

Review of regulatory decisions

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Overview

- Input methodologies
 - What goes where
 - Cost of capital
- Merit review
 - Legislative settings
 - Outcomes
 - Reflections

IMs: what goes where?

Instrument	Content
Legislation	<ul style="list-style-type: none"> Purpose statement Mode of regulation for the sector Require IMs for key building blocks Require IMs to give sufficient certainty Require determinations to be consistent
Input methodology	<ul style="list-style-type: none"> Rules for calculating the building blocks Rules for incentive schemes Rules for any re-opener or amendment
Front line determination	<ul style="list-style-type: none"> Set maximum revenues / prices Calculations consistent with the IMs Set minimum quality standards Specify incentive schemes Compliance processes

IMs: cost of capital

Input Methodology (EDBs; DPP+CPP)	DPP Determination
Mid-point estimate of Vanilla WACC	Prescribe starting prices for 5 year period, and annual rates of change
Using the CAPM	
Leverage 42%	(Consistent with a 5 year MAR calculation
Equity beta 0.60	Using building blocks methodology
Debt issuance costs 0.2%	Including cost of capital IM)
TAMRP 7.0%	
Average investor tax rate defined	
Prescribed process for identifying Rf	
Prescribed process for identifying debt premium	
Calculation of the 67th percentile	

Merit review: availability

	IM	DPP	CPP	IPP	ID	NA
Merit review	✓					
General appeal*			✓	✓		
Appeal on Q of law	✓	✓	✓	✓	✓	✓
Judicial review	✓	✓	✓	✓	✓	✓

Merit review: standard

- “Materially better” at advancing ...
- the purpose of regulation (long term benefit of consumers) or the IMs (increased certainty)
- Assess IM as a whole and bear in mind its role in the overall scheme
- Look through the inevitable conflict of views and determine whether the alternative is sufficiently compelling
- No deference principle
- Closed record
- Cf general appeal (appellate court disagrees)

Merit review: the outcome

Similar settings to the current Australian LMR framework

Different results:

- First, full, IM rule book issued December 2010
- Comprehensive merit review appeals followed
- Near total dismissal of appeals
- Significant IM decisions since have not provoked appeals (WACC percentile; review of IM rule book)

Reflections on the system

- The HC as a forum
- Commission decisions
- Alternative IM as a whole materially better at advancing LTBC
- Practicalities of remedies
- One-shot merit appeal
- Engagement

Reflections on the balance struck

- Accountability?
- Did the IM construct improve the workings of the merit review system?

Reflections on where to for Alice

- Merit review is important and IMs / guidelines are no substitute (whether your goal is accountability, quality, or less volatility)
- Politics react to prices + volatility
- Can you assure stakeholders that you can shift the dial across the system?