



AER Consumer Reference Group

# **2022 Rate of Return**

## **Presentation to the National Consumer Roundtable**

Bev Hughson, Chair Consumer Reference Group

26.10.2021

# Agenda



- Introduction to the Consumer Reference Group (CRG)
- Background to the Rate of Return Instrument (RoRI)
- Why the RoRI is important to consumers
- How the RoR fits into the AER's network revenue decision
- Where are the 'battle grounds' – and a bit of RoR detail
- AER's RoRI timetable for 2021-22
- How you might influence the AER & how we can help you
- Appendix: Some bed-time reading

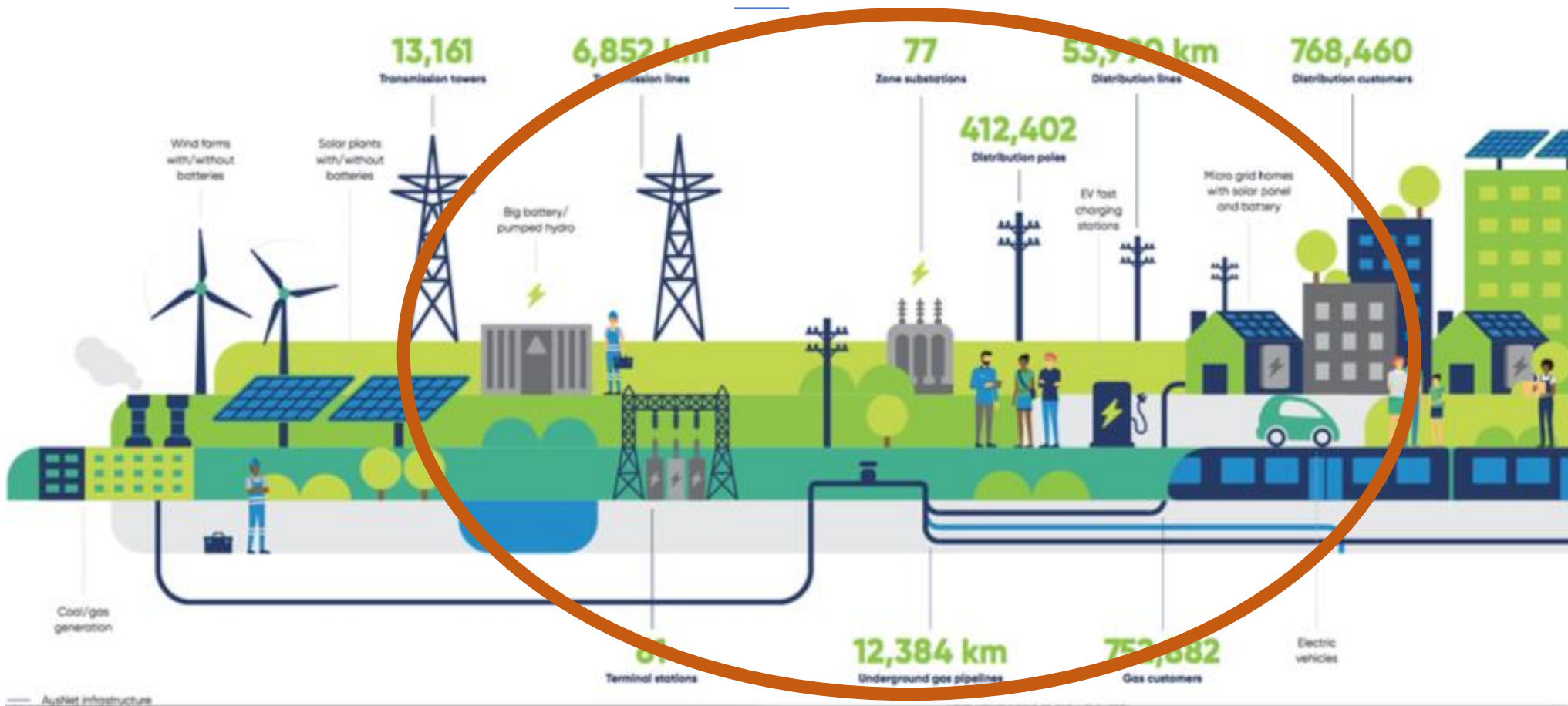
# About the Consumer Reference Group (CRG)



AER  
Consumer  
Reference Group

- Our role derives from the [National Electricity Law and National Gas Law](#)
  - The Laws were amended in 2018 to establish a new process for the AER's determination of the regulated rate of return
  - Removed the right of networks to appeal to the Australian Competition Tribunal
  - Established a formal obligation for the AER to establish and fund an independent consumer reference group
- The CRG's role is defined in the Law to:
  - Provide direct advice to the Australian Energy Regulator (AER) on Rate of Return (RoR) issues
  - Advise the AER on consumer interests and preferences
  - Assist the AER to implement an develop an effective communication consultation process for making the rate of return Instrument
- To do this, the CRG:
  - Provides written advice to the AER and the AER Board on technical issues arising during the development of the RoR Instrument
  - Engages widely with consumers, consumer representatives, industry players and independent investors
  - Encourages as many people as possible to engage directly or indirectly in this process.
- More info: <https://www.aer.gov.au/about-us/stakeholder-engagement/consumer-reference-group>

# What does the RoRI apply to? - \$110 billion worth of electricity and gas networks



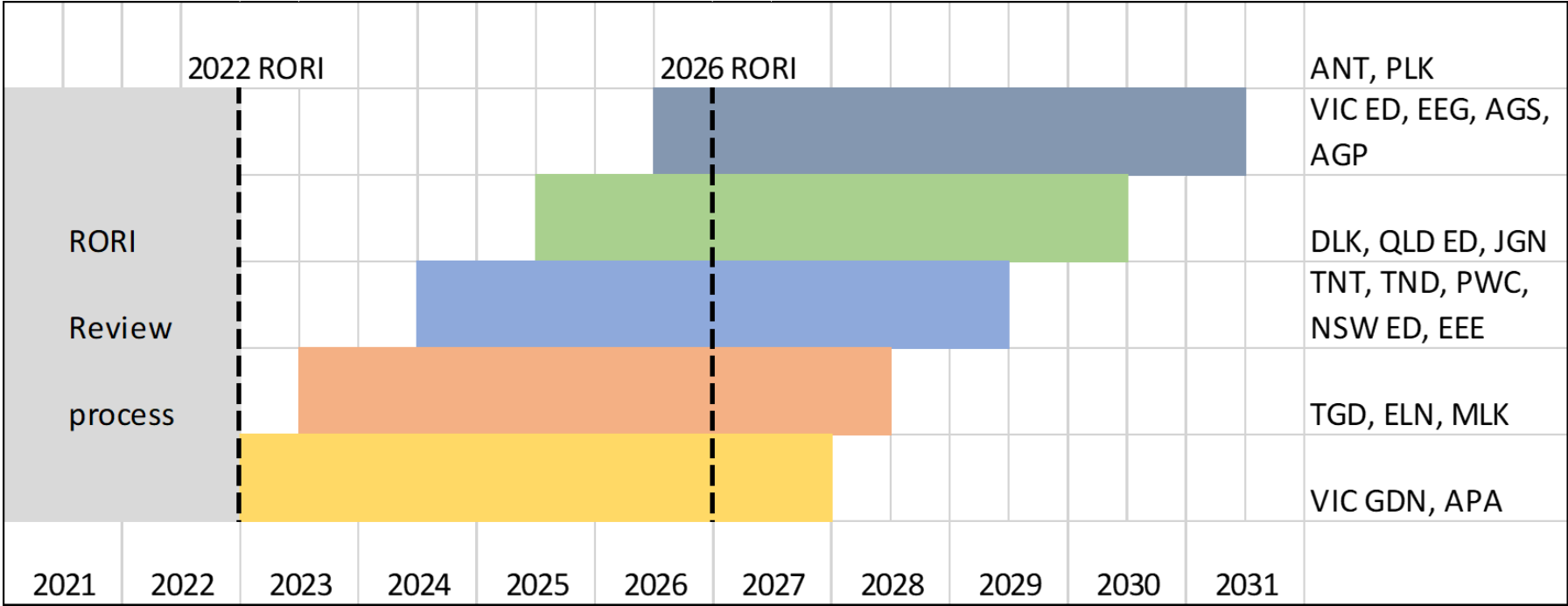
A regulated RoR of 5% means a total cost to consumers of ? per year

# About the Rate of Return Instrument (RoRI)



- The AER's RoR is a **binding rate** of return:
  - the binding instrument details are set out in the Law - and require extensive consultation process before the Final RoRI, including an expert conclave and Independent Panel review, as well as the formation of the CRG
- There is no right of appeal on the merits, only judicial review
  - There used to be a right of appeal, known as a Limited Merits Review (LMR), but this was replaced with the binding instrument, effective from 2018 – LMR was considered costly and disruptive
  - The first binding RoRI came into effect in 2018, to apply from Jan 2019
  - The second binding RoRI will be the 2022 RoRI and will apply from Jan 2023
- The AER has already published a series of “Working Papers” as part of its “Pathway” to the 2022 Rate of return Instrument
  - The 2022 RoRI will have effect over multiple regulatory periods (see next slide)

# RoRI and Determinations Timeline



The AER's 2022 RoR Decision will have an impact on network revenues - and consumers' energy bills through to 2031 (depending on where you live)

# Why is the Rate of Return important to consumers?

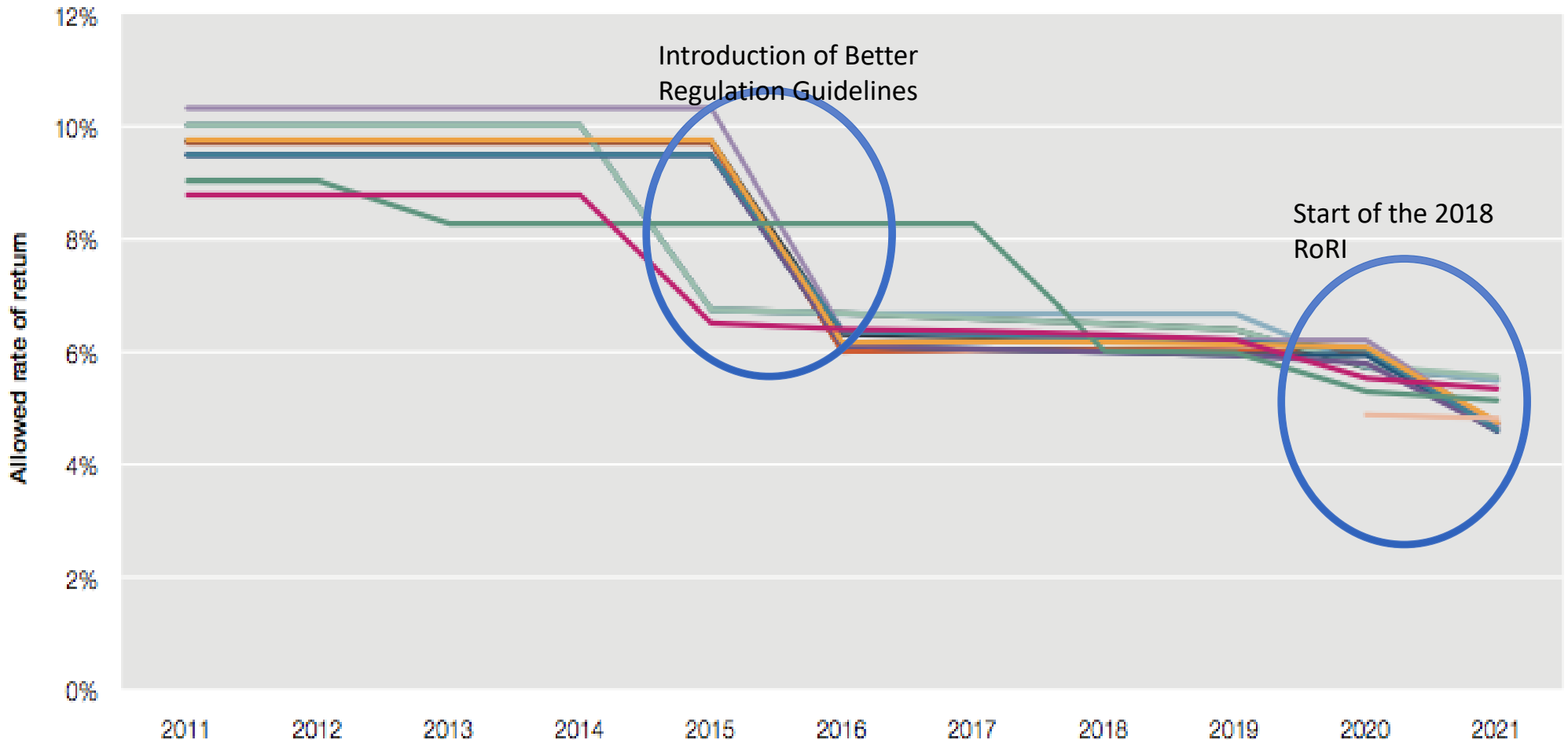


- Bev's rough and ready 50 % of 50% "rule"
  - network charges make up about 50 % of your electricity bill
  - RoR allowance makes up some 50% of the network charge
- An increase of **0.1%** in the allowed RoR will increase bills by \$100m annually
- Networks pushed for increases of **2% - 4% higher** than the AER's final allowed RoR in 2018
- And that's why consumer voices are **SO** important in the lead up to the AER's 2022 decision

*Consumers total bill*



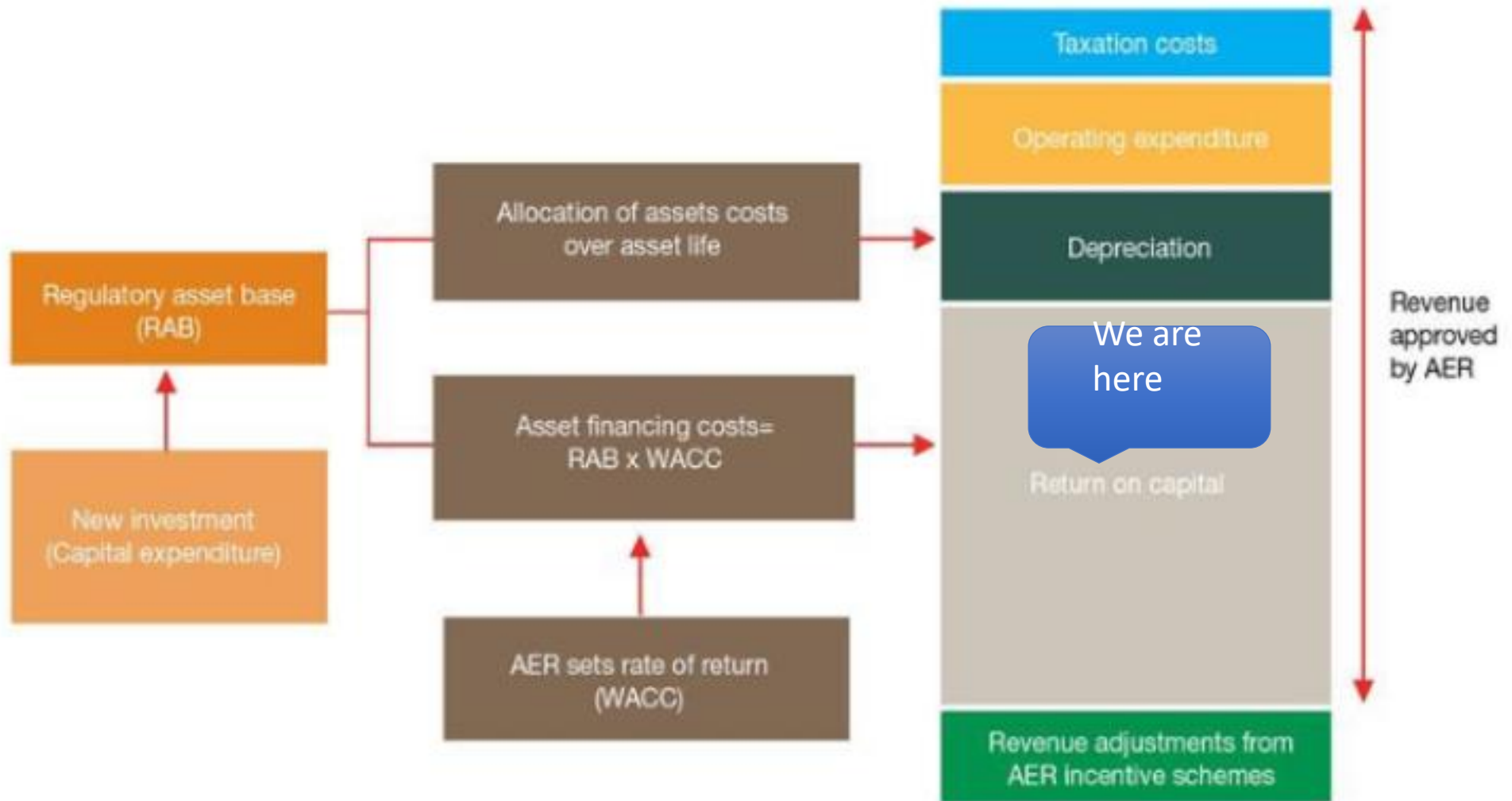
# The allowed rate of return has declined significantly since 2011 – lower interest rates and improved regulation?



Note: Each line represents a different electricity distribution company with changes in the allowed RoR reflecting the timing of the AER's RoR determination for that network

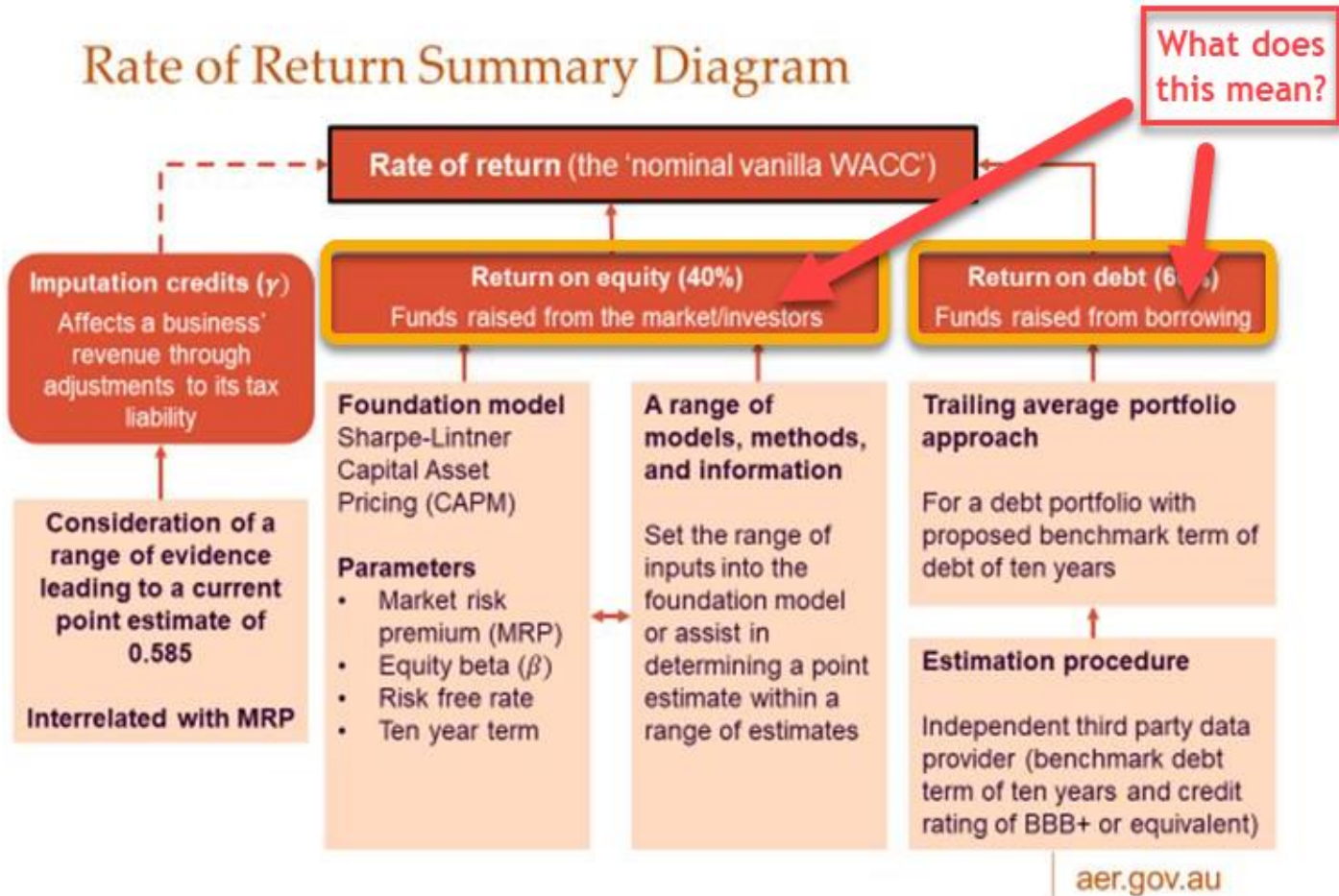


# Where does the RoR fit into the AER's network revenue allowance?



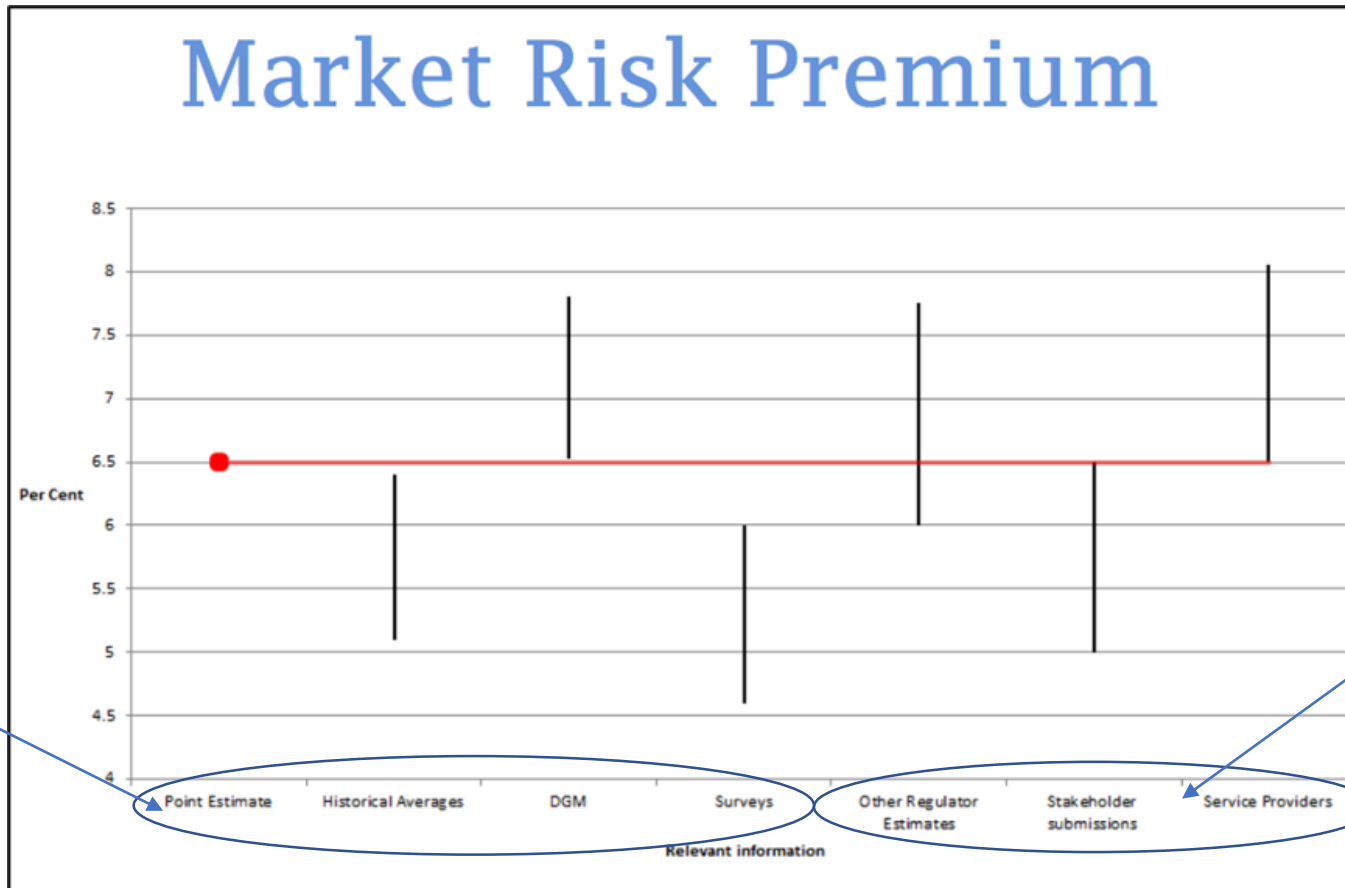
# Where are the “battle grounds”?

## Rate of Return Summary Diagram



# Return on Equity – how to exercise “judgment” when you can’t know the real value

## Market Risk Premium



- Point Estimate
- Historical Averages
- DGM
- Surveys

- Other Regulator Estimates
- Stakeholder submissions
- Service Providers

**Question:** If you were the decision maker, how would you use this different information and why?

# Return on Debt – how low can you go?



BBB+ debt yield curves for RBA, Bloomberg & Thomson Reuters (April 2015 to April 2021)

# Next steps in the AER's RoRI Pathway



Table 1 Indicative Timeline

Milestone	Date
Publish Information Paper	December 2021
Expert Conclave	February 2022
Concurrent Evidence Sessions	February 2022
Submissions on Information Paper close	February 2022
Draft 2022 Rate of Return Instrument released	June 2022
Release of Independent Panel's Report	August 2022
Submissions on Draft Instrument close	September 2022
Final 2022 Rate of Return Instrument released	December 2022

Key milestones for the CRG (and consumers):

- Response to the Information Paper (Feb 2022)
- Response to the Draft Instrument (Sept 2022)

# Ways you can influence the AER's decision

- Write submissions to the AER on topics relevant to you, e.g.
  - The impact of higher energy prices on your constituents
  - Do your constituents value stability in prices or are they able to manage price volatility?
  - Would consumers trade lower prices for more volatility or vice versa?
  - Would consumers trade higher prices for higher reliability, or vice versa?
  - What consumer perspectives and experiences should the AER consider when exercising its judgement?
  - How do your constituents feel about the history of claims by networks that the RoR is too low?
  - Do you think networks are well enough positioned to attract investment
- How can the CRG help you participate in this process?

# Useful references for bed time reading

- [AER Rate of Return webpage](#)
- [CRG webpage](#)
- [Pathway to the RoR process](#)
- [AER position on the RoR and the long term interests of consumers](#)
- [CRG position on the RoR and the long term interests of consumers](#)
- [Overview information on the RoR including definitions of parameters](#)
- [Judgement \(pp.28-40\) and Risk \(pp.28-60\)](#)

## CRG SUBMISSIONS:

- [Debt Data Working Paper](#)
- [Return on Equity](#)
- [RoR and cashflows in a low interest rate environment](#)
- [Term of RoR](#)
- [Debt, Equity and Overall rate of return \(including gamma and gearing\) vol 1 and vol 2](#)