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IPART's Achievements

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Twenty years ago the Greiner Government established the first independent economic price regulator in Australia. Perhaps the boldness of that step is not fully appreciated. The Independent Pricing and Regulatory Tribunal (IPART), or the Government Pricing Tribunal as it was originally known, was established prior to the Hilmer report (Independent Committee of Inquiry, 1993) and its recommendations for the establishment of independent price regulation. Importantly, its focus was on the regulation of prices of government businesses. The United States (US) had a long history of regulation of privately-owned utilities. Chile and the United Kingdom (UK) separately established independent utility regulatory bodies as part of the process of privatising their utilities. In these cases, taking Ministers out of price setting was considered necessary to establish investor confidence.

But in New South Wales (NSW), the government did not link independent price setting to privatisation. In effect it was saying: 'It had previously set utility prices and the outcomes have been poor: Prices have been highly politicised and costs have been under-recovered, and the businesses have not performed well. There is seen to be a need to take the politicians out of the price-setting process and entrust the function to an independent agency operating transparently. Government's role is to set the broad objectives that this regulator must consider.'

Since IPART's establishment, independent economic regulation of government utilities has become the norm in Australia. Independent regulation of government monopolies has also become far more common overseas, often with the encouragement of international agencies such as the World Bank. These agencies have supported the independent regulation of government monopolies because they believe it is likely to provide pricing decisions that are based on evidence and are consistent through time, promoting more efficient provision and use of infrastructure services. The community's expectations of price regulators can be expressed in simpler, but more demanding terms: fair and balanced decisions.

So after 20 years, what has IPART achieved? Have the Government's initial hopes been fulfilled and how has IPART's role, and the Government's objectives, changed over time?

Overview of IPART's Achievements

In brief IPART has:

1. depoliticised pricing and made it more rational
2. improved transparency and public information
3. acted as a 'lightning conductor'
4. balanced certainty and improvement of regulatory regimes
5. provided stronger incentives for performance improvement by regulated businesses
6. depoliticised licensing
7. set standards of service
8. promoted competition in electricity, gas, transport and especially water
9. administered environmental programs
10. undertaken an expanding range of functions
11. provided a mechanism for policy development – through IPART's reviews, for example, of regulation, state taxes and local government.

Contents

* James Cox PSM is CEO and Full Time Member of IPART. This paper is based on a speech delivered at the conference *Regulation and Reform: IPART after 20 years*, held in Sydney on 10 August 2012. A full version of the speech is available on the IPART website.

One of IPART's very considerable successes has been to depoliticise pricing and make pricing more 'rational'. This has been the case in urban water pricing, as well as energy pricing.

In the case of water, charges based on property values were abolished in the mid-1990s, and the ratio of volume-based to fixed costs has increased, more accurately reflecting the structure of production costs.

A considerable degree of rationalisation in the structure of electricity prices has also occurred. The initial large cross-subsidies from business to residential customers were largely unwound through reductions in business electricity charges in the 1990s. Recent years have seen very substantial increases in electricity costs that have been passed on to consumers, without intervention by governments to artificially reduce consumer prices. However, IPART has been less successful in transport, where fares have at times been set below the levels which the Tribunal has determined.

Several important factors have contributed to these achievements:

- The objectives in the IPART Act largely reflect the community's expectations. IPART does not have a single objective under the IPART Act. Rather, the Tribunal is required to take into account a range of objectives including economic efficiency and financial sustainability, as well as impacts on consumers, the environment, the state government and taxpayers. In practice, IPART gives considerable weight to economic efficiency. Having regard to a number of objectives makes the regulator's task more difficult, but requires the Tribunal to consider all the factors that the community thinks are important. The recent difficulties which the Murray-Darling Basin Authority experienced in gaining acceptance of its draft recommendations highlights the risks of giving primacy to a single objective.
- Transparent processes and public information: IPART makes considerable efforts to ensure that its reviews are completed in a timely manner, and to make its reports as clear as possible. IPART's processes ensure that there is a greater understanding of the issues, and opportunity for stakeholders to participate, as well as a careful explanation of decisions. Stakeholders may – and do – still disagree with the decisions but they will have had a chance to participate and gain a better understanding of why the Tribunal has made the decision.
- IPART's processes enable the Government to allow debate and discussion to run at arm's length, rather than to react immediately to initial proposals that may be controversial. In effect, IPART has become a 'lightning rod'. As noted above, hopefully these processes lead to carefully considered proposals and greater community acceptance.

Over time, IPART's regulatory approach has become clearer and more consistent in its application. IPART has put considerable effort into documenting its approach. Its foundations are the 'cost building blocks' and IPART's financial models. The IPART Act gives the Tribunal considerable discretion which has been of concern to some, including asset owners. IPART has taken the view that, as Parliament has given the Tribunal this discretion, it is for Parliament, rather than IPART, to limit that discretion. However, IPART has documented its approach on the key issue of the cost of capital in considerable detail, and published papers setting out how the Tribunal will consider issues of financeability, affordability, and potential environmental impacts. IPART has been careful to consult with shareholders in developing its approach to these issues and to follow these approaches when making pricing decisions. The intention is to give greater certainty on how the Tribunal will exercise its discretion.

For most of IPART's first decade regulated businesses improved their efficiency. It can be argued that the regulatory regime was a contributing factor to this. Subsequently, productivity has deteriorated, with considerable upward pressure on prices, primarily as a result of large increases in capital expenditure for improved reliability, water security and other government-imposed requirements. To some extent, this problem arose when governments circumvented the established regulatory process.

Water Pricing Reform

One of IPART's first achievements was water pricing reform. Prior to 1990, all customers were given a certain 'water allowance' and paid for water by volume only if this allowance was exceeded. This meant that ratepayers using less than their 'water allowances', or whose properties were unmetered, confronted a zero price for the next unit of water they consumed. As this zero price was obviously less than the marginal cost of supplying that additional unit, the charging arrangements did nothing to ensure the efficient use of water. At the beginning of the 1990s, a significant part of a customer's water bill was dependent on the value of his or her property. The use of rates which were partially based on property values gave rise to a pricing system where virtually every water user had a different average cost of water.

This pricing arrangement led to a cross subsidisation of the residential sector by the commercial and industrial sectors, and resulted in a situation where Sydney had one of the cheapest residential water and wastewater bills in Australia and the most expensive non-residential bills in the world.

In 1992, the Tribunal commenced an inquiry into water pricing covering the Sydney, Newcastle, Central Coast, Illawarra and Blue Mountains regions, releasing its report in late 1993.

The Tribunal's 1993 proposals set out a program of longer-term reforms to be put in place by the metropolitan water agencies of NSW. Key elements of the reform program were:

- the elimination of water allowances where this had not already occurred,
- the progressive elimination of property value-based rates as a source of revenue with priority to be given to the reform of the non-residential sector,
- the move to a simple two-part tariff with a uniform usage charge to apply to all water used,
- the rigorous pursuit of efficiency gains by the water supply agencies accompanied by real revenue reductions over the short-to-medium term. This was accompanied with a recommendation that water agencies benchmark their activities against similar agencies internationally, and
- the adoption of charging arrangements for land developers which ensure that costs of infrastructure provision are fully recovered through a combination of common periodic charges and upfront contributions.

IPART's first role was to set prices, but as the Government has increasingly used licences to specify the rights and responsibilities of the service providers, and to impose community objectives, IPART has also been given the task of recommending which licences should be issued and monitoring the performance of licence holders. One of the spurs to this was the Sydney Water quality episode; the other was the increasing involvement of the private sector. Like pricing, there was a need to depoliticise licensing and make it more transparent – which IPART has achieved. IPART has put in place a very professional, risk-based approach to monitoring licensing performance with comprehensive independent audits. Some key licence conditions are audited annually, while others are audited less frequently, depending on the level of risk.

The start of competition in the urban water markets under WICA is now being seen. New private providers are entering the water markets providing, for example, recycled water to large industrial and commercial users as well as recycled water and sewage services to residential estates. The depoliticisation of regulation and licensing was an important pre-condition for the development of these innovative and competitive supply solutions.

Focus on Specific Areas

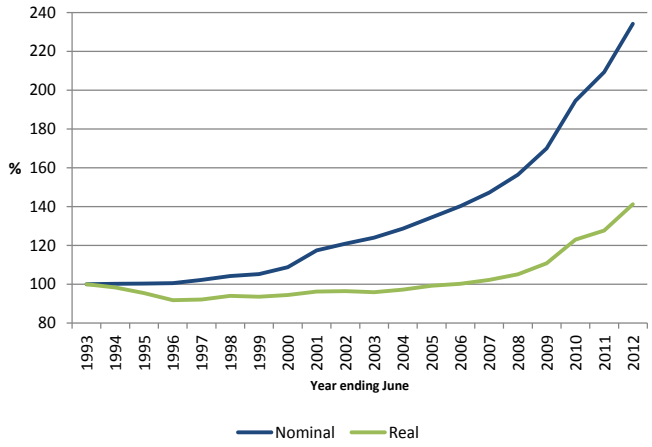
This section focuses on the course of five key economic variables – prices; capital expenditure (capex); productivity; service quality and profitability.

Prices

In 1993, IPART introduced an index of household charges to monitor the impact of its price determinations on households. Each year the index measures the weighted average change in the prices of the services it regulates, where the weights are derived from Australian Bureau of Statistics (ABS) data on household expenditure on electricity, gas, water and public transport (rail, bus and ferry services).

A graph of the composite index is shown in Figure 1.

Figure 1: Composite Index of Household Charges



Data source: IPART Analysis.

The main points are:

- Average household charges increased by 11.9 per cent in nominal terms (10.6 per cent in real terms) in 2011-12.
- By comparison, in 2010-11, the average household charges increased by only 7.6 per cent in nominal terms or 3.8 per cent in real terms.
- But this was low compared with the previous year, 2009-10, where the index rose 14.5 per cent in nominal terms (11.1 per cent in real terms).

- Since 1992-93, the index of household charges has risen a cumulative 134.1 per cent in nominal terms while the general price level has risen by 65.9 per cent.
- The rise in the index after adjusting for inflation has been 41.1 per cent, which is often stated as the rise 'in real terms'.
- The average annual nominal rise has been 4.6 per cent per annum (1.8 per cent in real terms), although much of the rise has been concentrated in the past few years.

Looking at the figures a bit closer, the past 20 years can be divided into two distinct periods.

During the 1990s, the index generally rose slower than inflation so that prices fell in real terms. This occurred mainly in the water and energy sectors, due to efficiencies brought about, in part, as a result of pressure from IPART. Public transport fares tended to rise in real terms during this period.

Since 2000, charges began to rise faster than inflation in response to a number of (largely cost) pressures, such as the need for greater infrastructure investment, including investment in the electricity networks and the desalination plant. By 2005-06, prices in real terms were back to their 1992-93 levels. Greater cost pressures have unfortunately caused larger cost increases in recent years, especially in the last three years.

Capital Expenditure

But has downward price pressure from IPART been responsible for keeping prices too low, to the extent that necessary infrastructure investment has not taken place, and now, urgently needed investment is causing the more recent price increases – especially in the electricity sector?

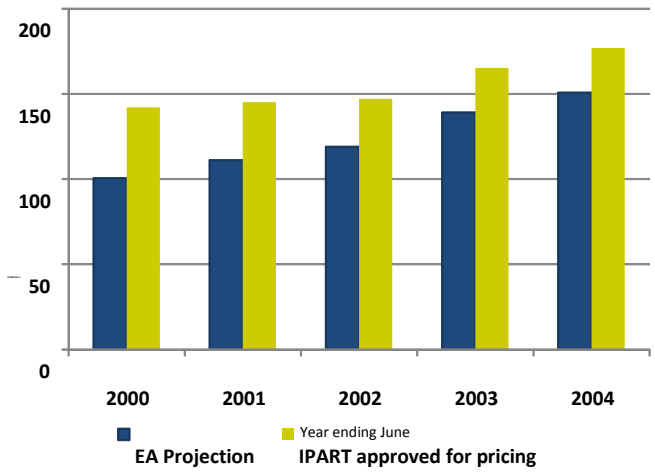
Did IPART prevent electricity networks from making prudent, gradual and timely investment over the past decade, and therefore putting them in a position where urgent 'catch-up' expenditure is now required?

This is the view put forward by George Maltabarow (2011; 2012), until recently, the Managing Director of Ausgrid (formerly EnergyAustralia).

However, a reading of IPART's pricing Determinations and Reports (IPART, 1999, pp. 83-85; IPART 2004a, p. 34; IPART 2004b, p. 31), and analysis of the figures will show that:

- IPART's revisions to EnergyAustralia's proposed capex programs were small and mostly involved revisions in the timing of projects.
- IPART has, in one instance, encouraged the electricity distributors, including EnergyAustralia, to spend more than they requested in their capex proposals. Looking back to IPART's 1999 Determination and Final Report, Figure 2 shows how the capex IPART approved to be included in its pricing decisions was higher than that which EnergyAustralia forecast in its submission.
- Thirdly, actual capital expenditure has been much greater than what the utilities themselves proposed, even in the first year of a regulatory period. This is especially evident since the announcement of new energy rules, that offer no penalty for distribution networks that spend more than their approved amounts, and arguably encourage them to do so.

Figure 2: EnergyAustralia (Ausgrid) Projected, and IPART-approved Capex – IPART Electricity Pricing Determination, 1999

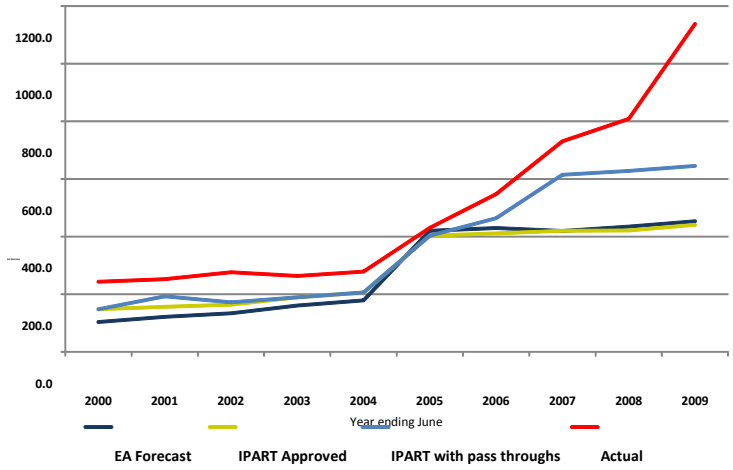


Data source: IPART, *Pricing for Electricity Networks and Retail Supply – Report, Volume 1,* June 1999.

For example, in the last three years of the 2004-05 to 2008-09 regulatory period, the NSW distribution businesses' actual capital expenditure was significantly higher than the regulatory allowances, which are determined prospectively. During the 2008-09 financial year alone, EnergyAustralia invested almost $500 million in capital more than the regulatory allowances. It should be noted that the regulatory allowances in the 2004-05 to 2008-09 period were largely based on the proposals submitted by the businesses themselves.

In fact, for every year of the entire 2000-2009 regulatory period, EnergyAustralia's actual capital expenditure outpaced both the proposals which EnergyAustralia submitted and IPART's approved limits – as can be seen in the graph in Figure 3.

Figure 3: EnergyAustralia (Ausgrid) Capital Expenditure 2000-2009



Data sources: IPART, *Pricing for Electricity Networks and Retail Supply – Report, Volume 1,* June 1999.

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IPART Analysis.

Figure 1.3 shows EnergyAustralia's proposed capex expenditure schedule, IPART's approved expenditure levels, IPART's decision after taking into account approved cost pass throughs as a result of the Full Retail Contestability (FRC) costs in 2000-01 and 2001-02 and Government's changes to reliability standards in later years.

The fourth line shows what EnergyAustralia actually spent.

In 2005-06 it became known that IPART would no longer regulate the prices for electricity networks. When the prevailing regulatory period ended, this responsibility would be transferred to the Australian Energy Regulator (AER), that would operate under different guidelines, known as the National Electricity and Gas Rules.

Coincidently or not, from the time the decision was made to transfer network regulation from IPART to the AER, the networks' capital expenditure started to dramatically increase. IPART considers that the new rules, rather than the change in regulator, was the more important factor.

In part, the higher expenditure levels may reflect the NSW distribution businesses' obligations to meet reliability of supply conditions imposed by the former NSW Government. However, the network electricity rules are likely to be encouraging this increased expenditure and resultant price rises.

In IPART's view:

- The current regulatory framework makes it difficult for the regulator not to accept the network business' spending proposals. The Rules constrain the AER's ability to apply what it considers to be the best estimate of the efficient operating and capital costs.

  The Rules provide strong incentives for network businesses to invest capital in the network because the prescriptive requirements of the Rules may yield excessive returns.

  The Rules allow the businesses to earn a return on all capital invested regardless of its efficiency and prudency, by requiring the AER to roll all capital expenditure – even if spent without being approved – into the asset base used for calculating required returns.

- They provide opportunities for the businesses to target particular issues through the appeal process.

Fortunately, these issues have been reviewed by the Australian Energy Market Commission (AEMC). IPART considers the proposed rule changes to be a significant step forward that will benefit the electricity consumers of New South Wales by moderating future prices.

In contrast to electricity, expenditure in the water sector has generally been in-line with, or below IPART's approved levels. Generally, differences between expenditure programs proposed by agencies, and IPART's approved levels, have been minor and differences with actual expenditure have related to phasing.

Productivity

It is not only retail prices and utility expenditure which IPART has been concerned with over the past 20 years. From time to time, the NSW Government has called on IPART to conduct other reviews.

In October 2009, the Government commissioned IPART to review the productivity of selected State-Owned Corporations (SOCs). These included the ports corporations, water utilities, Landcom, electricity generators, and electricity network service providers.

IPART's detailed analysis showed some telling trends in different sectors.

First, it should be noted that most SOCs it reviewed are very capital intensive, and capital investment naturally occurs in cycles. Due to the way Total Factor Productivity (or 'TFP') is measured, this 'lumpiness' can skew results. For example, Hunter Water achieved improvements in productivity in early years before they were reversed by a wave of capital

investment in 2003-04. A similar increase in capital expenditure set back Sydney Water's TFP.

However, even with measured productivity decreasing due to increasing investment, labour staff productivity over the analysis period of 1995-96 to 2008-09 substantially increased (IPART, 2010, p. 5). In the case of Sydney Water, labour productivity increased by 90 per cent, and in the case of Hunter Water, by 103 per cent (IPART, 2010, p. 28).

TFP at TransGrid declined between 1997-98 and 2008-09, mainly due to substantially increased capital expenditure on its transmission network. Reflecting this, its capital productivity declined. Nevertheless, labour productivity increased by 52 per cent (IPART, 2010, p. 47).

In contrast, not only has capital productivity declined in electricity distribution network service providers but, labour productivity also declined. Over the period 2001-02 to 2008-09, labour productivity in the electricity networks fell by between 27 per cent and 29 per cent (IPART, 2010, p. 55).

IPART made a number of recommendations on governance of SOCs to enhance and then maintain their autonomy, and ensure clear accountability for performance.

IPART believes transparent reporting of performance is an important discipline and incentive for government entities.

The Government, through Treasury, previously published an annual performance report on the SOCs, but this was discontinued in 2004. IPART encourages the Government to resume publication of these reports.

Service Quality

Price matters to the consumers of these essential services, but so does quality.

IPART's report *NSW Water Utilities Performance* (IPART 2012) – provides a number of indicators of service quality for the urban water suppliers. Some of the important quality measures for end-users are the duration of unplanned water interruptions, sewer chokes and breaks, and customer complaints.

The overall picture that emerges in water is one of stable or improving quality of service. Since 2003, complaints such as those regarding water quality, have remained at low levels (compared to its peers) for Sydney Water and declined for Hunter Water to levels that are above Sydney Water's, but comparable to its peers. The frequency of unplanned water interruptions (per 1000 households) declined from 2005-06 to 2007-08 and has remained broadly stable since then. The number of sewer main breaks and chokes has remained broadly stable over the period for both Hunter Water and Sydney Water.

Two of the most commonly used measures of service quality for electricity networks are the average duration and frequency of interruptions. The data on these indicators need to be handled cautiously. Firstly, statistical variability may well hide underlying trends or suggest trends that are not really there. Secondly, it is not known what the trends would have been if the network investment had not been undertaken, and the benefits of the increased network investment may well lag behind the actual spending.

In broad terms, though, the data suggest clearer evidence of an improvement in service quality (as measured by System Average Interruption Duration Index [SAIDI]) for Country Energy (now Essential Energy). The evidence is less clear for EnergyAustralia (now Ausgrid) where the average duration of interruptions on urban feeders has tended to increase. It should be noted that the SAIDI on EnergyAustralia's rural feeders has come down. The data for the central business district show a higher degree of fluctuation from year to year, making interpretation difficult.

Profitability

Although IPART encourages the utilities it regulates to be efficient and productive, and to minimise their prices, it also has a responsibility to the shareholders of those agencies, in most cases the NSW Government, to ensure those entities are run in a business-like manner, are profitable and earn a reasonable return on their investment.

According to data from the Auditor-General's reports to parliament, distributions to the NSW government – a combination of dividends and tax paid – by some of IPART's largest regulated entities were significant. Between 2003 and 2008 Hunter Water's distributions were around $50 million per year, while Sydney Water and EnergyAustralia (now Ausgrid) distributed between $100 million and $300 million per year. The fact that these agencies were able to make these tax and dividend payments refutes the assertion that IPART's pricing policies are squeezing the ability of the agencies to operate their businesses successfully.

Expressed as a return on investment, this figure is not excessive by commercial business standards. The Auditor-General's reports show returns for the water utilities have been around 2 to 4 per cent, while that for EnergyAustralia has been somewhat higher. However, these calculations are based on the replacement costs of assets which, for water, differ from the regulatory asset base that is used in price determinations.

Conclusion

In conclusion, the past 20 years has been quite a journey and IPART's achievements have been many, especially in the areas of:

- moderating price increases and increasing productivity
- encouraging responsible investment
- making price structures fair and cost reflective
- promoting competition, and
- maintaining a high and increasing level of service quality.

It is likely that the next 20 years will see even greater challenges and achievements.

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Critical Issues in Regulation – From the Journals

'Consumer Protection and Contingent Charges', Mark Armstrong and John Vickers, Journal of Economic Literature; 50(2), 2012, pp. 477-493.

Armstrong and Vickers examine the economics of contingent charges. These are charges incurred by consumers only if particular circumstances ('contingencies') arise. Examples include: unauthorised bank overdraft fees (fees charged where an account becomes negative); late payment fees for credit cards; mini-bar charges in hotel rooms; and international roaming charges for mobile phones. The authors argue that consumers are often unaware of contingent charges either because they do not know of them and/or they are not aware of the circumstances in which they would be charged.

Armstrong and Vickers examine whether unregulated contingent charges give rise to economic inefficiencies. Further, they ask: When do contingent charges cause undesirable distributional effects? Finally, they consider whether regulation can improve outcomes? A model of contingency charges with bank accounts is presented. Banking consumers are disaggregated into 'sophisticated' consumers and 'naïve' consumers. Sophisticated consumers are well informed about the availability, price and quality of available bank accounts. Sophisticated consumers also consider the cost of overdraft charges when choosing a bank. They are more diligent in controlling their finances and are less likely to go into overdraft when the effort of being diligent is relatively low. Naïve consumers do not investigate the cost of overdraft charges when selecting a bank account. Further, they are less diligent and are more likely to go into overdraft and incur overdraft charges.

The authors consider first, the case where the deals obtained by sophisticated and naïve consumers are linked. That is, the price that naïve consumers obtain is linked to that obtained by sophisticated consumers. The presence of a large number of sophisticated consumers may drive the price of bank accounts and contingent charges down. These lower prices are shared by naïve consumers. Armstrong and Vickers argue that, in this case, an additional sophisticated consumer confers a positive externality on all consumers. In contrast, naïve and sophisticated consumers end up with contrasting deals. For example, naïve consumers may pay higher contingent charges more often, allowing for the possibility that sophisticated consumers gain at the expense of naïve consumers.

The model suggests that where market outcomes for naïve consumers are linked to those of the sophisticated, then the naïve are protected by the sophisticated. The case for regulation of contingent charges is not strong in this scenario. Indeed, regulation may be counterproductive because it may diminish the incentive for consumers to become sophisticated. The authors conclude that the market works better for all consumers when there are more sophisticated consumers. In markets where the two types of consumers have contrasting outcomes, there is a redistribution from naïve consumers to sophisticated consumers. That is, sophisticated consumers benefit from the presence of the naïve because competition between firms causes profits from the naïve to be channelled to the sophisticated. Further, market efficiency may also suffer in these markets as the sophisticated undertake socially inefficient actions to avoid high contingent charges paid by the naïve. Armstrong and Vickers argue that a stronger case for consumer protection regulation of contingent charges emerges in these circumstances.

'Government Policy for a Partially Deregulated Industry: Deregulate it Fully', Clifford Winston, *American Economic Review: Papers and Proceedings,* 102(3), 2012, pp. 391-395.

Tracing the history of the significant deregulation program of Alfred Kahn, Clifford Winston argues that partial deregulation of markets has increased total welfare and that remaining inefficiencies can be overcome by full deregulation.

The article focuses on Kahn's influence in the aviation industry, pointing out that the 1978 Airline Deregulation Act led to lower fares for around 70 per cent of travellers. Winston then outlines some government interventions that were intended to retain social welfare in the face of the deregulation, such as subsidies for air services to small communities that may not have been economic in the deregulated environment, and argues that the interventions in fact had the opposite effect.

Winston also argues that the potential inefficiencies from full deregulation, such as predatory pricing, are negligible compared to existing inefficiencies that could be eliminated by further deregulation. These include a lack of competition at the infrastructure level (specifically airports), the use of dated contracting arrangements like 'exclusive gates' at airports that can only be used by one airline, an inefficient air-traffic control system, and landing fees that ignore congestion externalities.

In arguing for full deregulation, Winston suggests that opening the US airline market to foreign carriers would benefit consumers. He also argues that privatisation of airports and air-traffic control could be

welfare enhancing if handled correctly, though he acknowledges the complexity of maintaining competitive pressures in such infrastructure. Regarding air-traffic control, Winston suggests that the high-technology nature of the service is not suited to bureaucracy. He argues that deregulation may facilitate investment in technology and upgrading of equipment (e.g. planes' positioning and satellite systems) to allow for more automated air-traffic control that is both more efficient and safer than current human control.

Finally, Winston points out that Kahn's deregulation program had benefits in numerous other industries, from railroads to petroleum. Winston concludes that both cost efficiency and social welfare could be improved in these industries by further deregulation.

'Merchant and Regulated Transmission: Theory, Evidence and Policy', Stephen Littlechild, *Journal of Regulatory Economics*, published online 1 March, 2012.

This paper examines and compares the regulatory frameworks for transmission in Australia and Argentina. The first part of the paper focuses on evidence relating to alleged market failures and regulatory failure in Australia, where there have been both regulated and merchant interconnectors. To assess possible failures in Australian merchant interconnectors, the paper analysed five standard imperfections of market transmission: lumpiness of investment; market power; imperfect information; transaction costs; and other factors. Turning then to examine failures in Australian regulated interconnectors, the paper considered seven standard imperfections: imperfect information; bureaucratic processes; multiple regulatory jurisdictions; construction costs and conservatism in technology; interest group pressure; political influence; and regulatory resources and reliance on regulated firms. Littlechild finds that, in Australia, merchant transmission has generally not exhibited the standard examples of market failure, whereas regulated transmission has displayed the standard varieties of market failure.

The second part of the paper is concerned with the case of Argentina. A 'beneficiary pays' approach to transmission expansion is used in Argentina. This is not a simple merchant transmission, but rather exemplifies the new entrant-driven tariff-financed category of non-traditional transmission development. On this approach, beneficiaries are required to propose and approve major transmission expansion because of the observed weakness of transmission that has been regulated before. Contrary to initial impressions, the Argentine approach worked well – there were productive negotiations between transmission users that resulted in them commissioning desirable transmission expansions without undue transaction costs.

The Argentine experience with a 'beneficiary pays' approach is of particular significance today. The approach has recently been adopted by New York and by the FERC. In Argentina, costs fell significantly as a result of (i) giving control of the entire process to the beneficiaries who actually had to pay for the investment, and (ii) putting the project out to competitive tender, rather than leaving the decision with the incumbent state-owned transmission company. Experience in Argentina suggests that transactions costs are not a barrier to negotiations; and efficient investments can be determined by users.

Littlechild advocates that policy makers should seek to improve the regulatory framework and remove barriers to private initiatives. An important role for regulation is to facilitate coordination between potential providers and users of transmission lines. A central argument of the paper is that transmission investment projects and their costs and benefits are not known, either by regulators or by market participants. The paper concludes that a key task is to search for, discover and indeed, create, transmission investments that at least increase net benefits. To achieve this, it is necessary to discover or design the incentive-maximising and risk-sharing contractual arrangement most favourable to the successful coordination of such investment, while having due regard to the implications for competition and to the possibility of coordination across each region as a whole.

'Do Residential Customers Respond to Hourly Prices? Evidence from a Dynamic Pricing Experiment', Frank Wolak, *American Economic Review: Papers and Proceedings,* 2012, 101(3), pp. 83-87.

Many electricity businesses in the US have installed customer meters which are able to charge customers different prices for electricity at different points in time. The introduction of this technology gives rise to the question: what is the appropriate design for electricity tariffs which vary over time? Should the retail electricity tariff reflect hourly changes in the wholesale spot price for electricity? Wolak refers to such a tariff as 'hourly pricing' or HP. An alternative approach is for the electricity retailer to commit, usually 24 hours in advance, to a sustained period (four to six hours) of higher prices. This is known as Critical Peak Pricing or CPP. Customers are usually wary of critical peak pricing as it can result in significantly higher electricity bills. An alternative is to pay customers for reducing their consumption below a reference level during the critical peak period. This is referred to as Critical Peak Pricing with a Rebate, or CPR.

Wolak reports the results of an experiment which was carried out in Washington DC. The participants in the experiment were each randomly assigned to one of the three pricing plans (HP, CPP and CPR). A control group was also selected at random. None of the groups was told about the existence of the other pricing schemes. Both the CPP and CPR customers were subject to at most 12 CPP events during the summer and three CPP events during the winter. CPP and CPR customers were regularly notified whether or not the following day was a CPP day. HP participants were informed on a day-ahead basis when hourly prices were to be above 23 cents/kWh.

On average residential customers reduced their consumption by 9 per cent during a CPP and CPR event and 3 per cent following an HP warning. Wolak concludes that all three dynamic pricing programmes deliver stable, predictable, and sizeable demand reductions in response to CPP events and HP warnings. Under the CPP and CPR programmes, customer responses were similar to those that would have occurred under the equivalent HP regime. Wolak concludes that this is due to the fact that day-ahead hourly wholesale prices in US electricity markets are positively correlated: If they are high in one hour they are likely to be high in the next. The difference in practice between HP and CPP pricing is not large.

'Liberalization Models in the Electricity Sector: The Impact of the Market for Corporate Control in Britain and Spain (1996-2010)', Rocio Valdivielso del Real and Michel Goyer, *Competition and Regulation in Network Industries*, 13(1), pp. 71-100.

Despite its title, this paper is not really about electricity market liberalisation at all. It is primarily concerned with explaining the different experience with takeovers in the electricity industry in Britain and Spain over the past fifteen years. Following the liberalisation and privatisation of the electricity industry in Britain, almost all of the firms that emerged from that process were subsequently subject to takeover by foreign firms. Today the British electricity industry is almost entirely dominated by foreign firms. In contrast, in Spain, only one major firm – Endesa – has been acquired by a foreign rival.

The authors argue that these differences are due to institutional differences between the UK and Spain. The paper focuses on three institutional differences – differences in the concentration of ownership; differences in voting rights for minority shareholders; and differences in the independence of the authority overseeing foreign investment.

Regarding concentration of ownership, the central claim is that the privatisation process in the UK led to the creation of firms with diffuse ownership. The largest shareholders were too large to deter unwanted takeover bids. In contrast, concentration of ownership was much higher in some of the Spanish companies, but was low in Endesa once the Spanish Government abolished its golden share.

Regarding voting rights, privately-owned firms in the UK predominantly adopt a 'one-share-one-vote' policy. Prior to 1995, there existed a 'golden share' scheme which limited the size of the largest shareholder to 15 per cent of outstanding shares. This expired in 1995, after which there was a wave of successful takeovers. In contrast, the Spanish electricity industry is characterised by deviations from the one-share-one-vote principle, such as a limitation on the voting rights of any shareholder to 10 per cent of the capital of the company (at Endesa and Iberdrola).

Regarding independence of the regulatory authority, takeovers in the UK are administered by the 'Panel on Takeovers and Mergers', a self-regulated institution which focuses on maintaining shareholder value and protecting minority shareholders. In contrast, in Spain the sponsoring ministry monopolises the most important decision-making functions. The regulatory authorities in Spain have some independence but limited powers.

'Telecommunications Deregulation', Jerry Hausman and William Taylor, *American Economic Review: Papers & Proceedings*, 102(3), 2012, pp. 386-390.

This short paper by two veterans of the economics of telecommunications, Jerry Hausman and William Taylor, reviews the contributions of Alfred Kahn to telecommunications deregulation in the United States. Kahn, who died in 2010, was an economist at Cornell University, and became well-known as Chairman of the Civil Aeronautics Board, where he was active in promoting far-reaching airline deregulation in the US. Kahn published his *The Economics of Regulation* (in two volumes) in 1970. Hausman and Taylor describe this as 'magisterial'. The bibliography includes references to Alfred Kahn's numerous publications and affidavits on telecommunications economics and policy.

Hausman and Taylor begin by describing the state of the US telecommunications industry in the US in 1970, where there was a wireline monopoly that was 'pervasively regulated' and where wireless 'did not exist'. Regulation of long-distance telecommunications by the Federal Communications Commission (FCC) and for local and intra-state telecommunications by state public utility commissions was 'cost-plus, rate-of-return regulation'; justified by what Hausman and Taylor describe as 'presumed natural monopoly characteristics'. They then outline the main features

of the very different state of telecommunications after forty years, noting that:

> The path from then to now was tumultuous, driven by technological change ... and featuring a (regulatory induced) gold-rush-style entry and collapse of competitors, an industry-wide vertical divestiture largely offset by a subsequent merger wave, regulatory innovation (incentive regulation), industry restructuring (the 1996 Telecom Act) and regulatory initiatives (regulated pricing of network elements, network neutrality).

The body of the paper reviews Kahn's contributions to, and observations on, these changes. First, with respect to costs, Kahn had warned about what he saw as the futility of artificially allocating costs, and criticised the policies relating to the pricing of local service and of long-distance to which this had led. Kahn, in typically evocative prose, had likened the allocation approach by regulators, courts and the Department of Justice (DOJ) to searching for a black cat in a darkened room – except that there was no cat to be found. Hausman and Taylor claim that, if this basic point had been recognised earlier, 'the course of telecommunications history in the US would have been much different'.

Second, entry restrictions are seen as imposing 'enormous' costs – 'FCC and DOJ policies attempted to protect these [long-distance] companies from RBOC [regional Bell operating companies] competition in the mistaken belief that they would be viable local competitors, rather than the wireless or cable companies'.

Third, the path to deregulation (with a move from rate-of-return regulation to incentive regulation) was partially reversed after 1996, with what Kahn described as acts of 'astounding regulatory presumption'. This was primarily the introduction of total element long run incremental cost (TELRIC) to which Kahn attached the letters 'BS' for (of course) 'blank slate'. This was in reference to the assessment of the costs of the most efficient firm using the best technology. This was applied by the FCC to the unbundled network element platform (UNE-P) at what Hausman and Taylor regard as below-cost prices, 'spawning a gold rush-style entry in the late 1990s'. Following its overturning in 2004, cable and wireless competition increased – 'only after artificial competition was rolled back ... did facilities-based competition begin to replace regulation in residential telecommunications markets'.

The fourth and 'final chapter in Kahn's contribution to telecommunications deregulation' was 'his stand against reregulation of broadband access to the internet' – essentially his position as a 'voice of caution' on 'network neutrality'.

'Wholesale Provision of Broadband Services: Alternative Pricing Strategies and Associated Policies', Spyros Polykalas, George Prezerakos and Nikos Nikolinakos, *Info*, 14(3), 2012, pp. 16-34.

This paper explores the 'build or lease' dilemma that a new telecommunications operator faces when it intends to enter a liberalised telecommunications service market. In particular, the paper examines the dilemma that arises where the local loop network previously installed by the incumbent is accessible under a full or partial unbundling arrangement.

The local loop refers to the access network connection between the customers' premises and the operator's local exchange, usually a loop comprised of two copper wires. Unbundled access to the local loop allows access seekers to rent the local loop from the access provider under full local loop unbundling (LLU) and/or shared access. New entrants to the telecommunications market often need to make a 'build or lease' decision – that is, a decision whether to invest in new network infrastructure or to rent the access network via LLU.

The paper first considers whether LLU is really necessary for promoting broadband. The authors argue that LLU can indeed be considered as a useful instrument during the initial stages of broadband development. This appears to be consistent with the 'ladder of investment' theory and it is also supported empirically by the regulatory experience in the US – at least up to the early 2000s – and in the European Union. In a small number of developed countries that have introduced alternative technologies, however, LLU no longer plays a significant role in the promotion of broadband services.

Having reviewed the development of the Greek telecommunications market, the authors conclude that, in the absence of alternative technologies, LLU has contributed to the rise in the penetration of broadband services in Greece. Using data from the Greek market, the paper presents a cost model that determines the wholesale costs of providing broadband services through LLU and/or Wholesale Broadband Access (WBA). The key parameters modelled include access type, co-location type, bandwidth and capacity of the backhaul link. The analysis shows that there are several factors that should be examined when new entrants design their broadband deployment strategy. For example, the fall in wholesale unit costs associated with higher numbers of customers suggests that LLU becomes attractive as an operator establishes its market presence.

The authors judge that the cost model developed can be used to guide an operator in the design of a successful broadband strategy based on LLU and

WBA. The authors also discuss a range of policy and regulatory issue relating to the promotion of broadband deployment.

'How Holistic Should Economic Measurement Be? A Cautionary Note on Valuing Ecosystem Services as Part of the Murray-Darling Basin Plan', Lin Crase, *Economic Papers*, 31, 2, June 2012, pp. 182-191.

The Murray-Darling Basin Authority supports research on valuing ecosystem services in the Murray-Darling Basin. In this article, Lin Crase examines the challenges posed by the valuation exercise and attempts to predict how the results might be used by the Authority. Following an introduction, there are sections on the history of the Murray-Darling Basin Plan; holistic measurement and water policy decisions; framing winners and losers; lessons for ecosystem valuation and concluding remarks. Apart from names of bodies or authors, two initialisations are used in the paper – BCA (benefit cost analysis) and SDL (sustainable diversion limit).

Following the useful background section on the history of the Murray-Darling Basin Plan, the author moves on to a discussion of the relationship between 'holistic measurement and water policy decisions'. This section sets out some elements of BCA considered by the author to be important in this context. First, Crase highlights the difficulties involved in using techniques, such as the travel-cost method and the creation of a hypothetical market, to determine benefits where there are no market prices to draw on. The author contends that it is 'unclear that ... policy makers are cognisant of the limitations that attend the results' (p. 186). He then considers the approach to discounting future costs and benefits. This is followed by a discussion of the validity of including the direct employment effects in the BCA; without including the broader effects (including on employment) of using taxpayer dollars. Next, Crase turns to the sometimes 'troublesome' decision rule in BCA, which he discusses in relation to the benefit-cost ratio. (The NPV rule – the absolute difference between benefits and costs – is another decision rule used in BCA.) Finally, the more limited exercise of conducting a cost-effectiveness analysis is considered, as a means of avoiding the need to estimate environmental benefits.

The next section is titled 'framing winners and losers' where Crase questions the focus on one outcome – SDLs – where there are multiple objectives (economic, social and environmental). Reference is made to Jan Tinbergen's rule of requiring a separate instrument for each target. The author then revisits aspects of his BCA discussion from the previous section of his paper; particularly in relation to the inclusion of both the positive employment impacts in the basin and the negative impacts on employment more broadly as a consequence of 'extraordinary taxation on the wider citizenry' (p. 188).

The final section considers 'lessons for ecosystem valuation in the Murray-Darling Basin'. One of the points made in this section is that 'developing an estimate of ecosystem services runs the risk of providing yet another distraction from ... basic policy prescriptions' (p. 189). Crase also rehearses two earlier points – that about the desirability of considering the welfare of 'the Australian community at large' and that which argues that the estimation methods for environmental benefits are contested and 'contentious'. The overall conclusion of the paper is that 'there are grounds for being somewhat sceptical about the usefulness and purpose of research work that will measure the economic benefits of ecosystem services in the Murray-Darling Basin' (p. 190). Lin Crase is concerned that 'the scope of any BCA will be manipulated to favour high-cost delivery of the Basin Plan' (p. 190).

'Equity Risk Premium Myths', Robert Arnott, in *Rethinking the Equity Risk Premium*, Research Foundation of CFA Institute, 2011, pp. 71-100.

According to Arnott, it is often the case that many fundamental assumptions in finance theory fail when tested empirically. The upshot is that financial analysts should be more willing to explore the implications that these assumptions are erroneous. Arnott examines seven 'myths' related to the equity risk premium (ERP) and systematically refutes each. For the purposes of this analysis, the ERP is defined as the expected (forward-looking) long-term difference between stock returns and bond market expected returns.

First, Arnott examines the assumption that the ERP is equal to five per cent and that this value does not change significantly over time, except in response to a stock's beta value. Arnott contends finance theory does not support this assumption. Past returns across different time periods are examined, including from 1802 to 2010. They generally reflect a lower ERP.

The second 'myth' is that the ERP is static over time, across markets, and across companies. Again, Arnott argues that nothing in neoclassical finance theory suggests that the ERP must be static. Behavioural finance observers, for example, contradict the notion of a static ERP because risk, risk expectations, and risk tolerance are all non-static. As Arnott states, 'Uncertainty is always with us … If you want God to laugh, tell him your plans'.

The third 'myth' is the 'ERP Puzzle'. This suggests that the returns from stocks have exceeded the return on bonds by more than can be explained by finance theory. Arnott explains that the ERP Puzzle attempts to explain excess ERP returns of five per cent.

However, a five per cent return has not been earned in 'normal' markets. Rather, an excess return of two or three per cent is more generally observed.

The fourth myth is that the returns from stocks will be greater than the returns from bonds in the long term. The long term is considered to be 20 to 30 years, or longer. Arnott observes that, during a 41- year span from 1968 to 2009, returns of ordinary long US treasury-bonds were actually greater than the returns from the S&P 500 Index. Further, Arnott claims that many non-US examples also disprove this myth.

The fifth myth is that when stock yields and payout ratios are low, buybacks provide stock growth opportunities for shareholders. Arnott examines historical data that suggest that 'true buy-backs' are unusual, regardless of stock yields and payout ratios. 'True buy-backs' are defined as buybacks that reduce outstanding shares, rather than buybacks that merely recapture shares that were issued in a context of management stock option redemption.

The sixth myth refuted by Arnott is that stock market earnings grow with GDP. Arnott suggests that, if this myth were true, the expected return on stocks would match the yield plus expected GDP growth. However, this ignores the fact that the share of corporate profits in GDP growth consists of the growth in existing enterprises plus the creation of new enterprises. The problem is that the ERP is generally smaller than adherents to this misconception expect.

'An Examination of Potential Changes in Ratio Measurements: Historical Cost versus Fair Value Measurement in Valuing Tangible Operational Assets', Pamela Smith Baker, *Journal of Accounting and Finance*, 11(2), 2011, pp. 170-176.

The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) have been working on a project to limit the differences between the 'generally accepted accounting principles' (GAAP) in the United States and the 'international financial reporting standards' (IFRS). One point of difference is that the GAAP only permits historical-cost methodologies for valuing fixed assets, whereas the IFRS permits either historical-cost or current fair-value approaches. The latter enables the firm to revalue its assets over time. Advocates of the fair value approach argue that this methodology presents a more relevant and contemporary valuation of the firm. However, Smith Baker argues that there are important shortcomings with the fair value approach – namely, that values that are not based on actual market prices have the potential to be manipulated. Manipulation of asset values may increase business risk and uncertainty.

Smith Baker compares the historical-cost approach to the fair-value approach for a set of fixed assets. The comparison reveals the extent of the divergence between fair-value and historical-cost measures and its implications for the reporting of profitability, asset utilisation and debt utilisation. Smith Baker randomly selected properties in Denton County, Texas, for the years ending 2004 to 2008. She removed from the sample all properties that are exclusively land, that are under property tax protests, and that have improvements. After these exclusions, the sample consisted of 30 properties.

Two corresponding outcomes are observed for the two independent variables, fair value and historical cost. The historical cost is determined using the sales price for which the property was sold. The allocation of value to land and buildings is based on the basket purchase method (where the fair value of each asset is estimated at the time of the purchase, and the sum of the fair values is equal to the sale price). Buildings have an assumed 27.5 year useful life and are depreciated using a straight-line method. For the fair value method, buildings and land are originally valued at historical cost. However, each year the assets are re-valued. The buildings have an assumed 27.5 year life and are depreciated using a straight-line method.

Analysis conducted by Smith Baker revealed significant differences on the financial statements. Depreciation expense is 44 per cent higher under the fair-value method since fixed investment properties receive a 38 per cent higher valuation *vis a vis* the historical-cost method. As a result of the lower depreciation expense that is incurred using the historical-cost method, net income is 57 per cent higher using this method. Assets appear to be better utilised under the historical-cost method since, for a given turnover, the assets receive a lower (historical) value. While assets and shareholders' equity are higher under the fair-value method, the profitability ratio is higher under the historical-cost method (where the latter will raise the market value of equity). Under the fair-value method, debt utilisation is more favourable since revaluation of the assets under fair value reduces the amount of debt per dollar of equity.

The author concludes that historical cost provides more favourable measures of profitability and asset utilisation since net income is higher as a proportion of the asset values. However, fair-value measures present more favourable debt utilisation ratios since, for a given level of debt, asset values are higher.

'The Debt Maturity Issue in Access Pricing', Kevin Davis, Australian Centre for Financial Studies, *ACFS Publications*, 2 September, 2012.

This paper is concerned with methodologies for estimating the cost of debt when setting regulatory prices. In particular, Davis addresses the question of whether the term of debt should be benchmarked at the length of the regulatory period or whether, instead, the benchmark term should be longer (perhaps corresponding to the asset's expected life). The paper argues that, for the purpose of access pricing, the term should correspond to the regulatory period. The argument is based on the following two premises. First, the regulated businesses' expected cash flows should be set in such a way that, after making allowance for required debt repayments, the expected return to equity should equal its required return. Second, the expected cost of debt should be the minimum amount required by the access provider without increasing its risk over and above that allowed for in the regulatory determination. The paper argues that the two conditions are only met when the regulator uses a five-year term of debt assumption.

The intuition for Davis's argument can be explained by noting the similarity between the determination of allowable cash flows on an access asset and cash flows on a floating rate bond. The main difference between the two streams of cash flows is that those of a regulated asset are reset at regular dates by the regulator in line with movements in both risk-free interest rates and the credit spread facing the borrower. Davis observes that, by issuing debt with a term equal to the term of the regulatory period, the borrower will have financed and perfectly hedged the cash flows in the regulatory period. Moreover, in the next regulatory period, the borrower will also be able to hedge and finance its cash flows. Davis relies on an example that makes several simplifying assumptions, including the assumption that the useful life of the regulated asset is equal to two periods (each of which is one year).

Davis concludes his paper by noting that there are two feasible options for the regulator when estimating the regulated businesses' cost of debt. One option is for the regulator to continue to use a regulatory period that is less than the maturity of the regulated asset, in which case the term of debt used should equal the length of the regulatory period. The second option is for the regulator to use a regulatory period that is equal to the maturity of the regulated asset. In this case, the term of debt would be set equal to the asset life; and the cost of debt would not be updated over the life of the regulated asset.

'Regulated Prices and Real Options', Graeme Guthrie, *Telecommunications Policy,* 36, 2012, pp. 650–663.

This paper argues that investment payoffs for a firm in a workably competitive market are a function of not only the rate of return but also the reduction in the real value of the firm's growth options whenever it invests. The reduction in the real option value can inform a regulator's estimation of the real option value when regulated firms commit to investment. In other words, the regulator allows the regulated firm a rate of return equal to its weighted average cost of capital (applied to the regulated asset base) plus a multiplier that represents the value of the exercised growth option. The multiplier approach works by increasing each item of capital expenditure by a fixed percentage at the time when it is added to the regulatory asset base.

Guthrie presents four possible approaches that regulators can use to estimate the value of the real option of capital expenditure undertaken by regulated firms. Each approach is based on an established real options model, and the value of the real option is estimated from observed investment behaviour in a workably competitive market. (Note, however, that the author does not define 'workable competition'). The first approach relates to the standard model of the option to delay capital expenditure until the investment environment improves. In a workably competitive market, the market value of the completed project and the required amount of capital expenditure evolve randomly over time, and investment is irreversible. The value of the option to delay investment before pre-emption by competitors in a workably competitive market can be estimated as the regulated firm's option value for any capital expenditure project.

The second approach is based on a real option model in which managers have the additional flexibility of suspending production in the future if economic conditions deteriorate. While making the investment destroys the value of waiting, it also creates an option value to suspend production without cost once the capital expenditure has taken place. Guthrie argues that this option value – applied to the regulated firms' capital expenditure projects – can be estimated by regulators.

The third approach is grounded in a model in which the option gains value when multiple rounds of investment are possible. In this model, investment creates an option to carry out further investment. The value of the real option is equal to the value of the options destroyed by investment minus the value of the options it creates. This net option value can be estimated by the regulator.

The fourth approach relates to the case in which managers choose the timing of investment, recognising that investment in new assets affects the market value of existing assets. In contrast to the other approaches, according to this model, new capital expenditure causes the firm's older assets to become stranded.

Guthrie concludes that estimating real option values is challenging for regulators as the data required are not available in regulated industries. Guthrie argues that, nevertheless, real option values can be estimated from observations of the dynamics of a workably competitive market, such as estimating how long a firm would delay an investment before being pre-empted by competitors.

Regulatory Decisions in Australia and New Zealand

Australia

Australian Competition and Consumer Commission (ACCC)

ACCC Issues Guide on Dispute Resolution between Australia Post and Bulk Mail Users

On 14 December 2012 the ACCC issued a guide on the resolution of disputes that may arise between Australia Post and bulk mail users. The guide is available here.

ACCC Issues 2012 Petrol Report

On 6 December 2012, the ACCC released its 2012 report on the prices, costs and profits of unleaded petrol in Australia. The petrol report is available here.

PC Inquiry into the National Access Regime

On 30 November 2012, the Productivity Commission (PC) released an Issues Paper on its inquiry into the National Access Regime (Part IIIA of the Competition and Consumer Act 2010 (Cth) and clause 6 of the Competition Principles Agreement), and the operation and terms of the Competition and Infrastructure Reform Agreement. The issues the PC has been asked to examine include: the rationale, role and objectives of the National Access Regime (the Regime), and Australia's overall framework of access regulation; the performance of the Regime in meeting its rationale and objectives; and whether the implementation of the Regime adequately ensures that its economic efficiency objectives are met. The PC has also been asked to provide advice on ways to improve processes and decisions for facilitating third-party access to essential infrastructure. Initial submissions are due by 8 February 2013. **Read more**

ACCC Allows GrainCorp to Introduce Long-term Port Access Agreements

On 30 November 2012 the ACCC announced it would not object to GrainCorp Operations Limited's proposal to offer long-term agreements (LTAs) to users of its bulk grain export facilities on the East Coast of Australia. GrainCorp will allocate up to 60 per cent of its port capacity through LTAs to exporters who commit to minimum export volumes over a three-year period. At least 40 per cent of capacity per port, per month will remain available to all exporters. GrainCorp intends to invite nominations for long-term capacity in February 2013. The ACCC oversees port access arrangements for wheat exporters. Access undertakings are intended to ensure that third-party exporters of bulk wheat are able to access ports operated by vertically integrated port terminal operators. **Read more**

ACCC Begins Consultation on New Telstra Measures Developed Under the Migration Plan

On 22 November 2012 the ACCC released a discussion paper inviting comment on four measures developed by Telstra under its migration plan. The measures are intended to provide appropriate protections to consumers and competition during the migration from Telstra's copper and HFC networks to the NBN. Telstra was required to develop these measures and seek the ACCC's approval as it did not have fully effective processes in place at the time of lodgement of the migration plan. Submissions were required by 14 December 2012. **Read more**

ACCC Commences First Public Consultation on NBN Co Special Access Undertaking

On 12 November 2012 the ACCC released the first consultation paper on the Special Access Undertaking (SAU) lodged by NBN Co on 28 September 2012. If accepted by the ACCC, the SAU will be a key part of the framework that governs the price and other terms upon which NBN Co will supply services over its fibre, wireless and satellite networks to telecommunications companies. It will also build upon the role for the ACCC in resolving disputes between NBN Co and its customers. The ACCC re-iterates that it expects parties to agree to short-term arrangements for the continuing supply of NBN Co's services until assessment of the undertaking concludes and the regulatory framework is established. The ACCC hosted a stakeholder forum on the SAU in December 2012. Submissions on the consultation paper are required by 11 January 2013. A draft decision on the SAU is expected in March 2013. **Read more**

Competition to Provide the Next Wave of Reform in Australian Stevedoring

On 1 November 2012 the ACCC released the 14th annual container stevedoring monitoring report. The ACCC has monitored stevedoring services at six Australian container ports since 1999. Persistently high returns (23 per cent on average over the last decade) have previously led the ACCC to question the intensity of competition in the industry. The addition of capacity at most ports and the entry of a new stevedore, Hutchison Port Holdings, in Brisbane and Sydney next year are both important

developments for promoting heightened competition. Read more

ACCC Approves Transition to More Efficient Trains for the Hunter Valley Coal Chain

On 17 October 2012 the ACCC agreed to arrangements for transitioning to more efficient train services proposed by the Australian Rail Track Corporation (ARTC) for its rail network in the Hunter Valley. ARTC's proposal involved varying the arrangements in its Hunter Valley Access Undertaking (HVAU), which was approved by the ACCC on 29 June 2011. The ACCC has a role in monitoring ARTC's compliance with the requirements in the HVAU, in addition to assessing any proposed variations. **Read more**

ACCC Makes Final Access Determination for Non-NBN Local Bitstream Access Service

On 5 October 2012 the ACCC announced that it has made a final access determination for the declared local bitstream access service (LBAS). This will apply for three years and expire on 5 October 2015. The LBAS is a wholesale access service for fixed-line networks that are built or upgraded after January 2011. The LBAS is a 'last mile' fixed-line service provided to residences and small business where the download transmission rate is superfast (25 megabits per second (Mbps) or faster). It does not apply to the NBN or to wireless or satellite networks. **Read more**

Australian Competition Tribunal (ACT)

Nil.

Australian Energy Market Commission (AEMC)

Review of Competition in New South Wales Retail Electricity and Natural Gas Markets

On 13 December 2012 the AEMC called for public submissions on the issues paper which launches the consultation process for its review of competition in New South Wales retail electricity and natural gas markets. Submissions are to be received no later than 8 February 2013. **Read more**

Consultation Paper on Pipeline Operator Cost Recovery Processes Published

On 6 December 2012 the AEMC announced commencement of consultation on a rule change request submitted by the AER. The proposed rule change seeks to improve the efficiency and operation of the process for the recovery of costs incurred by pipeline operators in relation to the market operator service allocation service and natural gas market bulletin board aggregation and information service. Submissions are due by 24 January 2013. The AEMC has published a notice under s. 317 of the National Gas Law to extend the period of time for making the draft rule determination. **Read more**

AEMC Proposes New Opportunities for Consumers to Manage their Electricity Use and Expenditure

On 30 November 2012 the AEMC announced that reforms to the National Electricity Market (NEM) have been recommended to Commonwealth and state governments by the AEMC in its final report of the Power of Choice Review. This is intended to provide consumers options in the way they use electricity. The recommendations include changes to the National Electricity Rules (NER), the National Energy Retail Rules and several government programs to provide the information, technology and price options. The final report and a detailed implementation plan, were considered by the Standing Council on Energy and Resources (SCER) on 14 December 2012.

Draft Report on Review of Arrangements for Compensation Following an Administered Price, Market Price Cap or Market Floor Price

On 29 November 2012, the AEMC published a draft report for the review of compensation arrangements following an administered price, market price cap or market floor price. To date, only one claim for compensation has been made in the NEM, however, it is important that transparent compensation frameworks can help ensure efficient outcomes for consumers. Submissions regarding the draft report are required by 24 January 2013. **Read more**

Final Determination Made on Small Generation Aggregator Framework

On 29 November 2012, the AEMC published the Small Generation Aggregator Framework final determination and final rule. The rule as made seeks to lessen potential barriers to fully participating in the market faced by small generators. **Read more**

Final Determination on Network Regulation Rule Changes

On 29 November 2012 the AEMC published its final determination and final rules on the regulation of electricity and gas network prices. The new rules, that take effect immediately, give the regulator additional tools to set maximum prices which network businesses can charge. The rules are aimed at improving the capacity of the regulator to determine network price increases so consumers do not pay more than necessary for reliable supplies of electricity and gas. **Read more**

Proposed National Blueprint for Electricity Reliability Targets

On 28 November 2012 the AEMC called for public submissions on its draft report proposing the introduction of a national framework for state and territory governments to set efficient reliability targets for distribution networks. Jurisdictional governments retain responsibility for setting reliability standards under the AEMC's framework. Feedback is required by 25 January 2013. **Read more**

Draft Report Published on Energy Adequacy Assessment Projection (EAAP) Review

On 15 November 2012, the AEMC's Reliability Panel published its draft report on the EAAP review. The findings are to maintain the existing provisions for the EAAP under the National Electricity Rules, including maintaining the existing current three-monthly reporting requirement for the EAAP. Submissions on the draft report were required by 21 December 2012. **Read more**

New Rules for Networks

On 15 November 2012, the AEMC published its final position on new rules to regulate electricity network prices. The final rules and implementation arrangements took effect on 29 November 2012, and give the regulator new tools to set maximum prices which network businesses can charge. In addition, the AEMC is working across the electricity and gas supply chains to identify other areas where changes can be made to improve the efficiency of the total system. **Read more**

Electricity Market Financial Resilience

On 9 November 2012, the AEMC called for public comment on options for mitigating the financial risks that could be caused by the failure of a large electricity retailer. Submissions were required by 20 December 2012. **Read more**

Final Determination Made on Reference Service and Rebateable Service Definitions

On 1 November 2012, the AEMC announced a new rule to give the Australian Energy Regulatory (AER) and the Economic Regulatory Authority of Western Australia (ERA) more flexibility when regulating efficiency prices for natural gas pipeline services. The rule will apply from 2 May 2013. **Read more**

Final Determination Made on Optimisation of Regulatory Asset Base and Use of Fully Depreciated Assets

On 13 September 2012, the AEMC published a final rule determination in respect of the Major Energy Users Inc's (MEU) rule-change requests on the optimisation of the regulatory asset base and the continued use of fully depreciated assets that are still useful. The AEMC decided not to make a rule in response to the MEU's requests. **Read more**

Australian Energy Regulator (AER)

AER Decision on Victorian Electricity Distribution Pricing Proposals 2013

On 19 December 2012 the AER announced that it has approved increases in Victorian electricity network tariffs for the period 1 January 2013 to 31 December 2013 for the distribution network service providers (DNSPs), CitiPower, Powercor, SP AusNet, Jemena Electricity and United Energy. Network tariffs recover the costs associated with transporting electricity along the low and high voltage power lines, and typically make up between 30-40 per cent of total residential electricity bills in Victoria. The AER expected network charges for the average residential customer to increase by 16 per cent in 2013. **Read more**

AER – Better Regulation

On 18 December 2012, the AER Chairman, Andrew Reeves, announced the start of consultation on *Better Regulation*, a program of work that will deliver improved regulation of network businesses focused upon the long term interests of consumers. This follows changes to the National Energy Rules announced by the AEMC at the end of November 2012. **Read more**.

AER Approves 2011 Demand Management Incentive Scheme Expenditure for Victorian DNSPs

On 5 December 2012 the AER published a final decision for expenditures in 2011 by: CitiPower (VIC); Jemena Electricity Networks (VIC); and SP AusNet (VIC). The DNSPs sought approval of total expenditures of around $550,000 relating to three projects. **Read more**

AER Releases Draft Decision for AMI Remote Services

On 24 November 2012 the AER released a draft decision on proposed charges and terms and conditions for Advanced Metering Infrastructure (AMI) remote services in Victoria. AMI remote services are metering services that were previously provided through a field officer visit, but can now be offered remotely using AMI or smart-meter technology. These services are provided on a fee-for-service basis where requested by a customer who has a smart-meter installed. Submissions are required by 22 December 2012. **Read more**

AER Cost Thresholds Review for the Regulatory Investment Test for Transmission Final Determination

On 20 November 2012 the AER published a final determination on the cost thresholds associated with the Regulatory Investment Test for Transmission (RIT-T). Its final determination is that: the $5 million cost thresholds, in relation to the definition of replacement transmission network asset and in relation to transmission investment, be maintained at $5 million; and the $35 million cost threshold in clause 5.6.6(y) be increased to $38 million (from 1 January 2013). The RIT-T is a cost-benefit test that transmission companies must apply before building electricity transmission infrastructure where the costs of proposed investments are above certain thresholds. **Read more**

AER Releases Issues Paper on Short-Term Trading Market

On 8 November 2012 the AER released an issues paper on reporting triggers for significant price variations in the gas Short Term Trading Market. Under Rule 498 of the National Gas Rules, the AER is required to develop and publish guidelines as to what constitutes a significant price variation for reporting purposes. Submissions closed on 30 November 2012. **Read more**

AER Varies Victorian Electricity Network Charges Following Tribunal Decision

On 2 October 2012 the AER announced it has remade its Victorian electricity distribution determinations in accordance with decisions by the Australian Competition Tribunal. These affect the network charges that can be levied by the five Victorian distribution network businesses, Citipower, Powercor, SP AusNet, Jemena Electricity and United Energy. The remade determinations will have the effect of increasing network charges in the remaining years of the current regulatory period, between 2013 and 2015. The remade determinations have also been affected by new Victorian legislation. The consequent increase in network charges across all the distribution businesses is estimated to be around 2.6 per cent for the average residential bill in 2013. **Read more**

AER Issues Draft on Two Victorian Gas Pipelines

On 24 September 2012 the AER released a draft decision on Multinet and Envestra's access arrangements, including charges for use of their gas distribution networks for the 2013-17 period. Envestra and Multinet are able to respond to the AER's draft decision by submitting revised regulatory proposals. Other stakeholders also have the opportunity to provide submissions in response to the AER's draft decision. Draft decisions for APA GasNet and SP AusNet were released on 11 September 2012. The AER will make a final decision on Envestra and Multinet's regulatory proposals in March 2013. **Read more**

National Competition Council (NCC)

Application for Coverage of the South Eastern Pipeline System

On 28 November 2012, the NCC received an application under the National Gas Law from Kimberly-Clark Australia Pty Limited for coverage of the South Eastern Pipeline System. The submission period on the application will commence on 8 January 2013 and close on 29 January 2013. **Read more**

Australian Capital Territory

Independent Competition and Regulatory Commission (ICRC)

Submissions Received on Possible Price Outcomes – Regulated Water and Sewerage Services 2013-18

On 22 October 2012, the ICRC announced receipt of submissions in response to the release of its community consultation paper. The paper addressed possible water price outcomes that could result from some of the propositions in ACTEW Water's submission on water and sewerage services. **Read more**

New South Wales

Independent Pricing and Regulatory Tribunal (IPART)

Review of Rental Arrangements for Communication Towers on Crown Land

On 12 December 2012 the IPART released an Issues Paper for the review of rental arrangements for communication towers on Crown land. The paper sets out the approach being taken for the review. The IPART seeks comments on the current fee schedule, including definitions of user and location categories, and market rentals for sites, as well as information on sites where rentals could be subject to a negotiation process, rather than set out in the fee schedule. Submissions are required by 12 February 2013. **Read more**

Gas Issues Paper

On 27 November 2012 the IPART released an issues paper on proposed regulated retail gas prices in New South Wales for the next three years, together with pricing proposals from each of the Standard Retailers. Standard Retailers have proposed average price increases from 3.5 per cent to 10.4 per cent for 2013-14. They are also seeking to set the prices for 2014-15 and 2015-16 closer to the time, when more information about wholesale gas costs and carbon costs is available. The issues paper details IPART's proposed approach to assessing these proposals, and identifies issues on which it seeks stakeholder comment. Submissions are due on 21 January 2013. **Read more**

Electricity Issues Paper

On 14 November 2012 the IPART released an issues paper for the 2013-16 review of regulated retail electricity prices. The issues paper seeks industry and community feedback about IPART's proposed approach to the review including determining average price changes and identifying how the determination can help to support the long-term interests of customers. Around half of all New South Wales residential and small business consumers are now on market contracts, so while the focus remains on setting regulated electricity prices, the review will also look at what measures are needed to further improve consumer confidence and promote participation in the competitive retail market. Submissions are required by 20 December 2012. **Read more**

Northern Territory

Utilities Commission

New Pricing Orders

On 19 December 2012 the Utilities Commission (the Commission) announced that the Regulatory Minister has issued new pricing orders, which come into effect 1 January 2013. The Commission is required to monitor and enforce compliance with the pricing orders. **Read more**

2014 Network Price Determination

On 3 December 2012, following consideration of submissions received and its own further analysis, the Commission released its Final Decision for the 2014 Network Price Decision Framework and Approach, which sets out the Commission's final decision on the form of control mechanism that will apply to standard control services during the 2014-19 regulatory control period. Its view is that generally accepted regulatory practice for electricity networks price determinations is the process undertaken by the Australian Energy Regulatory (AER) in accordance with the National Electricity Rules (NER), and that working towards alignment with such national arrangements is in the long term interest of Territory electricity consumers. **Read more**

Electricity Retail Supply Code Draft Decision

On 16 November 2012 the Commission released its draft decision to amend the Electricity Retail Supply Code in accordance with the Draft Decision Paper. The draft decision follows public consultation on QEnergy's proposed amendments and the Commission's 28 September 2012 Options Paper. Submissions on the Draft Decision Paper, Revised Retail Supply Code (with proposed amendments) and proposed Credit Support Guidelines were required by 30 November 2012. **Read more**

Review of Power and Water Corporation

On 9 November 2012 the Commission reported that the Northern Territory Government has engaged NERA/Marchment Hill to conduct a comprehensive review of Power and Water Corporation (PWC). While the Commission does not have a formal role in the review it has been invited to discuss specific aspects with the consultants including issues associated with the Territory's regulatory framework and the structure and governance of the Corporation. The review by NERA/Marchment Hill will consider the Commission's previous Priority Work Program reviews and will seek further input from the Commission on the review findings and recommendations. The NT Access Code requires the Commission, in consultation with interested

parties, to review the network price regulation methodology every five years. The next regulatory control period commences 1 July 2014. The Commission released a consultation paper in June 2012, setting out its preliminary position on the Framework and Approach for the 2014 Network Price Determination. **Read more**

Queensland

Queensland Competition Authority (QCA)

Rail: Proposed Standard Rail Connection Agreement (SCRA) Not Approved

On 14 December 2012 the QCA announced that it had decided not to approve Aurizon Network's proposal. The QCA's decision document outlines its reasons and the ways the SCRA should be amended for it to be approved. The QCA requires Aurizon Network to amend its SRCA in the way described in its final decision and resubmit it to the QCA no later than 8 February 2013. Read more

Review of Solar Feed-in Tariff for Queensland – Draft Report

On 27 November, the QCA released its Draft Report on estimating a fair and reasonable solar feed-in tariff for Queensland. The Draft Report provides the QCA's preliminary advice to the Minister for Energy and Water Supply to inform the Queensland Government's review of the Solar Bonus Scheme, which it will undertake by 30 June 2013.

Regulated Retail Electricity Price 2013-14 – Consultation on Transitional Issues

On 2 November 2012 the QCA released a Consultation Paper inviting submissions on a range of transitional issues. Legislative changes in late 2011 changed the way the QCA is required to determine regulated prices, starting with its determination of regulated prices for 2012-13. Instead of escalating all existing retail tariffs (most of which were introduced over 20 years ago) by the same percentage each year, as it had previously been required to do, the QCA was required to establish a new set of retail tariffs which better reflected the costs of supply. Submissions in response to the Consultation Paper are required by 7 January 2013. **Read more**

Rail: Proposed Standard Access Agreements

On 13 November 2012 the QCA announced receipt of eight submissions in relation to its draft decision not to approve QR Network's proposed standard access agreements. **Read more**

Report on a Framework for Reducing the Burden of Regulation

In late October 2012 the QCA released an Interim Report on measuring and reducing the burden of regulation. A final report is scheduled for 31 January 2013. **Read more**

South Australia

Essential Services Commission of South Australia (ESCOSA)

The ESCOSA Suspends Wholesale Electricity Costs Review

On 18 December 2012, the South Australian Government announced a policy change regarding price regulation of retail energy prices. In light of this announcement, the ESCOSA has suspended its wholesale electricity cost (WEC) review. **Read more**

The ESCOSA Approves First Water Licences – Media Release

On 29 November 2012 the ESCOSA approved the first water licences to be issued under the new Water Industry Act. Under the Act, retailers who currently provide water and/or sewerage services to end-use customers will need to obtain a licence by 1 January 2013. The licensing system will ensure, for the first time, all water and sewerage customers benefit from consumer protection measures. **Read more**

Determination of SA Water's Drinking Water and Sewerage Revenue 2013-14 – 2015-16

On 12 October 2012, the ESCOSA released for public consultation SA Water's Regulatory Business Proposal for Drinking Water and Sewerage Revenue 2013-14 – 2015-16, and an associated Issues Paper prepared by the ESCOSA. The consultation period closed on 9 November 2012. **Read more**

Water Consumer Protection Framework

On 16 November 2012 the ESCOSA released its final Water Retail Code – Major Retailers, to apply to SA Water from 1 January 2013. This follows an extensive public consultation process over the past two years to develop the water consumer protection framework. While SA Water is currently the only major retailer operating in South Australia, the Water Retail Code – Major Retailers is also intended to apply to future retailers that enter the market to compete for mass market customers. The ESCOSA will be consulting on a draft Water Retail Code to apply to other water retailers in December 2012. The ESCOSA is also undertaking consultation on the draft performance reporting guideline (Water Industry Guideline No. 2) to apply to SA Water. The final

Guideline is to be released by the end of December 2012. **Read more**

Regulatory Arrangements for Reticulated LPG Networks

On 22 October 2012 the ESCOSA released for comment a Further Draft Decision concerning the Regulatory Arrangements for Reticulated LPG Networks. The Government decided that LPG will continue to be regulated by the ESCOSA under the Gas Act. Feedback was required by 30 November 2012. The ESCOSA aims to release its Final Decision in early 2013. **Read more**

Electricity Standing Contract Price – Wholesale Electricity Costs – Submissions Received

On 16 November 2012 the ESCOSA announced receipt of submissions in response to its Draft Determination of the wholesale cost component of electricity standing contract prices. In 22 October 2012, the ESCOSA released requested Wholesale Electricity Cost Modelling Data developed by Frontier Economics Pty Ltd. On 2 October 2012, the ESCOSA had released for public consultation its Draft Determination to change the wholesale cost component of electricity standing contract prices. On 19 October 2012 the ESCOSA extended the period for consultation on its wholesale electricity cost review. The ESCOSA sets and regulates retail prices for the 25 per cent of small customers (residential and business customers using less than 160 megawatt hours per annum) who have a 'standing contract' offered by AGL SA. The other 75 per cent of customers have elected to sign 'market contracts' with their retail provider, which are not price regulated. Feedback was required by 26 October 2012. The ESCOSA will make a Final Determination in early December and the change in the standing contract price (if any) will apply from 1 January 2013. **Read more**

Review of SA Water's Regulatory Business Proposal (RBP) 2013 to 2016 – Issues Paper

On 12 October 2012 the ESCOSA released SA Water's RBP and an Issues Paper for public consultation. The ESCOSA will make its first revenue determination for SA Water in May 2013, setting maximum allowed revenues for drinking water and sewerage retail services for the three year period from 1 July 2013 to 30 June 2016. Submissions were required by 9 November 2012. **Read more**

2012 Ports Pricing and Access Review – Final Decision

On 2 October 2012 the ESCOSA finalised its 2012 Ports Pricing and Access Review (Review) in accordance with the requirements of the Essential Services Commission Act 2002 (ESC Act) and the Maritime Services (Access) Act 2000 (MSA Act). In conjunction with the Review, the ESCOSA also completed an Inquiry, pursuant to section 34 of the ESC Act, into areas where the ports pricing and access regimes may be generally improved, and concluded that the current ports price monitoring regime and third-party access regime should continue beyond 30 October 2012, for at least another five years. Following its review into the continuation of the South Australian ports pricing and access regimes, the ESCOSA has released a Final Price Determination enabling the existing ports price monitoring arrangements to continue from 31 October 2012 up to and including 30 October 2017. This price determination replaces the 2010 Ports (Variation) Price Determination, which expired on 30 October 2012. **Read more**

Tasmania

Office of the Tasmanian Economic Regulator (OTTER)

Amendments to the Regulatory Reporting Guideline, Tasmanian Gas Retail Code and Tasmanian Gas Distribution Code

On 21 November 2012 the OTTER issued Version 2 of the Regulatory Reporting Guideline – November 2012 (effective 23 November 2012). In early 2012, it undertook an audit of the regulatory reporting obligations of licensees across the electricity, gas and water and sewerage sectors. This review highlighted inconsistencies across licensees and industries with respect to the frequency of reviews and the obligatory or discretionary nature of such reporting. The OTTER released a Consultation Paper which provided an overview of the proposed amendments to the Guideline and Codes and sought submissions from interested parties and stakeholders. Submissions closed 26 October 2012. **Read more**

Victoria

Essential Services Commission (ESC)

ESC Report on Water Bills

On 14 December 2012 the ESC released a report showing that Victorian households used more water in 2011-12 after years of drought-induced restrictions. The ESC's report on Victoria's 16 urban water businesses found that weighted average household

consumption across Victoria increased from 143 kilolitres (kL) in 2010-11 to 150 kL in 2011-12, reversing the trend of declining consumption between 2006-07 and 2010-11. **Read more**

ESC to Consult on Energy Retail Performance Indicators

On 13 December 2012 the ESC released its staff consultation paper on the review of energy retail performance indicators. **Read more**

ESC to Consult on Regional Water Price Proposals

On 9 November 2012 the ESC announced it will hold a series of public meetings throughout Victoria to gauge public opinion on the proposed five-year (2013-18) water prices and expenditure of the 15 water businesses that supply urban and rural water outside Melbourne. The ESC will then formally assess the water businesses' five-year pricing and service proposals (water plans), before delivering a draft decision in March 2013. After a second period of public consultation, the ESC will make a final decision setting Victorian water prices for a five-year period from 1 July 2013. **Read more**

Retail Electricity and Gas Prices Increase in 2011-12 – Report

On 20 September 2012 the ESC released a report revealing that retail electricity prices rose on average between 10 and 12 per cent across Victoria in 2011-12, while retail gas prices increased by an average of seven per cent. **Read more**

Western Australia

Economic Regulation Authority (ERA)

Goldfields Gas Pipeline – Proposed Tariff Variation

On 13 December 2012 the ERA announced that it had allowed an adjustment to the Reference Tariff for the Goldfields Gas Pipeline, as proposed by Goldfields Gas Transmission Pty Ltd (GGT). The ERA has assessed GGT's notice and supporting information, and is satisfied that it complies with the approved reference tariff variation mechanism. **Read more**

Report on the Efficient Costs and Tariffs of the Water Corporation, Aqwest and the Busselton Water Board

On 29 November 2012 the ERA announced that, on 26 November 2012, it had delivered to the Treasurer its Report on the Inquiry into the Efficient Costs and Tariffs of the Water Corporation, Aqwest and the Busselton Water Board. **Read more**

Dampier to Bunbury Natural Gas Pipeline (DBNGP) Access Arrangement – Revised Decision

On 5 October 2012 the ERA published a revised decision pursuant to Rule 64(4) of the National Gas Rules (NGR) giving effect to the ERA's proposed access arrangement revisions for the Dampier to Bunbury Natural Gas Pipeline (DBNGP). The decision was revised by reason of, and pursuant to, orders of the Australian Competition Tribunal (Tribunal) made on 26 July 2012. The orders were made in an application by DBNGP (WA) Transmission Pty Ltd (DBP) for review of the revised access arrangement decision published by the ERA on 22 December 2011. The revised decision document includes background to the appeal, a summary of the Tribunal's decision in respect of the application and the amended access arrangement. The ERA required DBP to revise its access arrangement information in accordance with its revised decision and to re-submit the revised access arrangement information by 19 October 2012. **Read more**

New Zealand

Commerce Commission (NZCC)

NZCC Announces Proposed Wholesale Price for Broadband Bitstream Service

On 3 December 2012 the NZCC released a draft decision on a new cost-based price for Chorus's unbundled bitstream access (UBA) service. The proposed full UBA price is $32.45 per month per line and will come into effect on 1 December 2014 (current price of $44.98 for most lines). **Read more**

NZCC Announces Small Reduction in Wholesale Price for Chorus's Local Copper Lines

On 3 December 2012 the NZCC released a final decision on the wholesale price for access to Chorus's unbundled copper local loop (UCLL). The new geographically averaged price is $23.52 per month per line and comes into effect on 1 December 2014. This change equates to a 3.85 per cent reduction on the prices set in 2007. **Read more**

New Pricing Limits for 16 Electricity Distribution Businesses

On 30 November 2012 the NZCC released its final decision to reset the default price-quality paths for 16 electricity distributors. Two of the distributors will have to reduce their prices, while the remainder will be able to increase their prices if they choose. The new price limits will take effect from 1 April 2013. **Read more**

NZCC Welcomes Supreme Court Ruling on Input Methodologies

On 15 November 2012 the NZCC welcomed a Supreme Court decision confirming that the NZCC is not required to determine a starting price input methodology for electricity distribution and gas pipeline services. **Read more**

NZCC Issues Draft Report on Wellington International Airport

On 2 November 2012 the NZCC released a draft of a report to the Ministers of Commerce and Transport on how well information disclosure regulation is promoting the purpose of that regulation for Wellington International Airport. **Read more**

NZCC to Monitor Fixed-to-mobile Prices

On 1 November 2012 the Telecommunications Commissioner announced that the NZCC will extend its monitoring of the telecommunications market to include fixed-to-mobile pricing. The decision follows a 30 October 2012 announcement by the NZCC that an application from Vodafone to buy TelstraClear was cleared to proceed. The merger means that Vodafone will move from being a provider of mainly mobile services to having also the fixed-line services currently owned by TelstraClear. **Read more**

Transpower's Maximum Allowable Revenues Adjusted for Coming Two-Year Period

On 31 October 2012 the NZCC completed its review of Transpower's performance in 2011-12 against prices set in the Individual price-quality path, and adjusted Transpower's maximum allowable revenue (MAR) for 2013-14 and 2014-15. Each year the NZCC reviews Transpower's actual revenue and expenditure and adjusts allowed revenue for the years to ensure Transpower continues to comply with the price path. Adjustments are made to exclude capital expenditure which has not yet been approved by the NZCC, and to include new future capital expenditure that has been approved by the NZCC. **Read more**

Vector Seeks Clearance to Acquire Contact Energy's Gas Metering Business

On 25 October 2012 the NZCC received an application from Vector Limited seeking clearance to acquire some or all of the shares or assets of Contact Energy Limited's natural gas metering business. Vector owns and operates infrastructure networks, including gas transmission pipelines and reticulated gas distribution. The NZCC's role is to determine whether the acquisition has the effect of substantially lessening competition in any market. **Read more**

NZCC Proposes Default Price-Quality Paths for Gas Pipeline Services

On 24 October 2012 the NZCC released a revised draft decision proposing the first default price-quality paths for gas pipeline services. The paths will set the maximum prices that gas pipeline businesses are allowed to charge customers for their services from 1 July 2013. Submissions on the revised draft decision were due on 7 December 2012, and cross-submissions due on 21 December 2012. A final decision is expected on the default price-quality paths by 28 February 2013. Changes resulting from the default price-quality path would apply to suppliers of gas pipeline services from 1 July 2013. **Read more**

NZCC Outlines Approach to Telecommunications Development Levy

On 19 October 2012 the NZCC released a paper on its plans to set the Telecommunications Development Levy to be paid by telecommunications companies to the government. The government will use the $50 million a year levy to fund things such as the relay service for the hearing impaired, the Rural

Broadband Initiative and upgrades to the 111 emergency calling systems. Feedback was required by 2 November 2012. **Read more**

Competition Agencies Welcome International Cooperation Act

On 17 October 2012 the NZCC and the ACCC announced the passing of legislation arising out of the Commerce Commission (International Co-operation, and Fees) Act; enabling them to cooperate more effectively on trans-Tasman competition, consumer and telecommunications issues. The NZCC will renew its cooperation arrangement with the ACCC in line with the Act. **Read more**

NZCC Releases Further Input Methodologies

On 1 October 2012 the NZCC released input methodologies for the default price-quality paths applying to electricity distribution services and gas pipeline services. These concern the valuation of assets, allocation of costs and treatment of taxation. **Read more**

NZCC Releases New Information Disclosure Requirements for Electricity and Gas Businesses

On 1 October 2012 the NZCC released new information disclosure requirements for suppliers of electricity distribution services and gas pipeline services. Under the new requirements, regulated businesses will publicly disclose information about investment and innovation, financial performance, pricing and network management. Electricity distribution and gas pipeline businesses must make their first annual disclosures under the new requirements in 2013. **Read more**

Notes on Interesting Decisions

Rural Water Charging Arrangement, Amanda Chadwick and Chen Chou, IPART

After more than a decade of price regulation by IPART, responsibility for the determination of prices for State Water's operations in regulated rivers in the Murray-Darling Basin will transfer to the ACCC under the Commonwealth *Water Act 2007* from 1 July 2014. To facilitate this transition, IPART was requested to examine options for the billing of bulk water charges that better matched customers' cash flows; and to examine and make recommendations about some of the key implications of change.[1] The recommendations of this review may inform State Water and stakeholders' submissions to the ACCC's 2014 price review.

The review issues of broader interest include:

- addressing stakeholder concerns about paying bills in times of low water availability
- options to continue to share efficient costs between customers and the Government based on the principle of impactor-pays
- analysis of financial concerns arising from an estimated 17 per cent reduction in State Water's revenue requirement due to the change in the regulatory regime and current low market interest rates.

IPART's recommendations have generally been accepted by Government.

Billing options

The Government asked IPART to examine options for the billing of bulk-water charges that might be better matched to business cash flows. IPART explored ways of doing this, including changes to:

- bill payment terms
- tariff structures – the ratio of fixed to variable costs, and
- the volatility allowance.

Volatility allowance is calculated such that State Water can recover the additional holding costs from conducting its business when revenue is low due to lower than forecast extractions.

Based on analysis and consultation, IPART has recommended:

- retention of the current tariff structures for State Water, which collects 40 per cent of its revenue requirement from fixed charges
- an amended volatility allowance calculation
- a new policy on the conditional deferral of payment for fixed charges in times of low water availability.

Analysis set out in the Final Report demonstrates that this approach achieves the best match for most customers' cash flows in times of low water availability, whilst minimising negative impacts on State Water and the State Budget. IPART also recommended that State Water investigate offering a 90:10 fixed-to-variable tariff structure for specific customers such as the Commonwealth Environmental Water Holder.

To define the trigger for conditional deferral conditions, IPART analysed the point at which income from water allocation trading would cease to cover fixed water charges for typical businesses. Selling seasonal allocations provides customers with some flexibility in managing their cash flows. Based on analysis of the impact on farm cash flows and the potential administrative burden and financial impacts on State Water, IPART recommended that customers should be able to choose to defer fixed charges with interest once there are two consecutive years of cumulative available water determinations at financial year end of below 5 per cent (expressed as a percentage of the share component of a Water Access Licence.). IPART recommended the deferral period be no more than two years, having regard to the debt management costs of State Water.

IPART's view is that a deferral of payment of fixed charges (with interest) is the most direct and simple way to reduce any negative cash flow impacts on customers during times of low water availability.

Cost shares

In the development of the WICR, the ACCC considered and decided against it continuing a system to share the costs of activities provided by State Water. A system for sharing based on the impactor-pays principle had been implemented in NSW for more than a decade. For this review, the Government asked IPART to identify options for determining the NSW Government's cost share for the Australian Competition and Consumer Commission's (ACCC) determined bulk water charges in NSW, which may include a role for IPART.

IPART examined four options:

[1] Terms of reference for the review of rural water charging systems.

- IPART to continue our existing method of reviewing cost sharing ratios prior to each ACCC determination, findings would then inform ACCC's calculation of the revenue requirement
- freeze the cost sharing ratios at current percentages of the costs of each activity
- continue to apply cost sharing ratios with IPART to review the methodology and ratios prior to every second ACCC determination period
- the Government to contribute a fixed amount to State Water's costs (i.e., cease cost share methodology).

IPART recommended and the Government has accepted reviewing the cost sharing ratios every second pricing determination. This option provided a suitable balance between the need to ensure that the cost sharing ratios remain appropriate, and the additional costs imposed in undertaking a separate review at every pricing determination. In practice, this means that the next review of activities and cost shares would be in time to inform State Water's submission to the ACCC in early 2016.

Financial Implications and Transition to the New Rules

The review identified that State Water's short term financial viability is likely to be negatively impacted by the transition to WICR. State Water's short term financial viability is impacted by the currently low market interest rates, which results in a lower return on capital in the revenue building block; by parameters for the WACC calculation locked into the WICR; and also by the change to the WICR post-tax framework from the pre-tax building block framework used to determine State Water's prices in 2010.

IPART's analysis showed that under a 40:60 fixed to variable tariff structure, a volatility allowance (calculated as per the 2010 determination) and a real post-tax WACC using June 2012 market parameters, State Water's notional revenue reduces by about 17 per cent. For comparison, data for 2010-11 from IPART's most recent State Water Determination, and other parameters based on the ACCC guidance documents, were used.

To address this significant revenue reduction, IPART recommended that State Water undertake further analysis and submit a case for a financeability allowance to the ACCC. Financeability refers to the capacity of a business to finance its activities – including its day-to-day operations and its capital investments – to renew and expand the infrastructure required for these activities. A financeability allowance is an addition to the revenue calculated under the building block approach. It is not a mechanism to mitigate revenue volatility or to adjust revenue during drought conditions.

Guidance on short term financial viability issues under WICR has not been developed to date. It is IPART's view that a decision by the ACCC to allow a financeability allowance is the most transparent way to address temporary potential revenue reductions for State Water.

If allowed, a financeability adjustment advances revenue from a future period as a temporary adjustment. The amount of any financeability allowance provided would be returned to customers by, for example, deducting it from the regulated asset base at subsequent price reviews.

Conclusion

The Terms of Reference for this review required IPART to make recommendations that took into account competing stakeholder interests. This was a challenge, as tariff structures that are better matched to business cash flows may have negative revenue implications for State Water and the NSW Budget. It was considered that introducing a conditional deferral of fixed charges, combined with State Water's existing tariff structure (including a volatility allowance) provides relief to customers when needed, in times of low water availability. At the same time, IPART recommended the condition for an optional deferral of fixed water charges be set at a level that took account of the ability for customers to trade water on the market, and that State Water levy interest on deferred charges to minimise negative financial impacts for both it and the NSW Budget.

To mitigate the impact of short term reductions in revenue from the transition to the WICR, it was recommended that State Water undertake further financial analysis and submit a case to the ACCC for a financeability allowance; advancing revenue from a future period as a temporary adjustment. The amount of any financeability allowance provided should be returned to customers at subsequent price reviews.

The NSW Government has accepted IPART's recommendation of reviewing cost share arrangements once every second ACCC pricing determination, starting from 2017. This means IPART will next review activities and cost shares in time to inform State Water's submission to the ACCC in early 2016.

Regulatory News

Regulatory Conference

Planning has commenced for the 2013 ACCC/AER Regulatory Conference, which will be held in Brisbane on 25 and 26 July 2013.

An outline of topics and main speakers will be provided early in 2013.

Conference bookings will then be open to expressions of interest.

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@accc.gov.au) and for mailing list enquiries please contact Genevieve Pound (Genevieve.Pound@accc.gov.au).