



MAJOR ELECTRICITY USERS' GROUP

2 December 2009

Murray Reynolds
Economist
Economic Services Branch
Commerce Commission
By email to NPB@comcom.govt.nz

Dear Murray

Post-workshop submission on draft cost of capital guidelines

1. This is a post-workshop submission by the Major Electricity Users' Group (MEUG) to the Commerce Commission in relation to the draft cost of capital guidelines workshop held 12th and 13th November 2009¹. Post the workshop the Commission published², amongst other things, a note from Dr Martin Lally "WACC and Leverage" dated 17th November 2009 and Commission memorandum "Effects of Leverage on WACC Under Two Different CAPMs".
2. The Commission requested Mr Garth Ireland of Ireland, Wallace & Associates to respond to matters arising at the workshop. A report by Mr Ireland covering those matters is attached. Mr Ireland attended the workshop as an Expert Advisor and has adopted that approach in the attached report. MEUG agrees with the advice of Mr Ireland.
3. The only other matter we wish to reiterate is the materiality of leverage. An estimate of the difference in costs to consumers of Part 4 regulated entities for zero and 40% leverage was set out in the Ireland, Wallace & Associates report to MEUG, "Input Methodologies Discussion Paper Submission", 31st July 2009 submitted to the Commission on the same date³. That estimate needs to be updated for the factors noted by Mr Ireland in the attached report; that is inclusion of debt issue costs in WACC and the debt premium being a function of leverage rather than being fixed. If those adjustments were made we expect the difference in prices for consumers of Part 4 regulated entities to be several tens if not in excess of one hundred million dollars per annum.

Yours sincerely

Ralph Matthes
Executive Director

¹ Refer <http://www.comcom.govt.nz/IndustryRegulation/Part4/DecisionsList.aspx#1312>

² Refer <http://www.comcom.govt.nz/IndustryRegulation/Part4/DecisionsList.aspx#1299>

³ Refer

http://www.comcom.govt.nz/IndustryRegulation/Part4/ContentFiles/Documents/MEUG%20attached%20Ireland%20Wallace%20-%20IM%20Paper%20-%200875570_1.pdf