 2009. The report contains information about the various elements of the Canadian energy sectors and notes that the convergence of energy efficiency and conservation with renewable energy policies was a key influence on the Canadian energy sector during the year. [Link](#)

Canada: NEB Sets Total Return on Capital for 2007 and 2008 for Gas Transmission

In March 2009 the NEB decided to vary the methodology that it had previously used to set the total return on capital for the Canadian gas transmission pipeline operator, Trans Québec & Maritimes (TQM). [Decision](#)

Canada: CTA Releases Decision on Western Grain Price Caps

Since 2000, rates set by the Canadian National Railway (CN) and Canadian Pacific Railway (CPR) for the movement of Canadian western grain by rail have been subject to an annual revenue cap determined by the Canadian Transportation Agency (CTA). On 30 April 2009 the CTA published its revenue cap decision for 2009-10 crop year beginning 1 August 2009. Most of the decrease in the volume-related composite price index (VRCPI) is attributable to lower fuel prices. [Link](#)

China: OECD Reviews China's Regulatory Reform

China is not a member of the OECD, but has been offered 'enhanced engagement' with a view to possible future membership. According to the OECD, China's ongoing transition to a market economy is among the greatest economic success stories of modern times, although it still faces important challenges in key areas, including strengthening regulatory institutions and processes. China's transition has been reviewed as part of the OECD Regulatory Reform Programme. The review focuses

on the economic context for regulatory reform, the Government's capacity to manage economic reform, competition policy and enforcement, and market openness. It also examines the regulatory frameworks in the electricity and water sectors. The report was published on 7 May 2009. [Report](#)

Europe: European Parliament Reaches Informal Agreement on Mobile Roaming Regulation

On 22 April 2009, the European Parliament reached a compromise agreement on the extension of the 2007 Roaming Regulation. The current Roaming Regulation only applies to voice calls within the EU and expires on 30 June 2010. The new Regulation sets ceilings beneath which mobile operators can compete by offering lower prices, extends the scope of the regulation to data roaming services and includes provisions to protect consumers from data 'bill shock'. The regulation will expire by 30 June 2012. [Link](#)

Europe: Average Price of Fixed Broadband Access Declines in Europe

A study by the European Commission (EC) released on 25 March 2009, found that there were significant falls in prices for fixed broadband internet access (DSL, cable modem, fibre) in Europe in 2008. However, there were significant differences between Member States in the structure and level of broadband retail prices for similar products. The EC has thus urged Member States to apply the EU rules consistently. [Link](#)

Europe: EC Requests German Regulator to Notify Deutsche Telekom's Origination and Termination Rates for Fixed Line Calls

On 27 March 2009, the EC wrote a letter to the German telecommunications regulator, *Bundesnetzagentur* (BNetzA), to ask it to notify the EC of Deutsche Telekom's fixed call origination and termination rates. Under the EU telecommunications rules' consultation (Article 7 procedure) national regulators generally notify all elements of price remedies, as part of their market analyses. However, the draft measure the BNetzA sent to the EC on 27 February 2009 only mentioned the general principles that it will apply in assessing Deutsche Telekom's requests for approval of rates. Should the BNetzA continue to fail to comply with its obligation,

the EC may open an infringement procedure for non-compliance with EU law. [Link](#)

Europe: EC Announces Cost-based Methodology for Calculating Termination Rates

Following consultation with the public and Member States, the EC published, on 7 May 2009, guidance for telecommunications regulators in Member States on the cost-based methodology to be used when calculating termination rates. The guidance is in the form of a 'Recommendation' that national regulators are obliged to take 'the utmost account' of. The Recommendation indicates that termination rates at the national level should be based only on the real costs that an efficient operator incurs to establish the connection. The Recommendation has been published because, despite efforts by some national regulators to bring termination rates closer to efficient levels, those rates remain disparate across the EU and there are large gaps between fixed and mobile termination rates, contrary to the increasing convergence of fixed and mobile telecommunications services.

The EC considers that these pricing anomalies and differing regulatory approaches undermine the Single-Market and Europe's competitiveness. The EC considers that all national regulators should apply the recommended approach to termination rates by the end of 2012. However, national regulators with limited resources may use different approaches for a limited further period as long as they achieve the same pro-competitive result. [Link](#)

Europe: EC Accepts German Gas Transmission Operator's Commitment to Divest Gas Transmission Network

On 18 March 2009, the EC decided to accept legally binding commitments offered by RWE to address concerns raised in the course of the EC's investigation of energy companies in five member states under EC antitrust rules. RWE is one of Europe's 'top five' electricity and gas companies, operating in generation, trading, transmission and supply of electricity and gas. The EC was concerned that RWE may have abused its dominant position in gas transmission networks by refusing to supply gas transmission services to third parties and by engaging in behaviour that intended to lower the margins (margin squeeze) of RWE's downstream competitors in gas supply. In response, RWE offered to divest its entire Western German high-pressure gas transmission network. [Link](#)

Europe: ERGEG Publishes Status Review of Retail Price Regulation

On 27 March 2009, the European Regulators Group for Electricity and Gas (ERGEG) published a Status Review of End-User Price Regulation which shows that regulated retail prices continue (alongside market prices) in a large number of EU countries (15 in electricity, and 13 in gas). More than 80 per cent of retail customers across all market segments remain on regulated prices. The ERGEG reiterated its views from a 2007 position paper that the need to protect vulnerable customers should not be confused with regulated tariffs for all (or certain categories) of customers. The ERGEG called for plans to phase-out regulated retail prices in the EU. [Status Review](#)

Europe: Final Implementation Report for Gas Regional Initiative North West Regional Energy Market Transmission Transparency Project

The ERGEG launched its Electricity and Gas Regional Initiatives (ERI and GRI respectively) in 2006. The Regional Initiatives framework created seven electricity regions and three gas regions in Europe. The overall aim of the Regional Initiatives is to facilitate the development of regional gas and electricity markets, working in cooperation with stakeholders, to remove barriers to trade and competition. The Gas Regional Initiative North-West (GRI NW) comprises nine countries and is the largest of the three Gas Regional Initiatives in terms of market size and geographic scope.

Stakeholders agreed that the main priorities for the GRI NW are transparency, capacity and investment to ensure that gas can be freely traded between Member States on a non-discriminatory basis. In relation to transparency, it was considered that information about available transmission capacity and the probability of interruptions was vital, particularly to promote new entry. Thus a project was commenced whereby 17 regional transmission system operators (TSOs) in the GRI NW committed to publishing information on capacity availability and gas flows at cross-border interconnection points by the end of 2008.

Participation in the project was on a voluntary basis. The TSOs committed to releasing the specified information at one of three project milestones in May, October and December 2008. An implementation report was published for each of these milestones to explain the progress made by participating TSOs. On 26 May 2009, the ERGEG published the third and [final Implementation Report](#).

Europe: EEA Recommends New Approach to Managing Water Resources

On 17 March 2009 the European Environment Agency (EEA) released a report, *Water Resources Across Europe — Confronting Water Scarcity and Drought*, confirming that water use is unsustainable in many parts of Europe. The EEA made recommendations for a new approach to managing water resources that shifts the management focus from increasing supply to minimising demand. Among other approaches, the EEA recommended that in all sectors, including agriculture, water should be priced according to the volume used. [Report](#)

France: Proposals to Reform Regulation of Value-added Services

On 7 May 2009 the French communications regulator, the *L'Autorité de régulation des communications électroniques et des postes* (ARCEP), published a report titled 'Value-added Services: Retail Pricing and Professional Code of Conduct' (in French) that announced priority areas for reforming so-called 'value added services'. These are calls made to particular numbers that connect to service platforms that serve a range of functions (e.g. connect consumers with different departments in a company or an administration, provide practical information, sell information or content, allow participation in a contest, etc) and are billed at a special tariff chosen by the service provider. The report was in response to rising consumer dissatisfaction and distrust of these services as a result of lack of clarity in pricing, unfair practices, and the prohibitive costs of some calls. [Link \(in French\)](#)

France: Competition Authority Accepts France Telecom's Commitments on Wholesale ADSL Offer in Overseas Regions

On 18 March 2009, French competition agency, the *Autorité de la Concurrence*, accepted commitments offered by France Telecom in relation to its wholesale ADSL offer in France's overseas regions (Guadelope, Martinique, French Guiana and Réunion), following an investigation by the Competition Authority. France Telecom's commitments will guarantee the availability of technical support during business hours in the overseas regions. France Telecom will also provide the Authority with indicators to evaluate the quality of its retail and wholesale ADSL offers in those regions. [Press Release \(in French\)](#).

France: Regulator to Examine Intermodal Transport Issues Prior to Rail Liberalisation

The French competition agency, the *Autorité de la Concurrence*, announced on 18 May 2009 that it will examine potential competition issues relating to intermodal transport in anticipation of liberalisation of international rail passenger traffic from 1 January 2010. It is expected that train stations will develop into transport hubs for train and other transport services, such as buses. Since France's incumbent rail operator, SNCF, operates across the whole transport chain, the *Autorité* will examine whether it is necessary to take steps to preserve competition and reduce the potential for SNCF to impede access to stations to the detriment of terrestrial public transport and/or intermodal markets. [Press Release \(in French\)](#).

France: CRE Adopts Guidelines on Conditions for Access to Natural Gas Transmission Networks by Electricity Generators

Since 2006, many project developers have submitted requests to GRTgaz and TIGF, the two natural gas transmission system operators (TSOs), to connect their natural-gas-fired electricity-generating stations to the gas transmission networks. The TSOs have identified a number of operating constraints arising from these generating stations' high levels of gas consumption and their need for intra-day flexibility, particularly when operating at semi-baseload and at peak-load. The energy regulator, the CRE, consulted with the TSOs and interested stakeholders during March 2009 about transportation and balancing rules that could apply. In particular, CRE sought views on two particular models:

- GRTgaz's proposal to set up an hourly balancing system for electricity-generating stations, or other large consumers characterised by significant fluctuations in demand.
- An 'integrated' model, whereby the TSOs' supply to electricity-generating stations integrates intraday flexibility while maintaining daily balancing for shippers.

In view of strong disagreement between the TSOs and other market participants, the CRE published, on 30 April 2009, guidance and principles relating to gas transportation and balancing conditions for electricity-generating stations connected to gas transmission networks. The CRE confirmed that daily balancing will be maintained on French gas transmission networks, until at least the end of 2009, contrary to GRTgaz's proposal. It is the TSOs' responsibility to

optimise intraday flexibility resources, but they should inform the CRE immediately of any difficulties encountered with providing such flexibility. GRTgaz and TIGF should also conduct a general study, to be submitted to CRE in September 2009, in coordination with other gas infrastructure operators, focusing on the ability of French gas infrastructures to meet the demand from planned electricity-generating stations. [Link](#)

Germany: Deregulation of Parts of Wholesale and Retail Markets

On 24 April 2009, the German telecommunications regulator, the Federal Network Agency (FNA) published a regulatory order setting out the key regulatory elements of the interconnection of Deutsche Telekom's (DTAG) network with rival networks. Under the new arrangements, calls terminating and originating on the DTAG's network will continue to be regulated. However, transit services over its network will be largely exempt from regulation as the FNA considers that these services can now also be supplied by other providers and, thus, the DTAG no longer has significant market power in respect of those services. The FNA has also withdrawn regulation in the retail market for national fixed network connections, finding that the market showed 'tendencies towards effective competition'. [Regulatory Order](#)

Germany: FNA Approves €415 m Investment Budgets

Under the German energy regulatory framework, energy systems operators may submit investment budgets for special projects for approval by the FNA. These investments may be needed, for example, to maintain supply quality, to connect new power plants or to enable energy from renewable sources. If approved, the operators are able to adjust their revenue caps. On 14 April 2009, the FNA approved the investment budgets submitted by two energy supply grid operators totalling €415 m. [Press Release](#)

Ireland: Mobile Termination Rates to be Reduced Further

The Mobile Termination Rates (MTRs) of Vodafone, O2 and Meteor have been subject to price control in Ireland since 2005, reflecting the Commission for Communications Regulation's (ComReg) view that prevailing MTRs were unlikely to reflect the efficient cost of provision. Despite successive reductions in MTRs since January 2006, the European Regulators Group (ERG) determined Ireland to be out of line with the EU average MTR, based on the current MTR schedule of reductions. In Information Notice 09/32, released on 16 April 2009, Vodafone, O2 and Meteor

all indicated their intention to reduce further their blended MTRs to a symmetrical maximum rate per minute of €0.05 over a three year period. [Information Notice 09/32](#)

The Netherlands: OPTA Releases Market Monitor for 2008

On 19 May 2009, the Dutch communications and postal regulator, the OPTA, released its annual Electronic Communications and Postal Market Monitor for 2008. The Monitor describes developments in the areas regulated by the OPTA based on external public data as well as information gathered by the OPTA from regulated entities. [Monitor](#)

The Netherlands: OPTA Releases Annual Report 2008

The OPTA also released its annual report for 2008, on 19 May 2009. In addition to outlining the OPTA's activities in 2008 the report contains an overview of recent developments in the Dutch telecommunications regulatory regime, including requirements for the incumbent, KPN, to provide wholesale broadband access for the regulatory period 2009-2011. [Annual Report](#)

Sweden: Release of Broadband Survey 2008

The Swedish Post and Telecom Agency (PTS) released, on 20 May 2009, the Broadband Survey 2008. The PTS has been monitoring the development of the broadband market over several years with the aim of determining whether broadband accessibility is improving. The report contains its findings. The report also provides the PTS with an understanding of future technical and commercial developments and contains a number of recommendations to help Sweden retain its position as a leading broadband nation. [Survey](#)

UK: Ofcom Publishes Guide to Investment in Super-fast Broadband Networks

The UK Office of Communications (Ofcom) published a guidance note on 27 May 2009 that is intended to highlight how telecommunications regulations in the UK apply to new-build investment in super-fast broadband networks. The note outlines the main elements of the Ofcom's policy and the regulatory processes that are most relevant to investment in these networks. This note is targeted at senior management of companies who are considering investing in new networks, as well as prospective financiers of such investments. [Guidance Note](#). The guidance note should be read alongside the

March 2009 Statement on [Delivering Super-fast Broadband in the UK](#) and a [Glossary of Terms](#).

UK: Ofcom Releases Latest Report on the Impact of the Strategic Review of Telecommunications

The Ofcom concluded its Strategic Review of Telecommunications in September 2005. Following the review's findings, the BT provided legally binding undertakings to the Ofcom in lieu of a reference to the UK Competition Commission (UKCC). These undertakings set the terms by which the BT would deliver the two key solutions to the competition concerns that were identified in the review: equality in the provision of inputs (equivalence of inputs (EOI)); and functional separation. To meet the separation requirement, the BT created a new organisation, Openreach, that is intended to be operationally distinct from the rest of the BT Group and which provides most of the wholesale EOI products. The Ofcom reports annually on the implementation of the undertakings and their impact on residential and business customers. The Ofcom released the report of its latest evaluation on 29 May 2009. The evaluation indicates a positive net effect of the undertakings to date, both for competition and consumers. The Ofcom remains of the view that the Undertakings are an effective mechanism to address the competition concerns identified in the review. [Report](#)

UK: Ofcom Confirms New Wholesale Prices for Openreach

The Ofcom released a decision document on 22 May 2009 after finalising its review of the prices of Wholesale Line Rental (WLR), fully unbundled lines (Metallic Path Facility or 'MPF') and shared unbundled lines (SMPF) charged by Openreach (the 'Core Rental Services'). The decision document sets out the new price controls for the MPF and SMPF services. In accordance with a recommendation by the European Commission, the Ofcom has delayed determining new prices for WLR until its Wholesale Narrowband Market Review is finalised. During the review, the Ofcom also proposed that other services provided by Openreach relating to the provision of the MPF and SMPF rental services should be subject to price controls. The decision document sets out the appropriate design of baskets for price controls of these services. [Link](#)

UK: Consumer Focus Warns of Growing Digital Divide

Consumer Focus is the new statutory consumer organisation representing UK consumers. Its remit includes working on behalf of vulnerable consumers,

including taking up energy and postal complaints on their behalf. On 26 May 2009, Consumer Focus released a report titled, 'The Digital Divide: Universal Service and Broadband'. The report warns that the 'digital divide' between those who can and cannot afford broadband could undermine the UK Government's target of achieving 'near universal participation in the digital economy'. The report pointed out that the digital divide arises because many consumers cannot afford the equipment and subscription fees, or do not have the necessary skills or confidence to use it. A significant proportion of non-users are, according to the report, older people, those on low incomes, mobile-only households and those with disabilities. Consumer Focus considers that the UK Government's Universal Service Commitment for broadband focuses too narrowly on providing physical connectivity and underestimates the barriers of affordability and usability that consumers face in reality. [Report](#)

UK: Ofgem Relaxes Industry Rules to Allow Faster Connection of Wind and Low-Carbon Generators

On 8 May 2009 the UK Office of the Gas and Electricity Markets (Ofgem) announced a temporary relaxation of industry rules for connection to, and use of, the high-voltage electricity networks, to allow much faster connection of wind and low-carbon generators. See Notes on Interesting

UK: Ofgem Releases Decision on Next Steps in Electricity Distribution Structure of Charges Project

The Electricity Distribution of Charges Project seeks to achieve a common, cost-reflective charging methodology with open governance arrangements across all 14 Distribution Network Operators (DNOs) in Great Britain by April 2010. In October 2008, the Ofgem's proposals to place new licence conditions on the DNOs to achieve this aim were blocked by two distribution-owning companies which did not agree with the Ofgem's proposed methodology for the highest network voltage levels. The Ofgem subsequently consulted on the best ways to take the project forward. On 20 March 2009, the Ofgem released a Decision Document that sets out the next steps for delivering the structure of charges project for electricity distribution businesses. [Decision](#)

UK: Ofgem Announces New Retail Market Rules

The Initial Findings Report of the Energy Supply Probe (the Probe), published in October 2008, found that the energy market is generally working well but

competition is not yet fully effective in all sectors, including retail. On 15 April 2009 the Ofgem published a package of proposals aimed to promote competition in the retail energy supply market. The proposed rules include a prohibition on unjustified price differences to retail customers; and a set of remedies to improve retail market transparency and consumer protection so that all customers are able to readily access the best retail offers. The retail remedies will be included in retailers' licence conditions. Submissions on those proposals were due in May 2009. The Ofgem will decide on the final package by July 2009 for implementation in the UK autumn. If the industry does not agree on the package of proposals, the Ofgem may refer the matter to the Competition Commission. [Link](#)

UK: Ofgem Releases Gas Distribution Annual Report for 2007-08

The Ofgem released on 27 March 2009 the first annual report on the eight gas distribution networks based on the regulatory reporting process introduced as part of the Gas Distribution Price Control Review for 2008-2013 (GDPCR). The report sets out revenue, expenditure and returns on regulatory equity for the year ended 31 March 2008. It also updates benchmarking information produced for the GDPCR, summarises quality of service information, and gives the Ofgem's provisional assessment of the Regulatory Asset Value (RAV) for each licensee as at 31 March 2008. The RAV will be finalised at the next price review. The report forms the basis for developing the annual reporting process over the next four years leading up to the next Price Control Review for the gas distribution networks. [Report](#)

UK: Ofgem Releases Transmission Annual Report for 2007-08

On 30 March 2009, the Ofgem released the second annual report on transmission licensees' costs and forecast capital expenditure based on the regulatory reporting process introduced as part of the Transmission Price Control Review for 2007-12. The report set out revenue, operating cost, capital expenditure, and returns on regulatory equity for the four licensees in respect of their transmission owner responsibilities for the year ended 31 March 2008. It also provided information on system operator responsibilities for the year ended 31 March 2008 and set out the Ofgem's provisional assessment of the RAV for each licensee as at 31 March 2008. [Report](#)

UK: Ofgem Finalises National Grid Electricity Transmission and National Grid Gas System Operator Incentives

from 1 April 2009 and Publishes an Open Letter to Stakeholders

On 1 April 2009 new National Grid Electricity Transmission (NGET) and National Grid Gas (NGG) System Operator (SO) incentive schemes became effective in the UK. These incentives were previously the subject of consultation, the final proposals being published on 17 February 2009. On 28 May 2009, the Ofgem published an Open Letter providing information on the objectives, process and timetable for the development of the SO incentive schemes to be in place from April 2010. This letter responded to points, relating to both process and the detail of the incentive schemes, raised during the 2008/09 consultation. [Open Letter](#)

UK: Ofwat Releases Paper on Sustainable Development

The UK water regulator, the Ofwat, has a statutory duty to contribute to sustainable development. In March 2009 it released a document titled *Water Today, Water Tomorrow – Ofwat and Sustainability*, explaining how the Ofwat intends to perform this duty. In developing its approach, the Ofwat has built on the UK Government's five principles for sustainable development and adapted these principles to the particular circumstances of the water and sewerage sectors. The document also highlights the progress that the UK water companies have made towards becoming more sustainable and discusses where they should concentrate their efforts in future. [Link](#)

UK: Ofwat Releases Its Responses to the Environment Agency's Consultation on Draft River Basin Management Plans

On 22 December 2008, the UK Environment Agency published eleven Draft River Basin Management Plans for consultation. These plans describe the main issues for each river basin district and highlight key actions proposed for dealing with those issues. Responses to the consultation will inform the UK Government's decisions on the measures necessary to protect and improve water quality in rivers, lakes, estuaries and coastal waters, as required by the European Water Framework Directive. The Ofwat published responses to ten of the plans on 8 April 2009, and will publish the remaining response shortly. [Link](#)

UK: BAA Appeals Competition Commission's Order to Sell Airports to CAT

On 18 May 2009, the BAA, the operator of a number of major UK airports, submitted an appeal to the

Competition Appeals Tribunal (CAT) on two separate grounds against the UK Competition Commission's (UKCC) March 2009 report that requires the BAA to sell three of its airports; Gatwick, Stansted and one of either Glasgow or Edinburgh. The first ground is that the UKCC's report is affected by apparent bias. The second ground is that of proportionality of the divestiture requirements in that the UKCC failed to take into account the material cost of divestiture on BAA, in particular the adverse impact of being required to sell three airports within two years in the current financial and economic circumstances. The CAT published a summary of the BAA's application on 22 May 2009. [Link](#)

UK: UKCC Accepts Interim Undertakings in Relation to Airports Investigation

In relation to the final report on the BAA airports market investigation, the UKCC accepted, on 15 May 2009, Interim Undertakings from FGP Topco Limited, ADI Finance 2 Limited, BAA Limited, BAA Airports Limited, BAA (AH) Limited, BAA (Non Des Topco) Limited, Gatwick Airport Limited, Stansted Airport Limited, Glasgow Airport Limited and Edinburgh Airport Limited. The Interim Undertakings will prevent action being taken by the signatories that might impede the UKCC's remedies to mitigate or prevent the adverse effects on competition identified in the investigation. [Link](#)

UK: CAA Determines Price Controls for Stansted Airport for 2009-2014

On 13 March 2009, the CAA published its decisions for the setting of new price controls at Stansted airport for the five years from 1 April 2009 to 31 March 2014 (the Q5 price control) and for addressing three public-interest findings made by the UKCC in relation to service quality, user consultation and the structure of airport charges. [Decision](#)

UK: UKCC Makes Final Order in Domestic Bulk Liquefied Petroleum Gas Market Investigation

On 29 June 2006, the UKCC released the final report of its inquiry into the supply of bulk liquefied petroleum gas (LPG) for domestic use. The UKCC found that there are features of the market which adversely affect competition in the UK and thus decided on a package of remedies to address these and the consequential detrimental effects on customers. On 13 October 2008 the UKCC published an Order which came into effect on 13 April 2009 and provided for remedies for certain customers. That Order, however, did not apply to domestic customers who received their supply of LPG as part of a metered estate. That is, where a LPG customer is supplied using a tank(s) and pipes which supply more

than one customer and individual consumption is measured by a meter. Following consultation on a draft Order, the UKCC published a second Order on 6 May 2009 that applies to Metered Estate supply arrangements. [Order](#)

UK: UKCC Spring Lecture: Utility Regulation, the Regulatory Asset Base and the Cost of Capital

The UKCC held the latest in its series of Spring Lectures on Wednesday 6 May 2009 with a lecture by Professor Dieter Helm CBE, from the University of Oxford on 'Utility Regulation, the Regulatory Asset Base and the Cost of Capital.' [Text of the lecture.](#) [Accompanying Slides.](#)

US: FERC Approves Several Transmission Plans

Order No. 890, issued in February 2007, reformed the Federal Energy Regulatory Commission's (FERC's) pro forma open access transmission tariff to ensure that the transmission service is provided on a non-discriminatory basis by developing an open, coordinated and transparent transmission planning process. The FERC recently approved, with certain conditions, transmission plans submitted by several regional transmission companies. On 21 May 2009 the FERC also announced that it will convene regional conferences later in the year to determine whether transmission providers' planning efforts can meet the challenges posed by wider integration of regional energy resources into the national power grid. [Link](#)

US: FERC Commissions Study on the Use of Frequency Response to Assess Reliable Integration of Wind and Other Renewable Resources

On 13 May 2009, the Federal Energy Regulatory Commission (FERC) commissioned a new study, to be completed within six months, from Lawrence Berkeley National Laboratory. The study will examine whether Frequency Response is a reliable metric to determine how much renewable energy can be reliably integrated into the bulk power system. If so, the resulting metric will be used to assess the reliability impact of various levels of renewable energy on the grid. These issues are particularly important given state renewable energy goals and the possibility of national minimum renewable energy goals. The FERC will use the study's results to validate an approach to assessing the reliability impacts of integrating renewable energy into the grid. [Link](#)

US: FERC Staff Presentations – State of the Markets Report 2008 and Summer Market and Reliability Assessment

On 16 April 2009 staff from the FERC's Office of Enforcement presented the State of the Markets Report 2008 to the FERC Commissioners and published the presentation on the FERC's website. The Report highlights observations about natural gas and electricity markets' performance in a particular year. The 2008 Report will be published shortly. The presentation of the 2008 Report focuses on a number of overarching themes:

- Fluctuations in natural gas prices during 2008 leading to record high prices in the US summer.
- The impact of the GFC on the role of financial products and participants in energy markets, as well as on the cost of, and access to, capital.
- The impact of fuel and commodity prices and the financial crisis on energy market outcomes.
- The emergence of alternative energy options, including energy efficiency, demand response and wind generation.
- Planned expansion of centrally administered electricity markets, including in regions that have depended solely on bilateral trading. [Presentation](#)

On 21 May 2009 FERC staff presented the 2009 Summer Market and Reliability Assessment to the FERC Commissioners. The presentation reflected staff's view of the key issues likely to influence the US energy markets in the summer of 2009 and discussed the market developments that staff intend to monitor during the summer. [Link](#)

Regulatory Decisions in Australia and New Zealand

New Zealand

Commerce Commission to Commence Mobile Roaming Investigation

On 30 June 2009, the Commerce Commission announced its intention to commence a Schedule 3 investigation into whether regulation of the national mobile roaming service should be extended to include price. The Commerce Commission plans to commence the investigation in August 2009 and release a draft report in mid October 2009. [Media Release](#)

Commerce Commission Releases Draft Recommendation to Regulate Mobile Termination Prices

On 30 June 2009, the Commerce Commission released its draft report recommending that mobile termination rates should be regulated, as they are significantly above cost. The Commerce Commission also recommended that the undertakings submitted in lieu of regulation by Vodafone, Telecom and 2degrees should be rejected. Consultation on the draft recommendations will close on 27 July 2009. [Media Release](#)

Commerce Commission Declines Transpower Request to Amend Settlement

On 22 June 2009 the Commerce Commission declined a request from Transpower that the Commission amend the administrative settlement that it reached with Transpower in 2008, in relation to breaches of the thresholds set under Part 4A of the *Commerce Act 1986*. Transpower sought an amendment to the settlement in order to remove its exposure to instantaneous reserve fees by allowing Transpower to pass through these costs to South Island generators, rather than absorbing them into Transpower's own operating costs. [Media Release](#)

Commerce Commission Releases Discussion Documents on Part 4 of the Commerce Act

The Commerce Commission released on 19 June 2009 three key discussion documents relating to regulation under the new Part 4 of the *Commerce Act* and also released revised draft guidelines on its approach to estimating the cost of capital. See Notes on Interesting Decisions.

Commerce Commission Issues Sub-Loop Decisions

The Commerce Commission released on 18 June 2009 its decision on the price and non-price terms on which Telecom must make the unbundled sub-loop services available to other telecommunications providers. [Media Release](#)

Commerce Commission Finds that Electricity Companies Have Not Breached the Commerce Act

On 21 May 2009, the Commerce Commission announced it had concluded its principal investigation into whether any participants in the wholesale or retail electricity markets may have breached Part 2 of the *Commerce Act*. The Commerce Commission found no evidence of breaches of the Act, although one warning was issued regarding a risk of a breach. See Notes on Interesting Decisions

Commerce Commission Finalises Review of Backhaul Services

On 1 May 2009 the Commerce Commission finalised its first review of backhaul services. The review looked at a number of backhaul routes and examined whether there was actual or potential competition to Telecom on them. The Commerce Commission concluded some routes not to be competitive, and regulated backhaul services were made available on those routes from 15 May 2009. [Media Release](#)

Telecommunications Market Monitoring Report for 2008 Released

On 14 April 2009 the Commerce Commission released its 2008 telecommunications monitoring report analysing the state of New Zealand telecommunications markets. The report highlights signs of increasing competition in fixed line markets during 2008. [Report](#)

Arrangements to Ensure Continuity of Telecommunications Decisions at Commerce Commission

On 2 April 2009, the Commerce Commission announced that plans had been put in place to ensure continuity of the large workload of telecommunications decisions during the period of transition being experienced. [Media Release](#)

Commerce Commission Releases Final Requirements for Regulatory Financial Reporting by Telecom

On 25 March 2009 the Commerce Commission issued the regulatory requirements for the accounting separation of Telecom. The first set of financial information will be released by Telecom in December 2009 for the financial year ending 30 June 2009. [Media Release](#)

Australian Competition and Consumer Commission (ACCC)

ACCC Submits Advice on Water Charge (Infrastructure) Rules

On 26 June 2009 the ACCC provided its final advice on the water infrastructure charge rules to the Minister for Climate Change and Water. The final advice followed draft advice issued with the draft rules in April 2009, in which the ACCC recommended a three tier approach to regulating water charges, public consultation on two issues papers and a position paper during 2008. [Media Release](#)

Water Market Rules and Water Charge (Termination Fees) Rules Commence – ACCC Issues Guides

On 23 June 2009 the Water Market Rules 2009 and Water Charge (Termination Fees) Rules 2009 came into effect after being registered by the Minister for Climate Change and Water in accordance with the *Water Act 2007*. The ACCC also issued guides to help irrigators and infrastructure operators understand the new arrangements. [Media Release](#)

ACCC Issues Draft Advice for Water Planning, Management Charge Rules

The ACCC issued on 8 May 2009 its draft water planning and management charge rules and draft advice to the Minister for Climate Change and Water, for public consultation. The proposed rules would require state government departments or agencies to publish details of water planning and management charges. The ACCC also intends to collect data and report annually on water planning and management activities, costs and cost recovery from users. Submissions on the draft rules and draft advice were due on 5 June 2009. [Media Release](#)

ACCC Rationalises Telecommunications Regulation

On 17 June 2009 the ACCC released its final report following a public inquiry into the digital data access service (DDAS) and the integrated services digital

network (ISDN). The ACCC decided to cease regulation of the DDAS and ISDN by allowing the declarations to expire on 30 June 2009. [Final Report](#)

Telecommunications Competition: Signs of Life but Yet to Thrive

On 16 June 2009 the ACCC published its *Telecommunications Reports 2007-08*. The report concluded that, while consumers have been rewarded with greater competition and investment in telecommunications, the current structure of the industry is likely to limit future pay-offs. [Media Release](#)

ACCC Proposes a Five-year Extension for Key Telecommunications Declarations

On 4 June 2009, the ACCC announced its intent to extend the declarations that enable Telstra's competitors to provide fixed voice and broadband services over Telstra's copper network for a further five years. Submissions on the draft decision were due on 25 June 2009. [Media Release](#)

ACCC Issues MTAS Declaration Final Report

The ACCC released the final report on its public inquiry into the declaration of the domestic mobile terminating access service (MTAS) on 1 June 2009. The report outlines the ACCC's decision to extend the existing MTAS declaration for a period of five years to 30 June 2014. [Media Release](#)

ACCC Invites Comment on Australian Rail Track Corporation Hunter Valley Rail Network Access Undertaking

On 29 May 2009 the ACCC invited submissions on the Australian Rail Track Corporation's voluntary access undertaking for the Hunter Valley rail network. If accepted by the ACCC, the undertaking will form the basis for third parties to negotiate access to the services covered by the undertaking. The period for submissions closed on 26 June 2009. [Media Release](#)

Competition Tribunal Requires Telstra to Provide Network Access to Optus

On 22 May 2009, the Competition Tribunal handed down a decision rejecting Telstra's exemption application to restrict regulated access for Optus in areas where Optus has its Hybrid Fibre Coaxial cable network. The decision confirmed an ongoing obligation on the part of Telstra to provide Optus with regulated access to its copper network in all areas of Australia. [Media Release](#)

ACCC Begins Consultation on Wheat Export Undertakings

On 29 April 2009 the ACCC invited submissions from participants in the wheat export industry on proposed undertakings lodged by Co-operative Bulk Handling Ltd, GrainCorp Operations Limited and ABB Grain Ltd relating to access to port terminal services for bulk wheat export at each of the export terminals they operate. The undertakings set out the terms and conditions under which CBH, GrainCorp and ABB propose to provide access to port terminal facilities for the export of bulk wheat. Submissions closed on 29 May 2009. [Media Release](#)

ACCC Issues Final Decision to Again Reject Telstra's Unreasonable ULLS Undertaking

The ACCC issued on 28 April 2009 its final decision to reject Telstra's Undertaking application for a \$30 monthly charge for the Unconditioned Local Loop Service in metropolitan areas. The ACCC considered the proposed charge to be unreasonable and unlikely to promote competition. [Media Release](#)

ACCC Finalises Access Arrangements for Digital Radio

On 23 April 2009 the ACCC finalised the access undertakings which set out the terms and conditions to apply to digital radio broadcasters and digital radio multiplex transmission service providers. This decision concludes 18 months of extensive consultation by the ACCC with industry and other interested stakeholders. [Media Release](#)

Australian Energy Regulator (AER)

AER Publishes Final Decision on Review of WACC Parameters for Electricity Transmission and Distribution Businesses

On 1 May 2009, the AER released its final decision on its first five-yearly industry-wide review of the WACC parameters for electricity transmission and distribution businesses. [Link](#)

AER Issues Final Decision on ACT and NSW Electricity Distribution Determinations

In April 2009, the AER released its final decision and distribution determinations for Country Energy, EnergyAustralia, Integral Energy and ActewAGL, for the regulatory control period 1 July 2009 to 30 June 2014. [Link](#)

AER Issues Final Decisions and Transmission Determinations for Transend and TransGrid

In April 2009 the AER released its final decision and transmission determination for both Transend and TransGrid for the regulatory control period 1 July 2009 to 30 June 2014. [Transend](#), [TransGrid](#)

Withdrawal of GasNet Access Arrangement Variation Proposal

In May 2009, the AER received formal notification from APA GasNet Australia Pty Ltd (GasNet) of the voluntary withdrawal of their access arrangement variation proposal, which was submitted to the AER on 18 December 2008 and the subject of a draft decision on 14 April 2009. [Link](#)

AER Issues Rebidding and Technical Parameters Guideline

On 7 April 2009 the AER released its draft Rebidding and Technical Parameters Guideline. The draft guideline covers several related areas associated with the bidding and rebidding of technical parameters, following the commencement of new Rules on 31 March 2009. Submissions were due 15 May 2009. [Link](#)

Australian Energy Markets Commission (AEMC)

AEMC Releases Issues Papers Relating to the Reliability Standard

On 26 June 2009, the Reliability Panel published two Issues Papers in respect of its Review of the Reliability Standard and Settings and its Review of the Operational Arrangements for the Reliability Standard. Submissions on the Reviews are due 14 August 2009 and 31 July 2009 respectively. [Reliability Standard and Settings](#), [Operational Arrangements](#)

Consultant Reports for Review into the Use of Total Factor Productivity for the Determination of Prices and Revenues

On 12 June 2009 the AEMC released three consultants' reports for public comment in relation to the Review into the Use of Total Factor Productivity for the Determination of Prices and Revenues. Submissions on the reports are due 31 July 2009. [Link](#)

New Version of the National Electricity Rules

On 28 May 2009 the AEMC published a new version of the National Electricity Rules. The new version consolidated two Rules made by the Commission into version 29 of the Rules. [Link](#)

Release of Frontier Economics' Report on the Impacts of Climate Change Policies on Electricity Retailers

On 27 May 2009, the AEMC released a report by Frontier Economics on the Impacts of Climate Change Policies on Electricity Retailers. The report is to further inform the AEMC's thinking and the discussion around the energy retail aspects of the Review of Energy Market Frameworks in light of Climate Change Policies. See Notes on Interesting Decisions.

Terms of Reference Released on Review of Extreme Weather Events and Electricity Supply

On 21 May 2009 the AEMC released Terms of Reference for the Review of the Effectiveness of National Electricity Market Security and Reliability Arrangements in light of Extreme Weather Events. [Link](#)

National Competition Council

NCC Makes its Final Recommendation on Certification of the NSW Water Industry Access Regime

On 11 May 2009 the NCC dispatched its final recommendation to the Commonwealth Minister on the effectiveness of the NSW access regime for water industry infrastructure services. The final recommendation follows the publication of a draft recommendation on 2 April 2009. [Link](#)

Third Party Access to Pilbara Railways

The Australian Competition Tribunal is considering applications for review of declaration decisions regarding the Mt Newman, Goldsworthy, Robe and Hamersley railway services in the Pilbara region, Western Australia. The timetable proposed by BHP Billiton, Rio Tinto and FMG/TPI intends that a hearing commence on 28 September 2009. [Link \(NCC\)](#)

Australian Capital Territory

Independent Competition and Regulatory Commission (ICRC)

Retail Prices for Non-contestable Electricity Customers 2009-2010

On 5 June 2009 the ICRC released its Final Decision and Price Direction on retail prices for non-contestable electricity customers in the ACT. [Final Decision](#)

GreenPower Scheme Licence Variation

On 25 March 2009, the ICRC varied all electricity supply licences granted under the *Utilities Act 2000* (the Utilities Act) The variations give effect to the ACT GreenPower Scheme and take account of requirements imposed under the Electricity Feed-in Scheme in relation to electricity supply utilities. The ICRC published an open letter to stakeholders regarding the variations. [Letter](#)

Sanctuary Energy Application for Electricity Supply Licence

On 7 April 2009 the ICRC agreed in principle to grant a licence to Sanctuary Energy for the supply of electricity in the ACT. [Link](#)

New South Wales

Independent Pricing and Regulatory Tribunal (IPART)

IPART Releases Determinations on Water Prices

On 24 April 2009 the IPART released a draft determination on water, sewerage and stormwater charges for the Hunter. On 15 May 2009, it released final determinations on water, sewerage and stormwater charges for Gosford and Wyong. On 5 June 2009, the IPART also released its final determination on the prices that the Sydney Catchment Authority (SCA) charges Sydney Water and its other customers for providing water from Sydney's dams. [The Hunter](#), [Gosford and Wyong](#), [SCA](#)

IPART Releases Final Determination on Regulated Retail Electricity Prices

On 20 May 2009 the IPART released its final report for 2009/10 of the electricity purchase allowance that is included in regulated electricity prices. This followed a draft report released in March 2009. [Media Release](#)

Queensland

Queensland Competition Authority (QCA) Review of Electricity Pricing and Tariff Structures

On 25 June 2009, the QCA received a Direction from the Premier and the Treasurer to conduct a Review of Electricity Pricing and Tariff Structures. The review will examine the current Benchmark Retail Cost Index (BRCI) methodology, as well as Queensland's existing retail electricity tariffs and alternative tariff structures. The QCA released a Request for Comments Paper on 25 June 2009 and submissions are due on 16 July 2009. [Media Release](#)

QCA Completes MTA Review for Ergon Energy

The QCA commenced its 2009 review of Ergon Energy's Minimalist Transitioning Approach (MTA) arrangements in April 2009. On 27 April 2009, the QCA released an Issues Paper inviting submissions from interested parties. On 24 June 2009, the QCA decided that the MTA arrangements should remain in force, to be reviewed again in 2010. [Media Release](#)

Final Decision on 2009-10 BRCI

On 9 June 2009 the QCA released its Final Decision on the Benchmark Retail Cost Index (BRCI) for 2009-10, which is used to adjust notified (regulated) electricity prices annually. The QCA also released a Consultation Paper on 8 May 2009, proposing an alternative method for estimating the NEM load. Load Traces calculated by this method were used in the Final Decision on the BRCI. [Link](#)

DBCT Access Undertaking ARR Roll-Forward 2009-10

On 28 May 2009 the QCA approved the roll-forward of the Dalrymple Bay Coal Terminal (DBCT) Annual Revenue Requirement (ARR) for 2009-10. The DBCT access undertaking provides for the QCA to approve the annual roll-forward of the terminal's regulated revenues and tariffs. [Link](#)

QCA Approves QR Network's DAAU to Extend Termination Date

On 25 May 2009 the QCA approved QR Network's draft amending access undertaking (DAAU) to extend the termination date of its 2008 undertaking from 30 June 2009 to 31 December 2009. [Link](#)

South Australia

Essential Services Commission of South Australia (ESCOSA)

Draft Decision on Licence Conditions for Wind Generators

On 25 June 2009, the ESCOSA published a Draft Decision Paper setting out their draft conclusions on wind generation license conditions which it considers will ensure South Australia can continue to reap the benefits of increased wind generation capacity while at the same time ensuring that electricity system reliability issues are appropriately addressed. Submissions are due on 24 July 2009. [Media Release](#)

Application for Pass Through of Costs Associated with the Residential Energy Efficiency Scheme (REES)

On 2 June 2009, the ESCOSA received applications from AGL South Australia and Origin Energy to pass costs associated with the introduction of the Residential Energy Efficiency Scheme (REES) through to regulated energy retail prices. The cost pass through, to take effect from 1 July 2009, would apply to standing contract electricity prices charged by AGL South Australia and standing contract gas prices charged by Origin Energy. [Link](#)

AGL SA's 2009/10 Adjustment of Electricity Retailer Tariffs

On 29 May 2009 the ESCOSA published a Statement of Approval submitted by AGL SA, of SA electricity standing contract retailer tariffs for the regulatory period 1 July 2009 – 30 June 2010, in accordance with the 2007 Price Determination. The ESCOSA will assess the statement to ensure it complies with all relevant requirements of the Determination. [Link](#)

Origin Energy's 2009/10 Adjustment of Gas Retailer Tariffs

On 28 May 2009, Origin Energy submitted a Statement of Approval of SA gas standing contract retailer tariffs for the regulatory period 1 July 2009 – 30 June 2010, in accordance with the 2008 Price Determination. The ESCOSA will assess the statement to ensure it complies with all relevant requirements of the Determination. [Link](#)

Inquiry into 2009/10 Water & Wastewater Pricing Processes - Issues Paper

On 2 April 2009, the ESCOSA published an Issues Paper regarding an inquiry into the processes followed by Government in setting the 2009/10 water and wastewater prices. Submissions to the Issues Paper were due by 1 May 2009. [Issues Paper](#)

Tasmania

Office of the Tasmanian Energy Regulator (OTTER)

OTTER Approves Aurora Energy's Pricing Proposals

The OTTER approved Aurora's Network Tariff Pricing Proposal for 2009 - 10 on 22 May 2009 and Aurora's Retail Tariff Pricing Proposal for 2009 -10 on 5 June 2009. The OTTER also released a Statement of Reasons setting out the reasons for and decisions in regard to the approval. [Statement of Reasons](#)

Treasurer Releases Two Documents Prepared by OTTER

On 15 April 2009, the Treasurer released a draft Interim Price Order as well as the advice from the Economic Regulator contained in the 'Final Report to Inform the Development of an Interim Pricing Order for the Tasmanian Water and Sewerage Sector' and the 'Revised Interim Pricing Analysis for the Tasmanian Water and Sewerage Sector'. The OTTER provided this advice to the Treasurer on 18 February 2009, in response to a request that it revise its analysis presented in the Interim Pricing Inquiry Report of November 2008. [Link](#)

Western Australia

Economic Regulation Authority (ERA)

2009 WACC Determination – The Pilbara Infrastructure Railway

On 22 June 2009, the ERA published its Final Determination on the 2009 Weighted Average Cost of Capital (WACC) for The Pilbara Infrastructure's (TPI) railway in the Pilbara. The ERA determined that the 2009 WACC, to apply to TPI's railway from 1 July 2009 to 30 June 2010, is 11.09 per-cent (real pre-tax). [Media Release](#)

2009 WACC Determination – Freight and Urban Rail Networks

On 19 June 2009, the ERA determined the WACC for both the freight and urban rail networks as at 30 June 2009, as required by the *Railways (Access) Code 2000*. The ERA determined that the 2009 WACC, to apply from 1 July 2009 to 30 June 2010, is 8.63 per cent for the freight network and 5.99 per-cent for the urban network (real pre-tax). [Media Release](#)

Issues Paper Released in the Inquiry into Water Resource Management and Planning Charges

On 30 April 2009 the ERA published an issues paper on its inquiry into water resource management and planning charges. The inquiry is to provide the State Government with a range of options and recommendations to recover water resource planning and management costs incurred by the Department of Water in the sustainable management of the State's water resources. Submissions on the inquiry were due by 12 June 2009. [Media Release](#)

IMO Publishes Report on Reserve Capacity Mechanism

In May 2009, the Western Australian Independent Market Operator (IMO) published its report on the reserve capacity mechanism, concluding that there appears to be sufficient projected capacity to comfortably meet projected demand until 2014-15. [Report](#)

Notes on Interesting Decisions

UK: Ofgem Releases Report on Increasing User Participation in Energy Regulatory Framework

On 28 March 2009 the Ofgem released a report commissioned from Stephen Littlechild and Nigel Cornwall that examines the scope for different ways of increasing user participation in the Great Britain energy sector regulatory framework, in particular, the forthcoming fifth electricity transmission price control review (termed TPCR5). Littlechild and Cornwall have looked in detail at four potentially relevant approaches that have actually been used in other jurisdictions or in other markets: the Public Contest Method as used in Argentina; the UK's constructive engagement approach; negotiated settlements as applied in parts of the US and Canada; and the Australian negotiated services approach.

Littlechild and Cornwall conclude that increased user and consumer involvement is already being incorporated in electricity regulation in Britain. However, there is scope to increase involvement and each of the four approaches considered has potential benefits and direct potential relevance in this regard, although each also has limitations. At this stage, Littlechild and Cornwall consider that an approach based on constructive engagement is the most promising prospect for further development, but note that it would need to be modified to reflect the particular conditions of the energy sector and that more research is required as to how such an arrangement could and should be developed and applied.

Littlechild and Cornwall note that any shift to a constructive engagement approach would require certain changes to the way the Ofgem conducts the periodic regulatory review. For example, in order to implement constructive engagement for TPCR5, the Ofgem would need to indicate clearly its commitment to such an approach and to set out the main elements of the process. [Report](#)

Stephen Littlechild is speaking at this year's ACCC Regulatory Conference on the topic, 'Are there Substitutes for Traditional Economic Regulation of Monopoly Infrastructure?'

UK: Ofgem Relaxes Industry Rules to Allow Faster Connection of Wind and Low-Carbon Generators

On 8 May 2009 the Ofgem announced a temporary relaxation of industry rules for connection to, and use of, the high-voltage electricity networks, to allow

much faster connection of wind and low-carbon generators. In particular, such generators will no longer be delayed by the need to invest in the grid. This is an interim measure to speed up connections until more enduring reforms to access arrangements are introduced. It is expected that some generators in 'a large queue of renewable projects' could start to connect this year.

The decision to relax rules for generation connection will mean that more new generators could get connected sooner but they may have to restrict their output from time to time, so that the system remains secure in operation. Any generator that is asked to reduce output receives compensation payments from National Grid. The Ofgem has asked National Grid to consider how it will address increases in such constraint payments, which are passed on to all electricity customers.

The revised connection approach followed the Ofgem's approval, in April 2009, of funding of £12.5 million so that two of the three electricity transmission companies can start feasibility studies and preparatory work on the investment needed to support new renewable generation connections to meet the UK's 2020 targets. The Ofgem is also developing new incentives for transmission companies which would enable them to earn a higher return for taking on some of the risk of building new transmission capacity in anticipation of new sustainable generation projects seeking connections to the grid. [Press Release](#)

Europe: EEA Recommends New Approach to Managing Water Resources

On 17 March 2009 the European Environment Agency (EEA) released a report, *Water Resources Across Europe — Confronting Water Scarcity and Drought*, confirming that water use is unsustainable in many parts of Europe. Historically, most Europeans have been insulated from the social, economic and environmental impacts of severe water shortages. However, the report identifies that due to over-abstraction and prolonged periods of low rainfall or drought, the balance between water demand and availability has reached a critical level in many areas of Europe. As a result, the EU has grown increasingly concerned with addressing issues of water scarcity. The Water Framework Directive, for example, promotes 'sustainable water use based on a long-term protection of available water resources'.

The EEA recommends a new approach to managing water resources that shifts the management focus from increasing supply to minimising demand. The

report identifies water pricing to be a key mechanism to achieve more sustainable water use, consistent with the requirement set out in the Water Framework Directive that water services be priced to reflect their full costs. The EEA therefore recommends that in all sectors, including agriculture, water should be priced according to the volume used and that metering be implemented across all sectors to achieve this. Other demand side policies identified by the EEA include awareness raising, tackling illegal water abstraction and promoting the efficient use of water through investment in new technologies and through linking agricultural subsidies to more efficient water use.

While, the EEA recommends that policies focus primarily on demand-side measures, it notes that expansion of supply may still be required in some regions. In those regions alternative sources of water supply should be accessed in a sustainable manner, such as through desalination or treatment of municipal water. [Report](#)

NZ: Commerce Commission Releases Discussion Documents on Part 4 of the Commerce Act

The Commerce Commission released on 19 June 2009 three key discussion documents relating to regulation under the new Part 4 of the Commerce Act, which regulates suppliers of electricity lines services, including Transpower New Zealand Limited, gas pipeline services and certain services supplied at Auckland, Wellington and Christchurch airports. In addition, the Commerce Commission has released revised draft guidelines on its approach to estimating the cost of capital.

The input methodologies discussion paper outlines the Commerce Commission's preliminary views on the key building blocks of the Part 4 regime including the cost of capital, the valuation of assets, the allocation of common costs and the treatment of taxation. The revised draft guidelines on estimating the cost of capital were released alongside this discussion paper, since the guidelines provide the framework for the input methodologies associated with the cost of capital.

The discussion paper on the reset of default price-quality paths for suppliers of electricity lines services (other than Transpower) sets out the Commerce Commission's preliminary views on how the default price-quality paths that apply to these suppliers (other than consumer-owned suppliers) should be reset. The reset will apply from 1 April 2010. The Transpower process and recommendation discussion paper outlines preliminary views on the options for price-quality regulation of Transpower.

The period for written submissions on all three discussion papers will close by the end of July 2009. In addition, the Commerce Commission intends to hold workshops on specific issues and is planning a conference on input methodologies for September 2009. The Commerce Commission is required to publish a summary of the determination containing the default price-quality paths by December 2009. [Discussion Documents](#), [Media Release](#)

NZ: Commerce Commission Finds that Electricity Companies Have Not Breached the Commerce Act

On 21 May 2009, the Commerce Commission announced it had concluded its principal investigation into whether any participants in the wholesale or retail electricity markets may have breached Part 2 of the *Commerce Act*. The investigation was opened in late 2005 after a number of complaints about high electricity prices, large company profits, a perceived low level of competitive activity and allegations of anti-competitive conduct. The investigation focused on the vertically integrated generator-retailers (also known as gentailers). In particular, the investigation considered whether they had market power and, if so, whether they had taken advantage of that market power for a proscribed purpose, namely the hindering or deterring of competitors in breach of section 36 of the *Commerce Act*. In addition, the Commerce Commission investigated whether any gentailers had behaved in a collusive manner in breach of sections 27 or 30.

The section 36 part of the investigation included an economic analysis of the wholesale market undertaken on the Commerce Commission's behalf by the Chairman of the market surveillance committee of the California Independent System Operator, Professor Frank Wolak of Stanford University. Professor Wolak's work is based on an analysis of data relating to the New Zealand wholesale electricity market for every half-hour period for every day from January 2001 to July 2007. The Commerce Commission concluded that each of the four largest gentailers – Contact, Genesis, Meridian and Mighty River Power had the opportunity to exercise market power on a recurring basis, particularly during dry periods. However, in increasing wholesale prices, gentailers had only been maximising profits within the current market structure and rules. The Competition Commission concluded that their behaviour did not amount to a breach of section 36 of the *Commerce Act*, not having an 'anticompetitive purpose'.

In terms of collusive conduct, The Commerce Commission found that Trustpower may have been at risk of breaching section 27 of the Act in 2004 and accordingly issued a warning to that company. Otherwise, the Commerce Commission found no evidence of collusive activity. One specific and limited event continues to be investigated by the Commerce Commission. The Commerce Commission also did not find a breach in the retail sector under the investigation to date and therefore determined there to be no basis for the Commerce Commission to make further assessment of the retail market or the effects of vertical integration.

In response to a number of requests, the Commerce Commission released both its full investigation report and the report of Professor Frank Wolak, under the provisions of the Official Information Act. [Investigation Report Documents](#), [Media Release](#).

AEMC Releases Frontier Economics' Report on the Impacts of Climate Change Policies on Electricity Retailers

The AEMC Review of Energy Market Frameworks in light of Climate Change Policies commenced in August 2008, on the direction of the Ministerial Council on Energy (MCE). The review is intended to examine the resilience of energy market frameworks to the changes in behaviour expected to result from the implementation of a Carbon Pollution Reduction Scheme (CPRS) and an expanded national Renewable Energy Target (expanded RET). The review will consider what, if any, existing market frameworks may require amendment and will conclude with advice to MCE in September 2009. [Link](#)

In May 2009, the AEMC released a report by Frontier Economics on the Impacts of Climate Change Policies on Electricity Retailers. The report is to further inform the AEMC's thinking and the discussion around the energy retail aspects of the Review of Energy Market Frameworks in light of Climate Change Policies. The report illustrates the materiality of the cost and volatility of the proposed CPRS on electricity retailers by analysing the various factors affecting carbon prices and the likely impact on electricity prices. The report also considers strategies likely to be used by retailers to manage their carbon risk. The report concludes that margin squeeze and threats to the financial viability of retailers will be of concern 'if regulated tariffs to end-use consumers do not adequately address the increased costs and risks that retailers will face under the CPRS'. [Frontier Report](#)

Regulatory News

International Benchmarking the Economic Regulation of Infrastructure

The ACCC has recently completed a research project for the Infrastructure Consultative Committee (ICC) on International Benchmarking of the Economic Regulation of Infrastructure. The research covers seven infrastructure areas (energy, telecommunications, posts, water and wastewater, rail, airports and ports) across eleven benchmark countries (Japan, Australia, New Zealand, France, Germany, Ireland, the Netherlands, Sweden, the United Kingdom, Canada and the United States of America). It also focuses on the role of the European Union and the relationship between competition bodies, Federal regulators and State regulators in the United States.

The report is in two parts – an **interpretative report** (covering interesting aspects of regulatory design, institutions and processes from across the benchmark countries); and a **country-based review** (containing the informational background on the regulation of the seven infrastructure areas across the eleven countries). Both documents are available on the ACCC website at:



Infrastructure
Consultative Committ

In conducting the research, ACCC staff and external consultants worked with an Advisory Committee comprised of members of the ICC drawn from a range of infrastructure areas – energy, telecommunications, water and wastewater and rail. Other members of the ICC also contributed advice on the research. Various sources of information were tapped including primary and secondary ‘desktop’ sources; personal contacts and regulator visits. Much of the European research was conducted by the Oxford-based economist, Dr Chris Decker.

The report contains many interesting ideas about regulatory design; institutional structures; alternative dispute resolution arrangements; the relationship between consultation and timeliness; methods of dealing with confidential information; and avenues for appeal of regulatory decisions. While there is much to learn from this international experience, the broad conclusion is that Australia is more a leader than a laggard in regulatory design and processes.

The country-based review is a rich data base which we hope others will find useful in their regulatory work. Because we are in the midst of so much regulatory change, it is hoped that the country-based review can be updated on an annual basis. Also, on the interpretative aspects of this work, there are a number of areas where more detailed and focused future research could be undertaken.

Tenth ACCC Regulatory Conference

The tenth ACCC Regulatory Conference will be held on 30 and 31 July 2009 at the Holiday Inn, Gold Coast, Queensland Australia. The theme for the conference is the *Regulation of Infrastructure in a Time of Transition*.

International speakers include:

Professor Tim Brennan, Professor of Public Policy and Economics, University of Maryland-Baltimore County and a Senior Fellow at Resources for the Future

Professor Ingo Vogelsang, Professor of Economics, Boston University

Professor Stephen Littlechild, Fellow, Judge Business School, University of Cambridge and a PostComm Commissioner

Professor Leslie Hannah, Visiting Professor, Department of Economic History, London School of Economics & Political Science

Professor Gary D Libecap, Research Fellow, Hoover Institution, Bren Professor of Corporate Environmental Policy and a Professor of Economics at the University of California, Santa Barbara

Professor Thomas Hazlett, Professor of Law and Economics, George Mason University, Virginia

Topics to be discussed include:

Infrastructure challenges in the early part of the twenty-first century

Regulation, incentives for investment and technological change

Are there substitutes for traditional economic regulation of monopoly infrastructure?

100 years of government control over public utilities

The challenges of climate change for energy markets

Lessons from US wireless spectrum auctions

Economic experts: How necessary are they?

The role of markets – rural to urban water trade

The conference is fully subscribed, but the papers will be placed on the ACCC website after the conference.

Forthcoming publication – *Evolution of Regulation in Australia*

The ACCC/AER is about to release their first publication in their new *Working Paper Series*. Working papers are intended to disseminate the results of current research by ACCC and AER staff and consultants. The aim of the series is to facilitate discussion and comment. The papers will be available in electronic format only from the ACCC's website (www.accc.gov.au) under publications>A-Z of publications.

The first paper in the series, *Evolution of Infrastructure Regulation in Australia*, is by Harriet Gray, who currently holds the position of Counsel with the ACCC/AER. The paper commences with an overview of the historical developments in the evolution of regulation and moves on to outline the sectoral history and current form of economic regulation for telecommunications, posts, airports, electricity and gas, rail, ports and shipping, water and petrol.

Network is a quarterly publication of the Australian Competition and Consumer Commission for the Utility Regulators Forum. For editorial enquiries please contact Rob Albon (Robert.Albon@acc.gov.au) and for mailing list enquiries please contact Katrina Huntington (Katrina.Huntington@acc.gov.au).