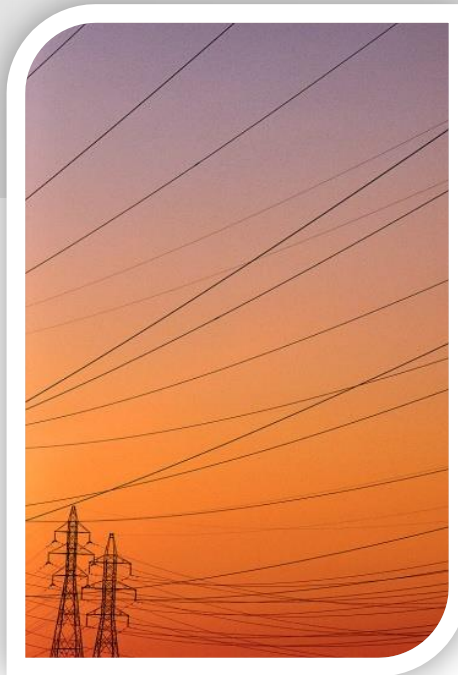


The Australian Energy Regulator



TasNetworks distribution
regulatory proposal 2017-19

Draft Decision Public Forum
18 October 2016

Agenda

- Part 1 – regulatory determination draft decision
 - AER presentation of draft decision
 - Consumer Challenge Panel (CCP) presentation
 - TasNetworks distribution presentation
 - Q&A
- Part 2 – tariff structure statement draft decision
 - AER presentation of draft decision
 - CCP presentation
 - TasNetworks presentation
 - Q&A
 - Next steps

Part 1

**AER presentation of distribution
determination draft decision**

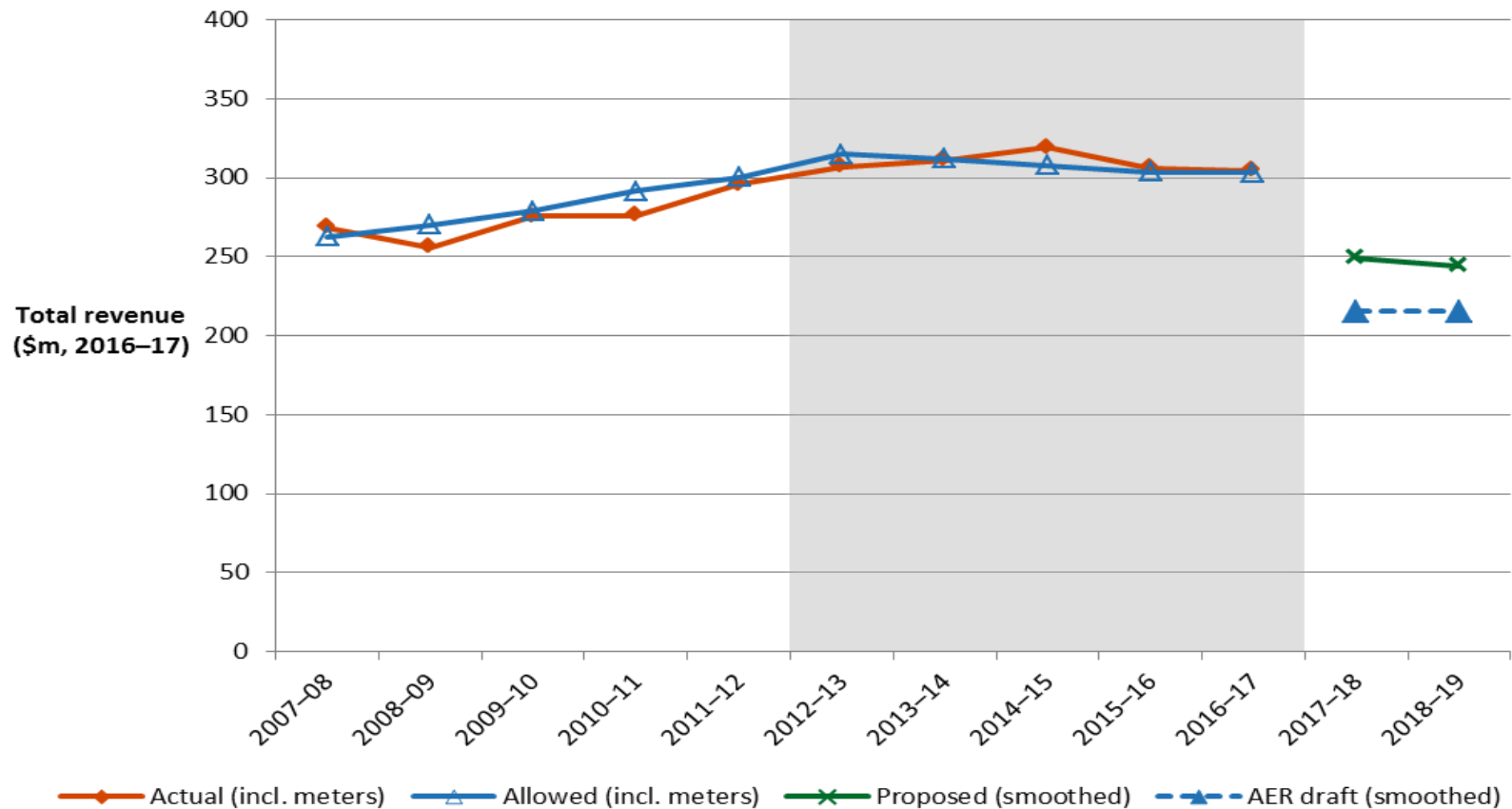
Key points

- The AER published its draft decision on TasNetworks' 2017-19 revenue proposal on 29 September 2016
- TasNetworks can recover \$446.6 million (\$ nominal, smoothed) from consumers over the 2017–19 regulatory control period. This is a 12.8 per cent reduction from TasNetworks' proposed revenue allowance of \$511.9 million (\$ nominal). This reduction is a combination of: aspects we have not approved and the fact that we have accepted TasNetworks methodology but this has required us to update the data proposed to be in line with changing market conditions.
- If implemented, our draft decision would result in a decrease in the distribution component of electricity bills in Tasmania over the 2017-19 regulatory period.

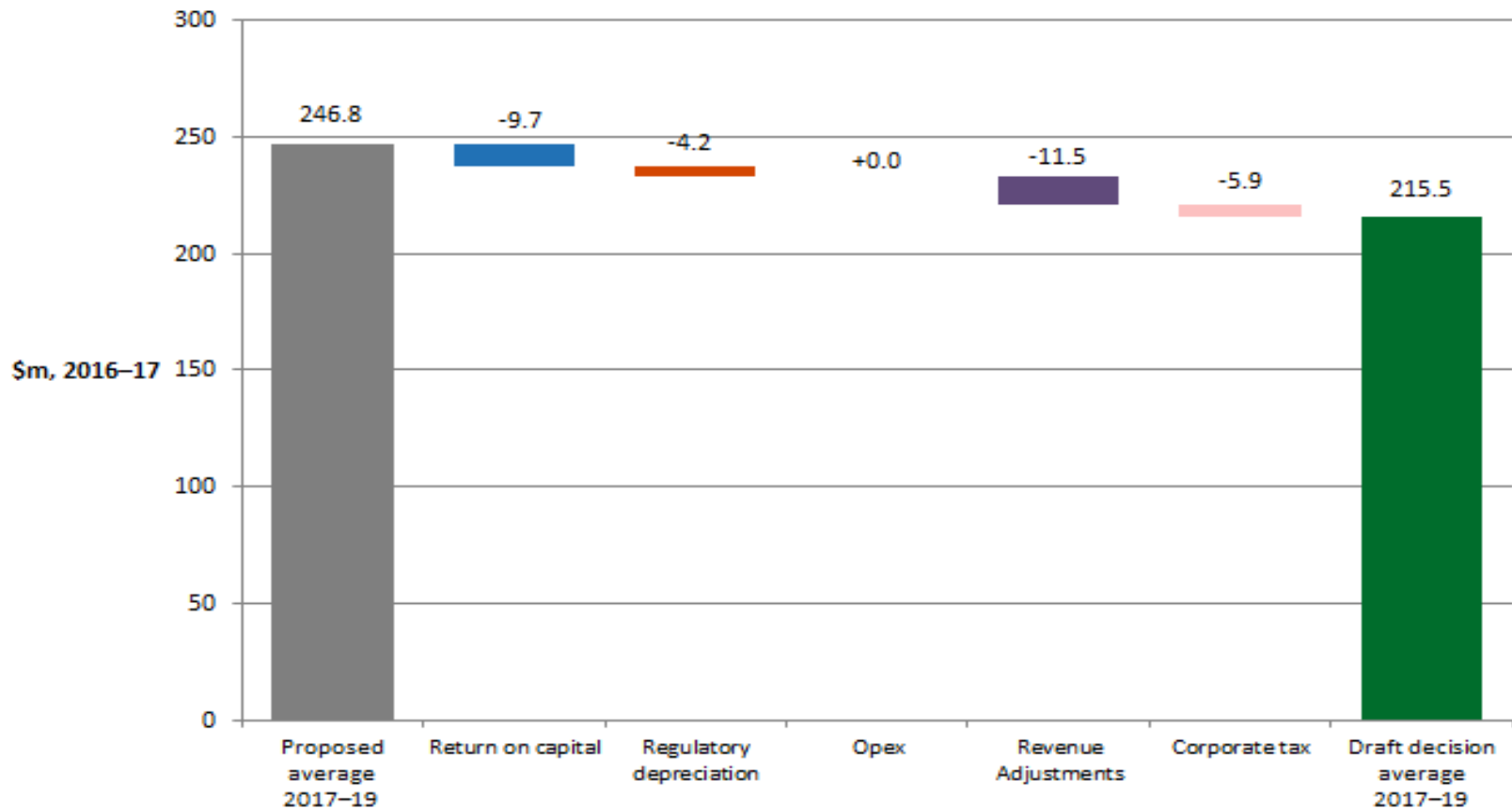
TasNetworks reset timeline

Step	Date
TasNetwork submitted its revenue proposal to AER	29 January 2016
AER published issues paper	11 March 2016
AER held public forum	17 March 2016
Submissions on revenue proposal closed	28 April 2016
AER published draft decision	29 September 2016
AER public forum to explain draft decision	18 October 2016
Submissions due on draft decision	1 December 2016
TasNetworks to submit revised proposal to AER	1 December 2016
Further submissions due, including on revised proposal	23 December 2016
AER to publish final decision	No later than 30 April 2017

Draft decision total revenue requirement (\$m, 2016-17)



AER's draft decision and TasNetworks' proposed annual building block costs (\$million, 2016-17)



Impact of draft decision on customer bills (\$nominal)

	2016–17	2017–18	2018–19
AER draft decision			
Residential annual electricity bill	1763 ^a	1582	1600
Annual change ^c		-181 (-10.2%)	17 (1.1%)
Small business annual electricity bill	3225 ^b	2894	2926
Annual change ^c		-331 (-10.2%)	31 (1.1%)
TasNetworks proposal			
Residential annual electricity bill	1763 ^a	1659	1668
Annual change ^c		-104 (-5.9%)	8 (0.5%)
Small business annual electricity bill	3225 ^b	3036	3051
Annual change ^c		-190 (-5.9%)	15 (0.5%)

Draft decision on rate of return

	AER previous decision (2012–17)	TasNetworks' proposal (2017–18)	AER draft decision (2017–18)	Allowed return over 2017–19 regulatory control period
Return on equity (nominal post-tax)	8.69	7.30	6.50	Constant (6.5%)
Return on debt (nominal pre-tax)	8.00	5.20	4.79	Updated annually
Gearing	60	60	60	Constant (60%)
Overall rate of return (nominal, vanilla)	8.28	6.04	5.48	Updated annually for return on debt
Forecast inflation	2.60	2.50	2.45	Constant (2.45%)

Rate of return

- In its proposal TasNetworks used the AER's approach to determining the rate of return (RoR) as set out in the AER's RoR guideline
- We have accepted this approach however, as the guideline requires consideration of prevailing market conditions at the time of the decision, there is a difference between our draft decision RoR (5.48%) and TasNetworks proposed RoR (6.04%). This is due to changes in financial market conditions since TasNetworks submitted its proposal
- In our final decision we will update the RoR again, having regard to the prevailing market conditions at the time we make our final decision

Draft decision on gamma

- We do not accept TasNetworks' proposed value of imputation credits (or gamma) of 0.25. Instead, we adopt a value of imputation credits of 0.4.
- We consider that the use of a value for imputation credits of 0.4 will result in equity investors in the benchmark efficient entity receiving an ex ante total return (inclusive of the value of imputation credits) commensurate with the efficient equity financing costs of a benchmark efficient entity.

Adjustments to the efficiency benefit sharing scheme

- We have determined an EBSS carryover amount of \$18.1 million (\$2016–17) from the application of the EBSS during the 2012–17 regulatory control period. This is \$23.0 million (\$2016–17) less than TasNetworks' proposal.
- The primary reason for this difference is that TasNetworks' EBSS calculations assume year 4 (2015–16) is used as the base year to forecast opex. However, TasNetworks used year 3 (2014–15) to forecast opex.

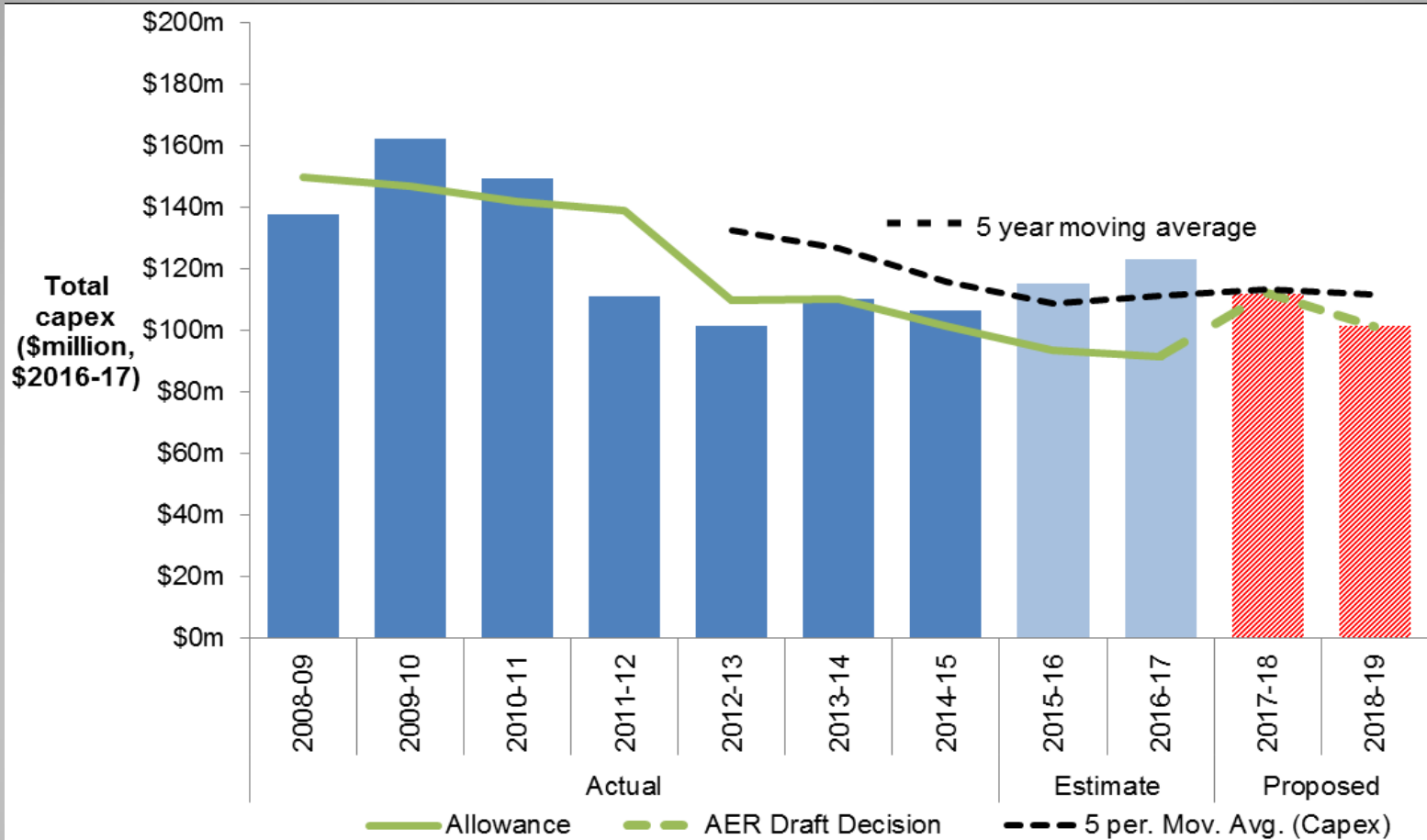
Depreciation

- We do not accept TasNetworks' proposed regulatory depreciation allowance of \$107.2 million (\$ nominal) for the 2017–19 regulatory control period.
- Instead, we determine a regulatory depreciation allowance of \$98.6 million (\$ nominal). This amount represents a reduction of \$8.6 million (or 8.0 per cent) on the proposed amount.

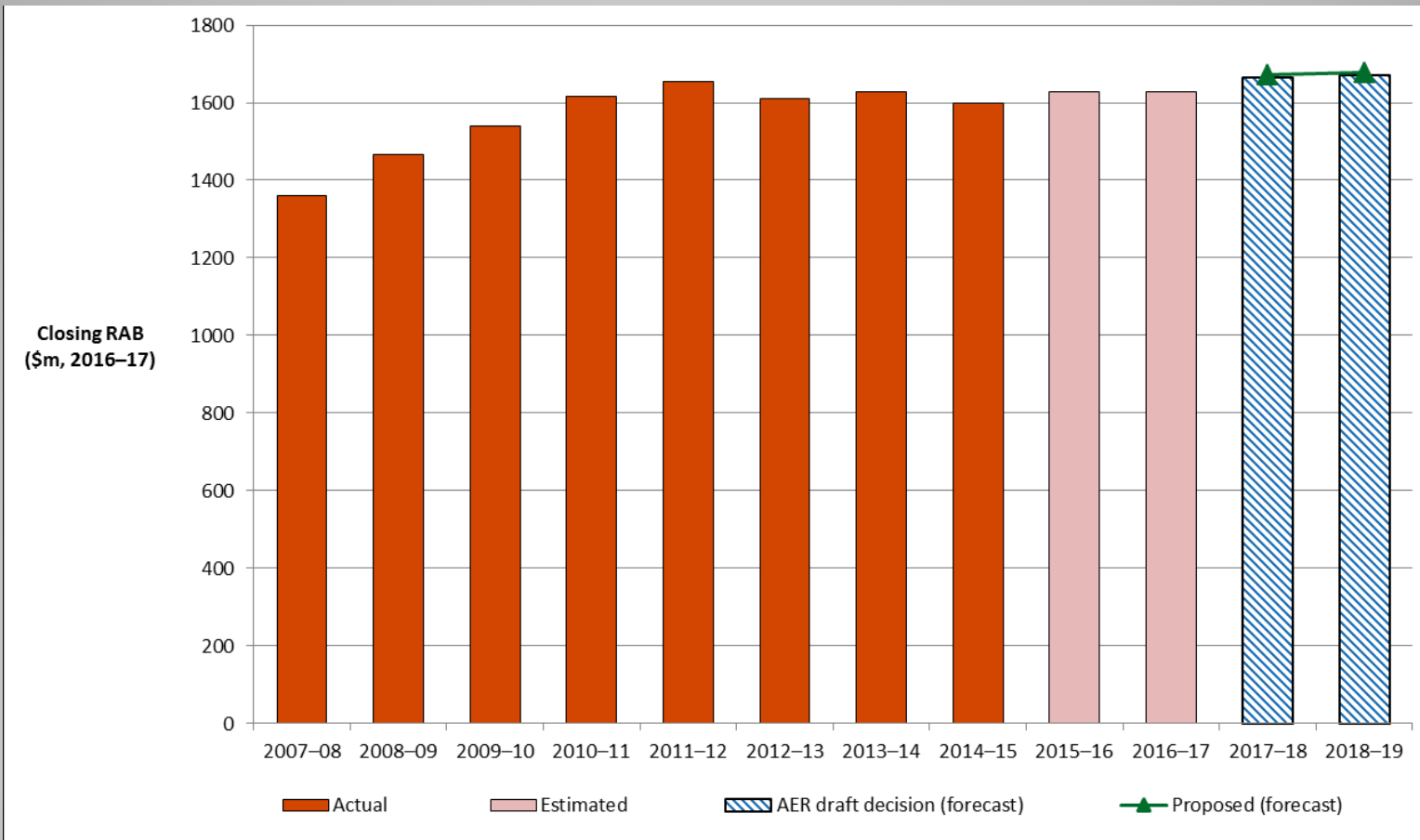
Capital expenditure

- TasNetworks proposed total forecast capex of \$213.4 million (\$2016–17) for the 2017–19 regulatory control period. Our draft decision is to accept TasNetworks' capex proposal which we consider reasonably reflects the capex criteria.
- As part of our assessment, we reviewed each of TasNetworks' capex components and their main drivers. We are satisfied with all categories of capex which we found are mostly reducing or in line with longer term trends.

Actual and forecast capex 2008-19



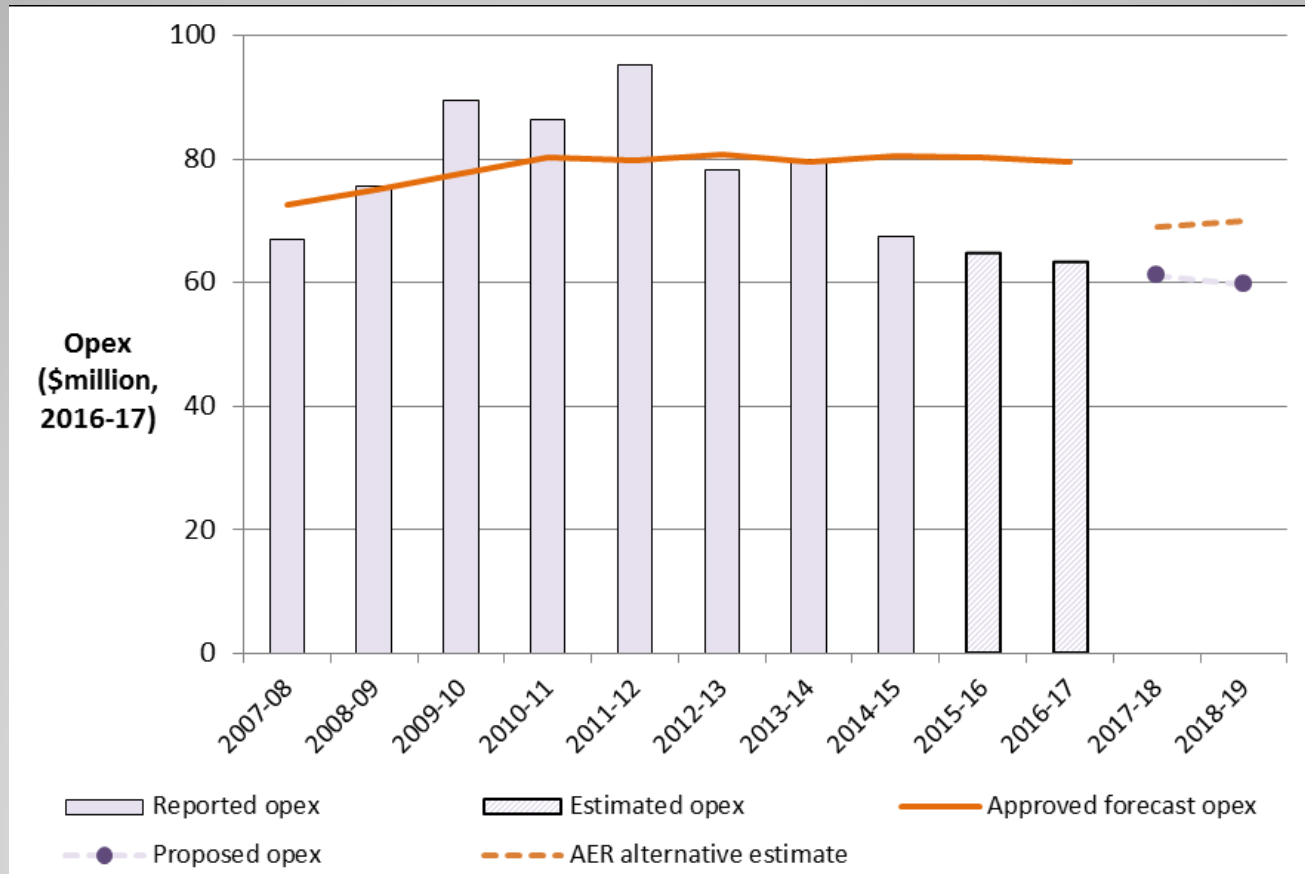
Actual, proposed, and draft decision RAB



Operating expenditure

- Our draft decision is to accept TasNetworks' opex forecast of \$123.1 million (\$2016–17) over the 2017–19 regulatory period. TasNetworks' proposal is 14.5 per cent lower (in real terms) than its annual opex spend over 2012–17. Stakeholder submissions were broadly supportive of TasNetworks' proposal.
- To assess TasNetworks' proposal, we developed an alternative estimate of efficient opex using our standard 'base-step-trend' approach. Our alternative estimate of forecast total opex is \$140.6 million (\$2016–17). This is \$17.5 million higher than TasNetworks' proposal, which we accept.

Draft decision on forecast operating expenditure



Consumer engagement

- TasNetworks has taken important steps to engage with its customers.
- All submissions spoke highly of TasNetworks engagement efforts and its openness and transparency

Consumer Challenge Panel presentation

TasNetworks presentation

Questions?

Part 2

**AER presentation of tariff structure
statement draft decision**

Draft decision on tariff structure statement

- Did not approve TasNetworks' proposed tariff structure because of one aspect – fixed charges for HV customers
- Otherwise, satisfied TSS meets the pricing principles
- Concur that demand based tariffs are appropriate means for charging and cost recovery
- Satisfied that two peak periods – morning and afternoon – are warranted for residential customer

Draft decision on tariff structure statement (cont.)

- Approve continuance of legacy tariffs – kWh based – for 2017-19
- Help customers understand new tariffs, and transition from legacy tariffs to demand based tariffs
- TasNetworks should spell out interaction with new meters/old meters and demand tariffs in revised TSS
- We note that move to cost reflective pricing necessitates removal of cross subsidised tariffs. TasNetworks is doing this over an extended 15 year time period

Draft decision on tariff structure statement (cont.)

- TasNetworks needs to undertake more work with High Voltage customers to explain large increase in proposed fixed charges
- Improvements for 2019-24 tariff structure consultation that we recommend be considered:
 - timeframes for LV customers to transition to demand tariffs
 - Reconsider use of single 30 minute window to measure demand – maybe average of top three/four demands better?
 - Timeframes for tariff realignment to eliminate cross subsidies
 - Update on options for irrigation customers
 - Consider incorporating replacement capex into long run marginal cost estimates

Consumer Challenge Panel TSS presentation

TasNetworks TSS presentation

Questions?

Next steps

- Submissions due by 1 December 2016
- Revised proposal due by 1 December 2016
- Further submissions (including on revised proposal) due by 23 December 2016
- Final decision due by 30 April 2017

- AER contact:
TasElectricity2017@aer.gov.au