Final decision

Victorian Energy Networks Corporation (VENCorp)

transmission determination

2008-09 to 2013-14

April 2008

AUSTRALIAN ENERGY REGULATOR

Contents

Shortened forms

$/Mwh	dollars per megawatt hour
$2007-08	real 2007-08 dollars
ACCC	Australian Competition and Consumer Commission
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
AIS	availability incentive scheme
cl.	Clause
CPI	consumer price index
EAPR	Electricity Annual Planning Report
m	Million
MAAR	Maximum allowable aggregate revenue
MAR	maximum allowed revenue
MW	Mega watt
Mwh	megawatt hour
NEL	National Electricity Law
NEM	National Electricity Market
NER	National Electricity Rules
NTSC	Negotiated transmission service criteria
opex	operating expenditure
RAB	Regulatory asset base
TNSP	Transmission service network provider
TUOS	transmission use of system
VENCorp	Victorian Energy Networks Corporation
Vic	Victoria
WACC	Weighted average cost of capital

Overview[1]

Under the National Electricity Law (NEL) and National Electricity Rules (NER), the Australian Energy Regulator (AER) is responsible for the economic regulation of monopoly transmission services in the National Electricity Market (NEM).

The AER is required to make transmission determinations under the NER in respect of certain services provided by transmission businesses, including VENCorp. The transmission arrangements in Victoria are unique in the NEM. SP AusNet owns and operates the transmission network and provides bulk transmission services to VENCorp. VENCorp owns no transmission assets, but provides shared network services to users and is responsible for planning and directing the augmentation of the shared network. Elements of VENCorp's transmission determination are therefore dependent on the transmission determination made for SP AusNet, as the latter recovers a significant proportion of its revenue from VENCorp.

The AER published its draft decision on VENCorp's transmission determination for the regulatory period 1 July 2008 to 30 June 2014 on 30 November 2007, rejecting VENCorp's proposed maximum allowable aggregate revenue (MAAR) of $2 889.80m, and allowing a lower MAAR of $2 713.93m. The draft decision also rejected VENCorp's proposed negotiating framework and pricing methodology, requiring changes to both to achieve compliance with the NER.

In response to the draft decision, VENCorp submitted a revised negotiating framework and pricing methodology implementing changes required by the AER. VENCorp has not responded to the AER's draft decision on its proposed MAAR. No submissions from other parties were received on the AER's draft decision or VENCorp's revised negotiating framework and pricing methodology.

This final decision approves the revised negotiating framework and pricing methodology submitted by VENCorp, and the negotiated transmission service criteria determined in the draft decision.

The MAAR determined for VENCorp in the draft decision was necessarily calculated on the basis of the AER's draft decision on SP AusNet's transmission determination. In determining VENCorp's MAAR for the forthcoming regulatory period, this final decision departs from the draft to recognise the AER's final decision on SP AusNet's transmission determination, which was released on 31 January 2008.

The resultant MAAR for VENCorp is a total of $2 866.46m over the six years of the regulatory period. This is an increase of $152.53m (or 5.62%) from the draft decision.

Excluding the impact of settlement residues received by VENCorp, this final decision is expected to result in an average annual increase of 4.63% to nominal transmission charges, from $7.50/Mwh in 2007-08 to $9.84/Mwh in 2014. Assuming purely for illustrative purposes that non-transmission costs increase by only inflation, a total small end user's annual bill is expected to increase, in nominal terms, from $1 200 in

[1] All figures are nominal unless otherwise indicated.

2007-08 to $1 411 in 2013-14. This represents an average annual nominal increase of 2.74% (0.15% real).

Summary

The Australian Energy Regulator (AER) is responsible for the economic regulation of monopoly transmission services in the National Electricity Market (NEM).

The AER must make transmission determinations for Transmission Network Service Providers (TNSPs) in accordance with the NER in respect of prescribed and negotiated transmission services. This is the AER's final decision on the transmission determination that will apply to the Victorian Energy Networks Corporation (VENCorp) for the regulatory period 1 July 2008 to 30 June 2014.

Introduction

The ACCC determined VENCorp's current revenue cap for the five and a half year period from 1 January 2003 to 30 June 2008 in accordance with its responsibilities under the National Electricity Code. The AER assumed responsibility for regulating the electricity transmission services provided by VENCorp on 1 July 2005. This final decision and transmission determination have been made in accordance with chapter 6A of the National Electricity Rules (NER), which took effect on 16 November 2006, as modified by the jurisdictional derogation for Victoria in chapter 9, Part A of the NER.

The AER's transmission determination for VENCorp has four components:

1. a determination of VENCorp's maximum allowable aggregate revenue (MAAR) for the regulatory period, and for each financial year of the regulatory period
2. a determination in relation to VENCorp's negotiating framework
3. a determination that specifies the negotiated transmission service criteria that apply to VENCorp
4. a determination that specifies the pricing methodology that applies to VENCorp.

The AER's final decision on each of these components is summarised in the sections below. Further detail is provided in the relevant chapters of this final decision.

The AER's transmission determination for VENCorp for the regulatory period 1 July 2008 to 30 June 2014 has been published with this final decision.

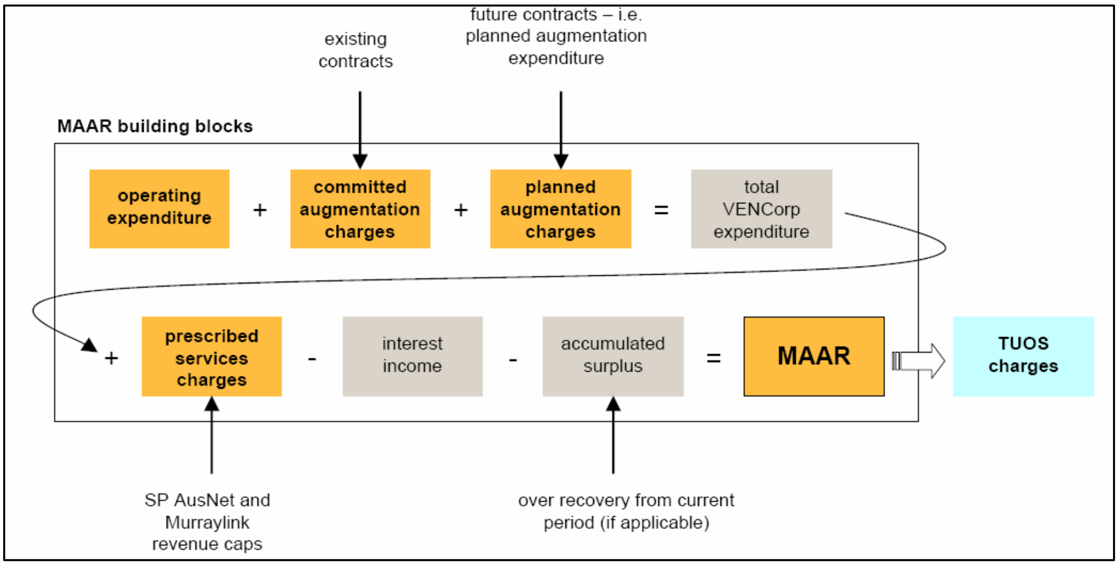
MAAR[2]

VENCorp's maximum allowable aggregate revenue (MAAR) is the total of VENCorp's operating expenditure (opex), planned augmentation charges, committed augmentation charges and prescribed service charges payable to SP AusNet and Murraylink for the provision of prescribed services by those TNSPs, adjusted for any surplus accumulated in the current regulatory period.

[2] All figures are nominal unless otherwise indicated.

For each year of the relevant regulatory period, VENCorp's total revenue requirement is calculated as shown in figure 1:

Figure 1 Calculation of maximum allowable aggregate revenue



Source: AER

The total revenue requirement determined by the AER in this final decision operates as a cap on the revenue that VENCorp may earn in the forthcoming regulatory period.

In its draft decision the AER rejected VENCorp's proposed MAAR of $2 889.80m, and allowed an adjusted MAAR of $2 713.93m calculated on the basis of adjustments to VENCorp's proposed values for the components above.

No submissions were received from VENCorp or any other party on this aspect of the AER's draft decision.

The AER's final decision on each component of VENCorp's revenue determination is set out below.

Operating expenditure

The AER's draft decision allowed total forecast operating expenditure (opex) of $39.37m (nominal), which the AER was satisfied reasonably reflected the opex criteria set out in cl. 6A.6.6 of the NER, taking into account the relevant opex factors in that clause.

The AER has not been made aware of any reason to depart from this aspect of its draft decision. For the reasons outlined in that decision, the AER has therefore determined that total forecast opex of $39.37m (nominal) will be included in VENCorp's MAAR for the forthcoming regulatory period.

Committed network augmentation charges

In its draft decision, the AER allowed a forecast allowance of $125.16m (nominal) to cover the cost of charges payable by VENCorp under contracts entered into during and prior to the current regulatory period.

For the reasons outlined in its draft decision, the AER's final decision is that a forecast of $125.16m (nominal) will be included in VENCorp's MAAR for the forthcoming regulatory period.

Forecast planned network augmentation expenditure and charges

The AER's draft decision allowed a forecast of $200.78m ($2007-08) of planned augmentation expenditure for the forthcoming regulatory period. Applying the methodology submitted by VENCorp for this purpose, the AER calculated a forecast of planned augmentation charges payable by VENCorp within the forthcoming regulatory period, under contracts expected to be entered into in that period.

To derive a forecast of planned augmentation charges from the underlying expenditure forecast, this methodology:

- depreciates the approved forecast planned augmentation expenditure using a straight line methodology over an assumed asset life of 30 years;
- applies a nominal vanilla WACC (in the draft decision, this was the indicative WACC of 8.85% applied in the AER's draft decision on SP AusNet's transmission determination for the same period);
- applies an inflation forecast (in the draft decision, this was a forecast of 3%); and
- adds an allowance of 1.5% of capital costs for the opex likely to be incurred on the capital component of forecast planned augmentations.

The draft decision allowed a total forecast of planned augmentation charges of $46.18m (nominal).

On 31 January 2008, the AER published its final transmission determination for SP AusNet. In place of the indicative WACC of 8.85% applied in its draft decision, the final transmission determination applied a nominal vanilla WACC of 9.76%.

As in its draft decision, the AER considers it appropriate to use a consistent WACC for SP AusNet and VENCorp. The AER has therefore recalculated its forecast of planned augmentation charges applying a nominal vanilla WACC of 9.76%.

The AER has also updated its forecast of inflation, using the methodology outlined in the SP AusNet final decision. To derive an implied 10-year inflation forecast, the AER has taken the average of the Reserve Bank of Australia's (RBA) short-term inflation forecasts, which are currently available for two years, and an assumed inflation forecast of 2.5% (the mid-point of the RBA's target range) for the remaining 8 years. The inflation forecast applied in this final decision is 2.63%.

No other changes to this calculation have been made.

The AER approves the inclusion of total forecast planned augmentation charges of $47.45m (nominal) in VENCorp's MAAR for the forthcoming regulatory period. This is an increase of $1.27m (or 2.75%) from the draft decision.

Prescribed services charges

The AER's draft decision allowed a forecast of $2 534.41m (nominal) in prescribed service charges payable by VENCorp to SP AusNet and Murraylink over the forthcoming regulatory period.

The forecast of prescribed service charges payable to SP AusNet was calculated on the following key assumptions:

- 85% of SP AusNet's non-easement tax maximum allowed revenue (MAR) is recovered through VENCorp; and
- 100% of SP AusNet's easement tax is recovered through VENCorp

The forecast of prescribed service charges payable to Murraylink was calculated on the basis of an agreement between VENCorp and ElectraNet, under which 55% of Murraylink's MAR is recovered through VENCorp.

The approved forecast of prescribed services payable to Murraylink was calculated on the basis of the substituted revenue cap approved by the ACCC on 1 April 2004. That revenue cap has not changed since the AER's draft decision on VENCorp's transmission determination was published.

At the time of the draft decision, the forecast of prescribed service charges payable to SP AusNet was necessarily based on the total MAR of $2 793.97m (nominal), and the forecast easement tax of $516.25m ($2007-08) in the AER's draft decision on SP AusNet's transmission determination. The AER's final decision on SP AusNet's transmission determination approved a higher MAR of $2 979.21m (nominal), and a higher easement tax forecast of $520.85m ($2007-08). As previously noted, the SP AusNet final decision also contained a 10 year inflation forecast of 2.59%.

The AER has recalculated its forecast of prescribed service charges payable to SP AusNet to reflect its final decision on SP AusNet's transmission determination, and approves the inclusion of total forecast prescribed service charges of $2 685.67m (nominal) in VENCorp's MAAR for the forthcoming regulatory period.

Other adjustments to VENCorp's MAAR

Interest income

In its draft decision the AER reduced the sum of VENCorp's forecast opex, committed augmentation charges, planned augmentation charges and prescribed services charges by $1m (nominal), in each year, to account for the interest income VENCorp expects to earn annually during its forthcoming regulatory period. The deduction of forecast interest income from VENCorp's forecast statutory electricity transmission-related costs is important to ensure that VENCorp's MAAR is determined on a full cost recovery and no operating surplus basis.

No submissions were received on this adjustment. The AER therefore maintains its draft decision that VENCorp's total forecast expenditure in each year of the regulatory period will be reduced by $1m (nominal).

Accumulated surplus

Pursuant to cl. 9.8.4C(e)(iii) of the NER, the AER must take into account any expected accumulated surplus or deficit from the current regulatory period in determining VENCorp's MAAR for the forthcoming regulatory period.

The AER's draft decision deducted the full amount of VENCorp's expected 2007-08 accumulated surplus ($25.19m, nominal) from its MAAR in 2008-09. This approach was based on the AER's understanding of the approach that VENCorp itself follows annually in setting its transmission charges.

The AER received no submissions on this matter, and VENCorp has provided no new information in relation to the amount of the surplus. The AER has therefore determined that the same adjustment of $25.19m (nominal) will be made to the 2008-09 MAAR determined for VENCorp in this final decision.

MAAR

Taking into account its conclusions on each component of VENCorp's MAAR, as set out in the sections above, the AER has determined VENCorp's MAAR for each financial year of the forthcoming regulatory period.

Table 1 Final decision – MAAR (nominal $m)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
Operating expenditure	5.99	6.20	6.43	6.67	6.91	7.17	39.37
Committed augmentation charges	19.35	19.93	20.53	21.14	21.78	22.43	125.16
Planned augmentation charges	0.39	1.06	5.42	11.09	15.67	13.82	47.45
Total VENCorp expenditure	**25.72**	**27.19**	**32.38**	**38.90**	**44.36**	**43.42**	**211.98**
Prescribed services charges	408.05	423.40	438.54	455.09	471.37	489.22	2685.67
minus Interest income	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-6.00
minus Accumulated surplus	-25.19						-25.19
MAAR	**407.59**	**449.60**	**469.92**	**492.99**	**514.73**	**531.64**	**2866.46**

Source: AER analysis

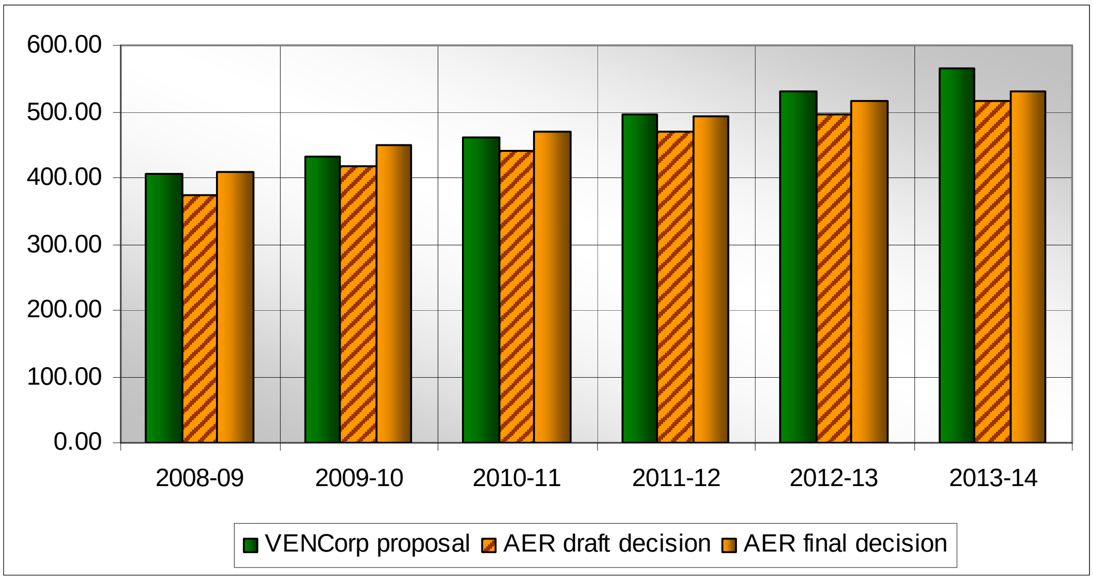
The resultant MAAR is a total of $2 866.46m (nominal) over the six years of the regulatory period. This is an increase of $152.53m (or 5.62%) from the draft decision, attributable predominately to the SP AusNet final decision.

Total adjustments in each year of the regulatory period are shown in the table and figure below.

Table 2 Final decision – MAAR, adjustment from draft decision ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
VENCorp proposal	**405.00**	**430.50**	**462.00**	**496.70**	**529.90**	**565.70**	**2889.80**
AER adjustment	-31.92	-12.20	-20.02	-27.86	-35.02	-48.85	-175.87
AER draft decision	**373.08**	**418.30**	**441.98**	**468.84**	**494.88**	**516.85**	**2713.93**
AER adjustment	34.51	31.30	27.93	24.15	19.84	14.80	152.53
AER final decision	**407.59**	**449.60**	**469.92**	**492.99**	**514.73**	**531.64**	**2,866.46**

Figure 2 Final decision – MAAR, adjustment from draft decision ($nominal)



Negotiating framework

The AER’s transmission determination for VENCorp must include a determination relating to VENCorp’s negotiating framework. The negotiating framework details the minimum procedure to be followed by VENCorp in determining the terms and conditions of access to negotiated services with a service applicant. Where an access dispute occurs between VENCorp and a service applicant, a commercial arbitrator must have regard to the negotiating framework when settling the dispute.

In its draft decision, the AER determined that VENCorp’s proposed negotiating framework was not compliant in one respect, and required amendment to the relevant clause of the framework.

Where VENCorp’s proposed negotiating framework required service applicants to pay a fee of $15,000 upon application for access to a negotiated service (to cover costs associated with processing such an application), the AER required insertion of a clause stating that where costs are less than $15 000, the difference will be refunded to the service applicant. This amendment was the only change required before the proposed framework could be considered compliant with the NER and approved by the AER.

In response to the draft decision, VENCorp submitted a revised proposed negotiating framework implementing the change required by the AER as set out in the draft decision, and without further amendment. No submissions were received from other parties in relation to this aspect of the draft decision or VENCorp's revised proposed negotiating framework.

The AER is satisfied that VENCorp's revised proposed negotiating framework is now compliant in all respects with the requirements of the NER, and approved the application of that framework for the 2008-14 regulatory period.

Negotiated transmission services criteria

The NER require a transmission determination by the AER to include negotiated transmission service criteria (negotiating criteria) applicable to VENCorp for the relevant regulatory period. The negotiating criteria must give effect to, and be consistent with, the negotiated transmission service principles set out in cl. 6A.9.1 of the NER, and will be applied:

- by the TNSP in negotiating the terms and conditions of access for negotiated transmission services; and
- by a commercial arbitrator in resolving any dispute between a TNSP and a person wishing to receive a negotiated transmission service.

The AER's draft decision determined negotiating criteria which gave effect to, and were consistent with the negotiated transmission service principles. No submissions were received from VENCorp or other interested parties in relation to the negotiating criteria set out in the draft decision.

This final decision therefore approves the negotiating criteria identified in the draft decision, which will apply to VENCorp for the forthcoming regulatory period.

Pricing methodology

VENCorp's initial proposed pricing methodology was developed under the agreed interim pricing methodology guidelines published by the AER on 16 February 2007. The final pricing guidelines were published on 30 October 2007. VENCorp elected to have the AER assess its pricing methodology against the final guidelines. Variances between the agreed interim arrangements under which VENCorp's proposed methodology was prepared, and the final pricing guidelines under which it was assessed, meant that the AER was unable to accept VENCorp's proposed pricing methodology.

The areas of non-compliance identified were related solely to the transition from the interim arrangements to the final guidelines. To comply with the AER's final guidelines, the draft decision required that VENCorp's methodology be amended to incorporate the following:

- an explanation of how the value of 'additional assets' will be calculated as it affects attributable cost shares (cl. 2.1(d)(1)(A));
- compliance with cl. 2.4 of the guidelines and use of priority ordering approach outlined in cl. 6A.23.2(d) of the NER (cl. 2.1(d)(2));
- whether and how the proposed methodology differs from that currently in use (cl. 2.1(r)); and
- whether and how VENCorp will monitor its compliance with its methodology and with Part J of the NER (cl. 2.1(s))

The AER has assessed VENCorp's revised pricing methodology against the final pricing guidelines and the pricing principles. Where the AER, in its draft decision, required further elaboration within the pricing methodology, VENCorp has provided this information in accordance with the final pricing guidelines. VENCorp has made no further changes other than those specified by the AER. Accordingly the AER has approved VENCorp's revised pricing methodology.

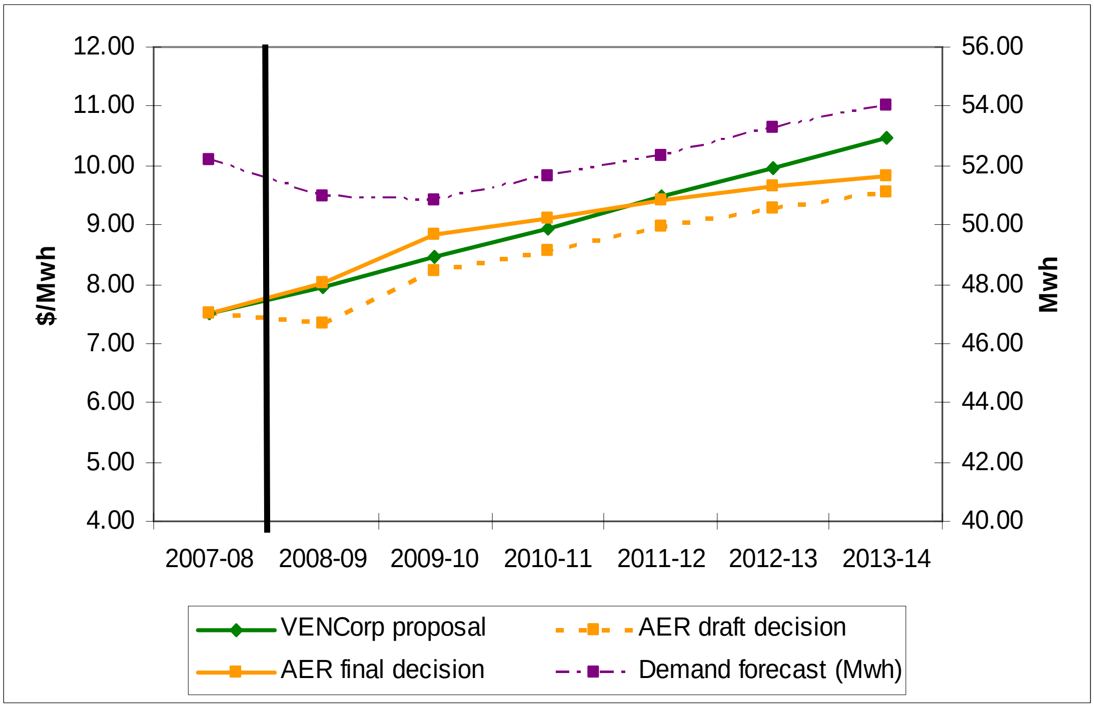
Indicative price impact

For the information of interested parties, this section estimates the expected impact on TUOS charges and end user prices as a result of this final decision. The AER does not determine TUOS charges or end user prices. These estimated outcomes rely on simple assumptions and are provided for illustrative purposes only to highlight the impact of changes to transmission prices.

Each year VENCorp receives settlement residue (approximately $35m p.a.) which offsets its MAAR. For simplicity's sake, these calculations assume, for purposes of illustration, that no settlement residue is received by VENCorp. The following price paths therefore represent a 'true' estimate of transmission costs, but may not reflect the charges that eventuate.

Under this final decision, nominal TUOS charges are expected to increase from $7.50/Mwh in 2007-08 to $9.84/Mwh in 2013-14, an average annual increase of 4.63%.

Figure 3 Indicative TUOS price path ($nominal)

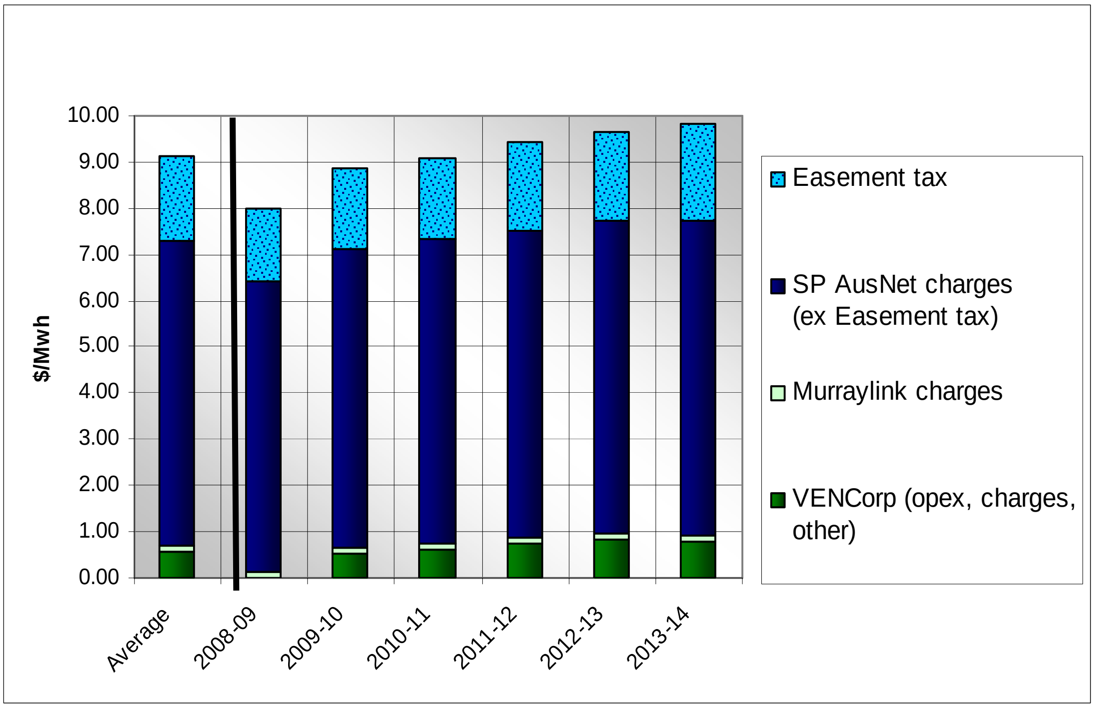


Source: AER analysis, VENCorp EAPR 2007

The following figure breaks the indicative nominal TUOS price path under the recommended decision into its respective components. Of the expected average TUOS charges of $9.15/Mwh:

- $1.85/Mwh relates to easement tax
- $6.58/Mwh relates to SP AusNet prescribed service charges (excluding easement tax)
- $0.14/Mwh relates to Murraylink prescribed service charges
- $0.57/Mwh relates to VENCorp's opex, committed augmentation charges and planned augmentation charges.

Figure 4 Indicative TUOS - components (nominal $m)



Assuming, for the purposes of this illustration, that the average annual bill of a small end user is $1 200, and that transmission costs account for 7% of the total costs for a small end user, the transmission component of an average small end user's annual bill is expected to increase, in nominal terms, from $84 in 2007-08 to $110 in 2013-14. This represents an average annual nominal increase of 4.63%.

Assuming, again for simplicity's sake in this illustration, that non-transmission costs increase by only inflation, a total small end user's annual bill is expected to increase, in nominal terms, from $1 200 in 2007-08 to $1 414 in 2013-14. This represents an average annual nominal increase of 2.78%.

The cost of transmission for an average large user (for illustrative purposes assumed to represent around 23% of an annual bill of $10 m) is expected to increase, in nominal terms, from $2.30 m per year in 2007-08 to $3.02 m in 2013-14. This represents an average annual nominal increase of 4.63% (1.95% real).

Using the same illustrative assumption that non-transmission costs increase by only inflation, a total large end user's annual bill is expected to increase, in nominal terms, from $10.00 m in 2007-08 to $12.02 m in 2013-14. This represents an average annual nominal increase of 3.11% (0.47% real).

1 Introduction

1.1 Background

The Australian Energy Regulator (AER) is responsible for the economic regulation of monopoly transmission services in the National Electricity Market (NEM). These functions were conferred on the AER by the National Electricity Law (NEL) and the National Electricity Rules (NER) on 1 July 2005.

The AER must make transmission determinations for Transmission Network Service Providers (TNSPs) in respect of prescribed and negotiated transmission services in accordance with the NER.

VENCorp's current revenue cap for the five and a half year period from 1 January 2003 to 30 June 2008 was determined by the ACCC in December 2002, and varied in 2004.

VENCorp submitted a revenue proposal and proposed negotiating framework and pricing methodology to the AER on 1 March 2007. The AER released a draft decision on the transmission determination for VENCorp for the 2008-09 to 2013-14 regulatory period on 30 November 2007.

1.2 Regulatory requirements

The requirements for VENCorp's transmission determination are set out in the NER, in chapter 6A and the jurisdictional derogation for Victoria in Chapter 9, Part A (the derogation). Chapter 6A of the NER applies to all TNSPs in the National Electricity Market (NEM).

The application of chapter 6A in respect of the Victorian Transmission Network or a part of the Victorian Transmission Network is subject to the modifications set out in clauses 9.8.4B to 9.8.4F of the derogation. Chapter 6A is not displaced by clauses 9.8.4B to 9.8.4F. The provisions of chapter 6A continue to apply to VENCorp, but are modified by the derogations in chapter 9.

1.2.1 Components of transmission determination

The AER is required to make a transmission determination for a TNSP that includes:

- a revenue determination for the service provider in respect of prescribed transmission services;
- a determination relating to the provider's negotiating framework;
- a determination specifying the negotiated transmission service criteria that apply to the provider; and
- a determination specifying the pricing methodology for prescribed transmission services to apply to the service provider.

1.2.1.1 Revenue determination

The AER's revenue determination for VENCorp is a determination of VENCorp's MAAR in respect of those services for which VENCorp may determine shared transmission network use charges. This compares to revenue determinations for all other TNSPs, which takes the form of the MAR in respect of prescribed transmission services.

Under cl. 9.8.4C(d) and (e)(4), the AER must determine VENCorp's MAAR for a relevant regulatory period. The AER's determination must set out the MAAR for each financial year of the relevant regulatory period.

The derogation requires that:

- the amount of VENCorp's MAAR for a relevant regulatory period must not exceed VENCorp's statutory electricity transmission related costs.
- VENCorp's MAAR must be determined on a full cost recovery but no operating surplus basis.

For the relevant regulatory period, VENCorp's statutory electricity transmission related costs are:

1. VENCorp's aggregate actual costs in operating and planning the Victorian Transmission Network;
2. all network charges payable by VENCorp to SP AusNet or any other owner of the Victorian Transmission Network or a part of the Victorian Transmission Network, including charges relating to augmentations;
3. all other charges payable by VENCorp to providers of network support services and other services which VENCorp uses to provide network services that are transmission services; and
4. any other costs that directly arise out of VENCorp's functions under the *Electricity Industry Act 2000* (Vic) relating to the transmission of electricity, the application of the Rules to VENCorp or the conditions imposed on VENCorp under its transmission licence relating to the transmission of electricity, for which there is no alternative method (legislative or contractual) for the recovery of those costs.

The components of VENCorp's revenue determination differ to the building blocks for other TNSPs.

VENCorp's MAAR is the total of VENCorp's opex, planned augmentation charges, committed augmentation charges and prescribed service charges payable to SP AusNet and Murraylink for the provision of prescribed services by those TNSPs, adjusted for any surplus accumulated in the current regulatory period.

For each year of the relevant regulatory period, VENCorp's total revenue requirement is calculated as:

Operating expenditure

Committed augmentation charges

Planned augmentation charges +

= Total forecast expenditure

Prescribed services charges +

Interest income -

Accumulated surplus (2002-08) -

= Total revenue requirement

If, over the regulatory period, VENCorp's statutory electricity transmission-related costs for a financial year exceed, or VENCorp anticipates they will exceed, the amount of the statutory transmission-related costs for that financial year assumed by the AER in determining VENCorp's MAAR. VENCorp may apply to the AER for an adjustment to its MAAR for each affected financial year in the forthcoming regulatory period of an amount equal to the amount required to ensure that its MAAR complies the principles outlined above.[3] This provision is not symmetrical, in that VENCorp is not required to make an application to the AER should its statutory electricity transmission-related costs be less than VENCorp's MAAR in any financial year.

1.2.2 Negotiating framework

VENCorp must prepare a negotiating framework, setting out the procedure to be followed during negotiations between VENCorp and any person who wishes to receive a negotiated transmission service from VENCorp, as to the terms and conditions of access for provision of the service.

The AER's determination on the negotiating framework must set out any requirements that are to be complied with in respect of the preparation, proposal or operation of VENCorp's negotiating framework.

1.2.3 Negotiated transmission service criteria

The Negotiated Transmission Service Criteria (NTSC) forming part of the transmission determination for VENCorp are the criteria that are to be applied:

1. by VENCorp in negotiating:

- the terms and conditions of access for negotiated transmission services, including the prices that are to be charged for the provision of those services by VENCorp for the relevant regulatory period; and
- any access charges which are negotiated by VENCorp during that regulatory period

2. by a commercial arbitrator in resolving any dispute between VENCorp and a person who wishes to receive a negotiated transmission service, in relation to:

[3] NER, cl. 9.8.4C(g2)

- the terms and conditions of access for the negotiated transmission service, including the price that is to be charged for the provision of that service by VENCorp; and
- any access charges that are to be paid to or by VENCorp.

The NTSC must give effect to and be consistent with the Negotiated Transmission Service Principles as set out in the NER.

1.2.4 Pricing methodology

VENCorp must comply with the pricing methodology approved by the AER, and other applicable requirements in the NER, when setting the prices that may be charged for the provision of prescribed transmission services.

The pricing methodology proposed by VENCorp and approved by the AER must give effect to and be consistent with the pricing principles for prescribed transmission services set out in part J of the NER Further, it must comply with the requirements of, and contain or be accompanied by such information as is required by, the pricing methodology guidelines made for that purpose by the AER.

Chapter 9 modifies the operation of Part J chapter 6A as it applies to VENCorp regarding the pricing for the provision of prescribed transmission services. Under cl. 9.8.4F:

- the allocation of the aggregate annual revenue requirement as determined under cl. 9.8.4C; and
- the allocation of transmission costs and the conversion of those allocated transmission costs to prescribed transmission service prices and charges, as provided for under Part J of chapter 6A

must reflect the arrangements in place in relation to the Victorian Transmission Network or a part of the Victorian Transmission Network under the Electricity Industry Act 2000 (Vic), the Essential Services Commission Act 2001 (Vic) and the Tariff Order.

1.3 Length of regulatory period

A revenue determination must specify the commencement and length of the regulatory period to which it applies. The regulatory period must not be less than five regulatory years. The AER must approve the commencement and length of the regulatory period as proposed by the TNSP on its revenue proposal if the length proposed is five regulatory years, but is not precluded from approving a longer period if that is proposed by the TNSP.

SP AusNet has proposed a six-year regulatory control period commencing on 1 April 2008, and ending on 31 March 2014. In order to be consistent with SP AusNet, VENCorp has also proposed a six-year regulatory period commencing 1 July 2008 to 30 June 2014.

The AER has accepted the proposed duration of the regulatory period to address the issues of regulatory burden identified by SP AusNet.

1.4 Review process

Under the derogations, the process and timing for the making of VENCorp's transmission determination are considerably modified. Chapter 9 provides for an abbreviated, single-stage process for all aspects of VENCorp's transmission determination, with the exception of its pricing methodology. However, in the interests of consistency with the process to be followed by SP AusNet, and to facilitate the input of interested parties, the AER requested, and VENCorp agreed, to submit its proposal on 1 March 2007, at the same time as SP AusNet, enabling the AER to publish and consult on a draft decision in November 2007.

A pre-determination conference was held on 12 December for the purposes of explaining the draft decision and receiving oral submissions from interested parties. The conference was attended by VENCorp. No submissions were made.

VENCorp was given the opportunity to submit a revised proposal addressing matters raised in the draft decision. A revised negotiating framework and pricing methodology were submitted for consideration in this final decision.

Written submissions from VENCorp and other interested parties were invited, but no submissions were received.

2 Maximum allowable aggregate revenue

2.1 Introduction

The AER must determine VENCorp's maximum allowable aggregate revenue for the forthcoming regulatory period.[4] The AER's determination must set out the maximum allowable aggregate revenue for each financial year in that period.[5]

The AER released its draft decision on VENCorp's MAAR on 30 November 2007, rejecting VENCorp's proposed revenue determination, and allowing a revised revenue determination that reflected reductions made to various components of VENCorp's maximum allowable aggregate revenue (MAAR).

This chapter sets out the AER's final decision on VENCorp's revenue determination.

2.2 Issues and AER's considerations

2.2.1 Components of VENCorp's revenue determination

VENCorp's maximum allowable aggregate revenue (MAAR) is the total of VENCorp's operating expenditure (opex), planned augmentation charges, committed augmentation charges and prescribed service charges payable to SP AusNet and Murraylink for the provision of prescribed services by those TNSPs. Together, these components make up VENCorp's statutory electricity transmission related costs.[6]

The amount of VENCorp's MAAR for the forthcoming regulatory period must not exceed its statutory electricity transmission related costs, and must be determined on a full cost recovery, no operating surplus basis.[7] In determining VENCorp's MAAR, the AER must take into account the difference (if any) between the most recent forecast of the revenue that VENCorp will recover by way of shared transmission network use charges and its statutory electricity transmission related costs (ie. VENCorp's accumulated surplus/deficit at the end of the current regulatory period). If there is such a difference, the AER must apply that difference in its determination.[8]

[4] NER, cl. 9.8.4C(d)
[5] NER, cl. 9.8.4C(e)(4)
[6] NER, cl. 9.3.1(2)
[7] NER, cll. 9.8.4C(e)(1), 9.8.4C(a)
[8] NER, cll. 9.8.4C(e)(3)(ii), 9.8.4C(f)

For each year of the relevant regulatory period, VENCorp's total revenue requirement is calculated as:

Operating expenditure

Committed augmentation charges

Planned augmentation charges +

= Total forecast expenditure

Prescribed services charges +

Interest income -

Accumulated surplus (2002-08) -

= Total revenue requirement

The total revenue requirement determined by the AER in this final decision operates as a cap on the revenue that VENCorp may earn in the forthcoming regulatory period.

The appropriate amount of each of these components was considered in the AER's draft decision, in accordance with the requirements of chapter 6A of the NER, as modified by the jurisdictional derogations for Victoria. In a number of respects, the AER was not satisfied that the amounts proposed by VENCorp satisfied the requirements of the NER, and was not able to accept them. For that reason, the AER did not approve VENCorp's proposed MAAR of $2 889.80m (nominal). The basis and rationale for the AER's rejection of VENCorp's proposal was set out in detail in the draft decision, as were its reasons for the substitute amounts allowed for each component, and its calculation of a revised MAAR of $2 713.93m (nominal) that the AER was satisfied complied with the requirements of the NER.

VENCorp did not elect to submit a revised proposal addressing the matters raised in the AER's draft decision, and made no submission in response the draft decision. This aspect of the AER's draft decision attracted no response from interested parties.

The AER's final decision on each component of VENCorp's revenue determination is set out below.

2.2.1.1 Operating expenditure (opex)

VENCorp proposed a total opex forecast of $44m (nominal) for the forthcoming regulatory period. The AER was not satisfied that VENCorp's proposed forecast opex reasonably reflected the opex criteria[9], having regard to the opex factors[10], and in its draft decision rejected the proposed forecast.

The AER's draft decision allowed a substitute forecast of total opex of $39.37m (nominal), which the AER was satisfied reasonably reflected the opex criteria, taking into account the relevant opex factors. In deriving this substitute forecast, the AER:

- accepted VENCorp's proposed base year of 2006-07 as the point from which to forecast its future opex requirements, but replaced the budgeted 2006-07 expenditure included in VENCorp's proposal with its actual expenditure in that year, which became available after the submission of VENCorp's proposal. The

[9] NER, cl. 6A.6.6(c)
[10] NER, cl. 6A.6.6(e)

AER also made a positive adjustment to VENCorp's actual 2006-07 expenditure to remove the effect of a defined superannuation adjustment, which the AER did not consider relevant to VENCorp's future opex requirements; and

- accepted VENCorp's proposed cost escalators of 4.5% (nominal) for labour and 3.0% (nominal) for non-labour costs.

No submissions were received on this aspect of the AER's draft decision. The AER has not been made aware of any reason to depart from this aspect of its draft decision. For the reasons outlined above and in that decision, the AER has therefore determined that total forecast opex of $39.37m (nominal) will be included in VENCorp's MAAR for the forthcoming regulatory period.

Table 2.1 Final decision: opex ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
VENCorp's proposal	6.69	6.98	7.17	7.47	7.71	7.98	**44.00**
AER adjustment	-0.70	-0.78	-0.74	-0.80	-0.80	-0.81	-4.63
Draft decision	5.99	6.20	6.43	6.67	6.91	7.17	**39.37**
AER adjustment	-	-	-	-	-	-	-
Final decision	5.99	6.20	6.43	6.67	6.91	7.17	**39.37**

2.2.1.2 Committed augmentation charges

VENCorp proposed an allowance of $148.0m (nominal) for committed augmentation charges in its MAAR, to reflect the expected cost of charges payable by VENCorp under contracts for network augmentations entered into in and prior to the current regulatory period. This forecast of committed augmentation charges was derived from VENCorp's budgeted network payments for 2008-09, the first year of the forthcoming regulatory period, inflated by an assumed CPI of 3% per annum for the remaining years of the regulatory period.

The AER was not satisfied that this forecast reasonably reflected a realistic expectation of the charges that VENCorp would incur in the 2008-14 regulatory period[11], and rejected the proposed allowance. The substitute allowance approved in the AER's draft decision reflected two adjustments to VENCorp's proposal:

- In reviewing VENCorp's proposal the AER identified, and VENCorp confirmed, a number of errors in the form of inappropriate inclusion and exclusion of contracts in VENCorp's calculation of budgeted 2008-09 network payments. VENCorp's 2008-09 forecast of committed augmentation charges was reduced as a result from $22.9m (nominal) to $19.35m.
- While it did not consider VENCorp's proposed 3% escalator was justified on the basis of inflation alone, the AER concluded that an assumed increase of 3% per annum was not an unrealistic expectation when considered in the context of the uncertainty surrounding potential contract variations within the regulatory period

[11] NER, cl. 6A.6.6(c)(3)

and the inflation adjustments to contracts within the regulatory period, and allowed the escalation on that basis.

The $125.16m (nominal) forecast of committed augmentation charges approved in the AER's draft decision was $22.84m lower than that in VENCorp's proposal. By correcting for the overstatement of charges payable in 2008-09, the AER was satisfied that this amount reasonably reflected a realistic expectation of the charges VENCorp is likely to incur in the forthcoming regulatory period under contracts entered into during and prior to the current regulatory period.

For the reasons outlined above and in its draft decision, and in the absence of any submissions on this matter, the AER's final decision is that a forecast of $125.16m (nominal) will be included in VENCorp's MAAR for the forthcoming regulatory period.

Table 2.2 Final decision: committed augmentation charges ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
VENCorp's proposal	22.9	23.6	24.3	25.0	25.7	26.5	**148.00**
AER adjustment	-.355	-3.67	-3.77	-3.86	-3.92	-4.07	-22.84
Draft decision	19.35	19.93	20.53	21.14	21.78	22.43	**125.16**
AER adjustment	-	-	-	-	-	-	**-**
Final decision	19.35	19.93	20.53	21.14	21.78	22.43	**125.16**

2.2.1.3 Forecast planned network augmentation expenditure and charges

VENCorp plans and procures augmentation services under contract from SP AusNet and other owners of Victorian electricity transmission assets. For the purposes of the AER's determination of VENCorp's MAAR, a forecast of the contract charges that will be payable in the relevant regulatory period is derived on the basis of an indicative planned augmentation expenditure forecast (forecast planned augmentation expenditure). The forecast contract charges expected to flow from this expenditure are referred to as VENCorp's forecast planned augmentation charges. It is forecast planned augmentation charges, rather than the forecast planned augmentation expenditure underlying it, that form the building block in VENCorp's MAAR. This component of VENCorp's MAAR represents planned augmentation charges payable by VENCorp within the forthcoming regulatory period, under contracts expected to be entered into in that period.

VENCorp's proposal

VENCorp proposed a forecast of planned augmentation expenditure of $288.16m ($2007-08), from which it derived a forecast of planned augmentation charges totalling $63.21 (nominal) over the six years of the forthcoming regulatory period using a methodology developed for this purpose on the basis of past contract experience. This methodology:

- depreciates the approved forecast planned augmentation expenditure using a straight line methodology over an assumed asset life of 30 years;
- applies a nominal vanilla WACC (in the draft decision, this was the indicative WACC of 8.85% applied in the AER's draft decision on SP AusNet's transmission determination for the same period);
- applies an inflation forecast (in the draft decision, this was a forecast of 3%); and
- adds an allowance of 1.5% of capital costs for the opex likely to be incurred on the capital component of forecast planned augmentations

Draft decision

On the balance of the available information, the AER was not satisfied that the forecast of $288.16m of planned augmentation expenditure proposed by VENCorp reasonably reflected the criteria established in the NER.[12]

In particular:

- VENCorp did not appear to have considered the inter-dependencies between its forecast planned augmentation projects and allowances;
- in forecasting planned augmentation expenditure VENCorp did not appear to have fully considered the impact of SP AusNet's replacement program on augmentation timing and requirements;
- the project documentation provided by VENCorp to support its forecast planned augmentation expenditure was limited, especially with respect to technical data and cost analysis; and
- the assumptions in VENCorp's indicative probabilistic forecasting approach, which is typically only used to develop an outlook for years six to ten of a ten year planning period, mean that there is likely to be systemic advancement in the timing of expenditure forecast in its revenue proposal.

In undertaking its assessment of VENCorp's proposed forecast planned network augmentation expenditure in accordance with the NER, the AER had regard, where relevant, to the capex factors listed at cl. 6A.6.7(e). In forming conclusions with respect to specific elements of VENCorp's proposal, the AER considered:

- the information presented by VENCorp in and accompanying its revenue proposal and reconciliation with the 2007 EAPR (cl. 6A.6.7(e)(1))
- submissions from interested parties received in the course of consulting on VENCorp's revenue proposal (cl. 6A.6.7(e)(2))
- the AER's own analysis, as outlined in this draft decision, and the analysis and recommendations of PB and Nuttall Consulting (cl. 6A.6.7(e)(3))
- benchmark capex that would be incurred by an efficient TNSP in the circumstances of VENCorp over the regulatory control period (cl. 6A.6.7(e)(4))
- VENCorp's actual and expected augmentation during the current regulatory period (cl. 6A.6.7(e)(5)).

[12] NER, cl. 6A.6.7(c)

Given that VENCorp's opex is forecast on corporate related costs, the relative prices of operating and capital inputs (cl. 6A.6.7(e)(6)) and the substitution possibilities between opex and capex (cl. 6A.6.7(e)(7)) had little, if any, bearing upon the draft decision.

The AER's adjustments to VENCorp's forecast planned augmentation expenditure amounted to a total reduction of $87.38m (approximately 30%) to VENCorp's proposal. The AER's draft decision allowed a forecast of $200.78m ($2007-08) of planned augmentation expenditure for the forthcoming regulatory period.

Having rejected VENCorp's forecast of planned augmentation expenditure, the AER could not be satisfied that the forecast of planned augmentation charges derived from VENCorp's $288m forecast of planned augmentation expenditure, reasonably reflected a realistic expectation of the charges that VENCorp will actually incur. If included in the calculation of VENCorp's MAAR, such a forecast was likely to result in a MAAR that exceeds VENCorp's statutory electricity transmission related costs and therefore fails to satisfy the principles set out in cl. 9.8.4C(a) of the derogation. Under cl. 6A.6.7(d) of the NER the AER could not, in these circumstances, accept VENCorp's total forecast planned network augmentation charges.

The AER was therefore required under cl. 6A.14.1(2)(ii) to provide an estimate of the total forecast planned augmentation charges that VENCorp will require over the forthcoming regulatory period which the AER was satisfied reasonably reflected the capital expenditure criteria, taking into account the capex factors.

To derive a forecast of planned augmentation charges from the approved underlying expenditure forecast, the AER applied the methodology submitted by VENCorp for this purpose.

On the basis of this calculation, the AER's draft decision allowed a total forecast of planned augmentation charges of $46.18m (nominal) for the 2008-14 regulatory period.

Final decision

The AER received no submissions on the forecast of planned augmentation charges allowed in its draft decision, or on the underlying forecast of planned augmentation expenditure.

On 31 January 2008, the AER published its final transmission determination for SP AusNet. In place of the indicative WACC of 8.85% applied in its draft decision, the final transmission determination applied a nominal vanilla WACC of 9.76% and 10 year inflation forecast of 2.59%.

As in its draft decision, the AER considers it appropriate to use a consistent WACC for SP AusNet and VENCorp. The AER has therefore recalculated its forecast of planned augmentation charges using the same methodology, but applying a nominal vanilla WACC of 9.76%.

The AER has also updated the forecast inflation used in its draft decision, applying the methodology set out in its final decision for SP AusNet. To derive an estimate of inflation over a 10 year period, the AER has applied the average of the Reserve Bank of Australia's (RBA) short-term inflation forecasts, which currently extend out to two years, and adopted the mid-point of the RBA's target range (2.5%) for the remaining eight years. An implied 10-year forecast of 2.63% per annum was derived by averaging these individual forecasts.

Table 2.3 Final decision – forecast inflation (%)

	June 2009	June 2010	June 2011	June 2012	June 2013	June 2014	June 2015	June 2016	June 2017	June 2018	Average
Forecast inflation	3.25	3.00	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.63

Source: RBA, *Statement on monetary policy*, 11 February 2008, p. 55.

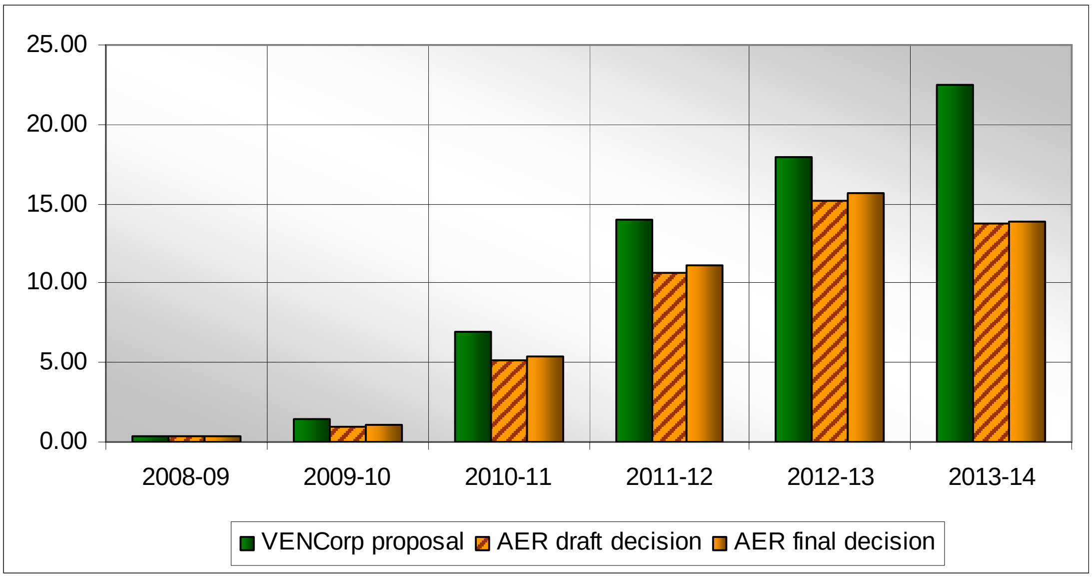
No other changes to this calculation have been made. This revision affects only the forecast of planned augmentation charges, and has no impact on the underlying forecast of planned augmentation expenditure.

The AER approves the inclusion of forecast planned augmentation charges of $47.45m (nominal) in VENCorp's MAAR for the forthcoming regulatory period. This is a small increase of $1.27m (or 2.75%) from the draft decision, which is attributable solely to the SP AusNet final decision.

Table 2.4 Final decision - planned augmentation charges ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
VENCorp's proposal	0.36	1.45	6.89	14.00	17.98	22.53	63.21
AER adjustment	0.01	-0.44	-1.73	-3.33	-2.73	-8.81	-17.03
AER draft decision	0.37	1.01	5.16	10.67	15.25	13.72	46.18
AER adjustment	0.02	0.05	0.26	0.41	0.42	0.11	1.27
AER final decision	**0.39**	**1.06**	**5.42**	**11.09**	**15.67**	**13.82**	**47.45**

Figure 2.1 Final decision – planned augmentation charges ($nominal)



2.2.1.4 Prescribed services charges — SP AusNet and Murraylink

Prescribed service charges are payments made by VENCorp to SP AusNet and Murraylink for the provision of prescribed transmission services.

The AER's draft decision allowed a forecast of $2 534.41m (nominal) in prescribed service charges payable by VENCorp to SP AusNet and Murraylink over the forthcoming regulatory period.

The forecast of prescribed service charges payable to SP AusNet was calculated on the following key assumptions put forward in VENCorp's proposal and accepted by the AER:

- 85% of SP AusNet's non-easement tax maximum allowed revenue (MAR) is recovered through VENCorp; and
- 100% of SP AusNet's easement tax is recovered through VENCorp

The forecast of prescribed services charges payable to Murraylink was calculated on the basis of an agreement between VENCorp and ElectraNet, under which 55% of Murraylink's MAR is recovered through VENCorp.

Murraylink prescribed services charges

VENCorp's proposed forecast of prescribed service charges payable to Murraylink appeared to have been based on the ACCC's 2003 decision on Murraylink's revenue cap.[13] The AER rejected this forecast, which did not reasonably reflect the charges expected to be incurred by VENCorp in the forthcoming regulatory period as required by the NER, and made the following adjustments to derive a compliant forecast:

[13] ACCC, *Decision – Murraylink Transmission Company Application for Conversion and Maximum Allowed Revenue*, 1 October 2003.

- The 2003 revenue cap on which VENCorp's forecast of charges was based was revoked and substituted in 2004.[14] The forecast of prescribed service charges payable to Murraylink approved in the draft decision was calculated on the basis of the substituted revenue cap approved by the ACCC on 1 April 2004.
- As VENCorp's forthcoming regulatory period extends one year beyond the period to which Murraylink's revenue cap relates, the AER was required to make an assumption about Murraylink's MAR for the first year beyond its current regulatory period. The AER adopted the x factor and forecast inflation rate in the Murraylink decision to make this extrapolation.

On this basis the AER approved the inclusion of $43.24m (nominal) in VENCorp's MAAR for forecast prescribed service charges payable to Murraylink.

There has been no change to Murraylink's revenue cap in the period between the AER's draft decision and this final decision, and no submissions were received on this matter.

The AER therefore maintains its draft decision on forecast prescribed services charges payable to Murraylink, and approves the inclusion of $43.24m (nominal) in VENCorp's MAAR.

Table 2.5 Final decision - Murraylink prescribed services charges ($m, nominal)

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	TOTAL
Murraylink	7.06	7.11	7.17	7.24	7.30	7.36	**43.24**

SP AusNet prescribed services charges

Prescribed service charges payable to SP AusNet comprise the majority of VENCorp's prescribed service charges forecast. VENCorp's forecast was based on SP AusNet's original revenue proposal. The AER, in its draft decision on SP AusNet's revenue determination, did not accept SP AusNet's proposal in its entirety. The AER therefore rejected VENCorp's proposal and updated the forecast of prescribed service charges payable to SP AusNet to reflect the SP AusNet draft decision. In doing so the AER noted that these charges would need to be updated again after the release of the AER's final decision on SP AusNet, should the final decision differ from the draft decision.

The draft decision also corrected for the difference in regulatory years between SP AusNet and VENCorp, which VENCorp did not do in its proposal. In making this correction the AER was required to make an assumption about SP AusNet's MAR for the first year beyond its forthcoming regulatory control period. The AER adopted the x factor and forecast inflation rate in the SP AusNet draft decision to make this extrapolation. The AER also assumed that SP AusNet's charges are applied uniformly over each year.

[14] ACCC, *Revocation and substitution of revenue cap*, letter to Murraylink Transmission Company, 1 April 2004.

At the time of the draft decision, the forecast of prescribed services charges payable to SP AusNet was necessarily based on the total MAR of $2 793.97m (nominal), and the forecast easement tax of $516.25m ($2007-08) in the AER's draft decision on SP AusNet's transmission determination.

The AER's final decision on SP AusNet's transmission determination approved a higher MAR of $2979.21m (nominal), and a higher easement tax forecast of $520.85m ($2007-08). As previously noted, the SP AusNet final decision also contained a 10 year inflation forecast of 2.59%. In order to allow VENCorp to recover the costs of prescribed service charges payable to SP AusNet, the forecast of those charges must be updated to reflect the final decision.

For the purposes of this final decision, the AER has recalculated the forecast of prescribed service charges payable to SP AusNet to reflect the final decision on SP AusNet's transmission determination, using the same assumptions applied in the draft decision.

Table 2.6 Final decision - SP AusNet prescribed services charges - components ($m, nominal)

(Year ending 30 June)	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	Total
Charges (ex Easement tax)*	319.97	327.41	339.51	347.10	359.94	367.64	2 061.57
Easement tax**	81.02	88.88	91.85	100.76	104.13	114.22	580.87
Total charges	**401.00**	**416.29**	**431.36**	**447.86**	**464.07**	**481.86**	**2 642.44**

* Recovery of non-easement tax MAR from VENCorp at 85%
** Recovery of forecast easement tax from VENCorp at 100%

The difference between the forecast of SP AusNet prescribed service charges in the draft decision and the revised calculations is a total of $151.26m (nominal), as shown in the table below:

Table 2.7 Final decision: SP AusNet prescribed services charges ($m, nominal)

(Year ending 30 June)	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	TOTAL
Draft decision	**366.51**	**385.04**	**403.68**	**424.12**	**444.65**	**467.17**	**2 491.17**
Adjustment	34.49	31.25	27.68	23.74	19.42	14.69	151.26
Final decision	**401.00**	**416.29**	**431.36**	**447.86**	**464.07**	**481.86**	**2 642.44**

Total prescribed services charges

The AER's draft decision made a downward adjustment of $70.09m (nominal) to VENCorp's total forecast prescribed service charges, noting that this adjustment would need to be updated to reflect differences (if any) between the SP AusNet draft and final decisions.

The AER has recalculated its forecast of prescribed service charges payable to SP AusNet to reflect its final decision on SP AusNet's transmission determination, and approves the inclusion of total forecast prescribed service charges of $2 685.67m (nominal) in VENCorp's MAAR for the forthcoming regulatory period.

The resultant total forecast of prescribed service charges is a total of $2 685.67m (nominal) over the six years of the regulatory period.

Table 2.8 Final decision - total prescribed services charges Murraylink and SP AusNet ($nominal)

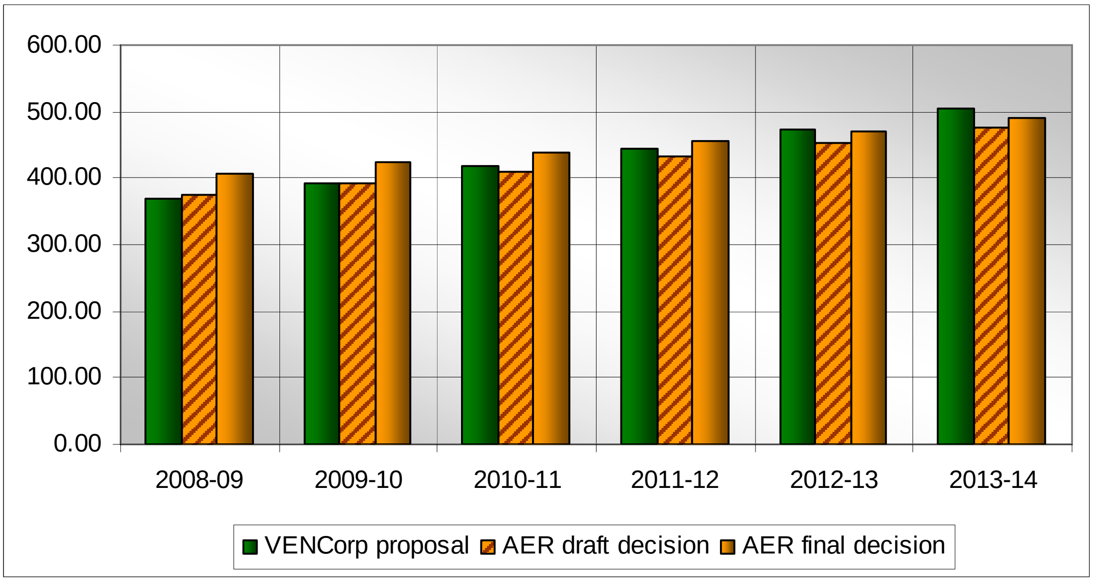
(Year ending 30 June)	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	TOTAL
Murraylink	7.06	7.11	7.17	7.24	7.30	7.36	43.24
SP AusNet	401.00	416.29	431.36	447.86	464.07	481.86	2 642.44
Total prescribed services charges	408.05	423.40	438.54	455.09	471.37	489.22	2,685.67

This is an increase of $151.26m (or 6%) from the draft decision, attributable solely to the SP AusNet final decision. This increase is necessary to ensure that the forecast of prescribed service charges payable by VENCorp to SP AusNet reasonably reflects a realistic expectation of the costs the VENCorp will incur in the forthcoming regulatory period.

Table 2.9 Final decision - total prescribed services charges ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
VENCorp proposal	370.00	393.50	418.60	445.20	473.50	503.70	**2604.50**
AER adjustment	3.57	-1.34	-7.74	-13.85	-21.56	-29.17	-70.09
AER draft decision	373.57	392.16	410.86	431.35	451.94	474.53	**2534.41**
AER adjustment	34.49	31.25	27.68	23.74	19.42	14.69	151.26
AER final decision	408.05	423.40	438.54	455.09	471.37	489.22	**2,685.67**

Figure 2.2 Final decision - total prescribed services charges ($nominal)



2.2.1.5 Other adjustments to VENCorp's MAAR

Interest income

In its draft decision the AER accepted VENCorp's proposal to reduce the sum of VENCorp's forecast opex, committed augmentation charges, planned augmentation charges and prescribed service charges by $1m (nominal), in each year, to account for the interest income VENCorp expects to earn annually during its forthcoming regulatory period. The deduction of forecast interest income from VENCorp's forecast statutory electricity transmission-related costs is important to ensure that VENCorp's MAAR is determined on a full cost recovery and no operating surplus basis.

No submissions were received on this adjustment. The AER therefore maintains its draft decision that VENCorp's total forecast expenditure in each year of the regulatory period will be reduced by $1m (nominal).

Table 2.10 Final decision - interest income ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
Interest income	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	**-6.00**

Accumulated surplus

Clause 9.8.4C(e)(iii) of the NER requires the AER to take into account any expected accumulated surplus or deficit from the current regulatory period in determining VENCorp's MAAR for the forthcoming regulatory period.

At the time it set its 2007-08 transmission charges, the AER understands that VENCorp was expecting an accumulated surplus of $26.61m (nominal) at the end of 2006-07. On this basis, VENCorp set its 2007-08 transmission charges with the aim of achieving a deficit of that amount, and an accumulated surplus/deficit of zero at the end of that year. VENCorp's proposal therefore assumed an accumulated surplus of zero at the end of the current regulatory period.

VENCorp's financial accounts, which became available after its proposal was submitted, indicated that at the end of 2006-07 VENCorp had an accumulated surplus of $49.8m (nominal), instead of the expected $26.61m. This appears to be the result of VENCorp receiving significantly more settlement residue than expected. The deficit of $26.61m built into VENCorp's transmission charges for 2007-08 is insufficient to offset this, and VENCorp is now expected to have an accumulated surplus of $25.19m (nominal) at the end of the current regulatory period.

The AER's draft decision deducted the full amount of VENCorp's expected 2007-08 accumulated surplus ($25.19m, nominal) from its MAAR in 2008-09. This approach was based on the AER's understanding of the approach that VENCorp itself follows annually in setting its transmission charges.

The AER received no submissions on this matter, and VENCorp has provided no new information in relation to the amount of the surplus. The AER has therefore determined that the same adjustment of $25.19m (nominal) will be made to the 2008-09 MAAR determined for VENCorp in this final decision.

Table 2.11 Final decision - accumulated surplus ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
Accumulated surplus	-25.19	-	-	-	-	-	**-25.19**

Availability incentive scheme

VENCorp's proposal erroneously included an annual allowance of $6m in its proposed MAAR for rebates payable by SP AusNet under the Availability Incentive Scheme (AIS) in the network services agreement between SP AusNet and VENCorp. This was corrected in the AER's draft decision. The same correction has been made in this final decision.

2.3 AER's conclusion

Taking into account its conclusions on each component of VENCorp's MAAR, as set out in the sections above, the AER has determined VENCorp's MAAR for each financial year of the forthcoming regulatory period.

Table 2.12 Final decision – MAAR (nominal $m)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
Operating expenditure	5.99	6.20	6.43	6.67	6.91	7.17	39.37
Committed augmentation charges	19.35	19.93	20.53	21.14	21.78	22.43	125.16
Planned augmentation charges	0.39	1.06	5.42	11.09	15.67	13.82	47.45
Total VENCorp expenditure	**25.72**	**27.19**	**32.38**	**38.90**	**44.36**	**43.42**	**211.98**
Prescribed services charges	408.05	423.40	438.54	455.09	471.37	489.22	2685.67
minus Interest income	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-6.00
minus Accumulated surplus	-25.19						-25.19
MAAR	**407.59**	**449.60**	**469.92**	**492.99**	**514.73**	**531.64**	**2866.46**

Source: AER analysis

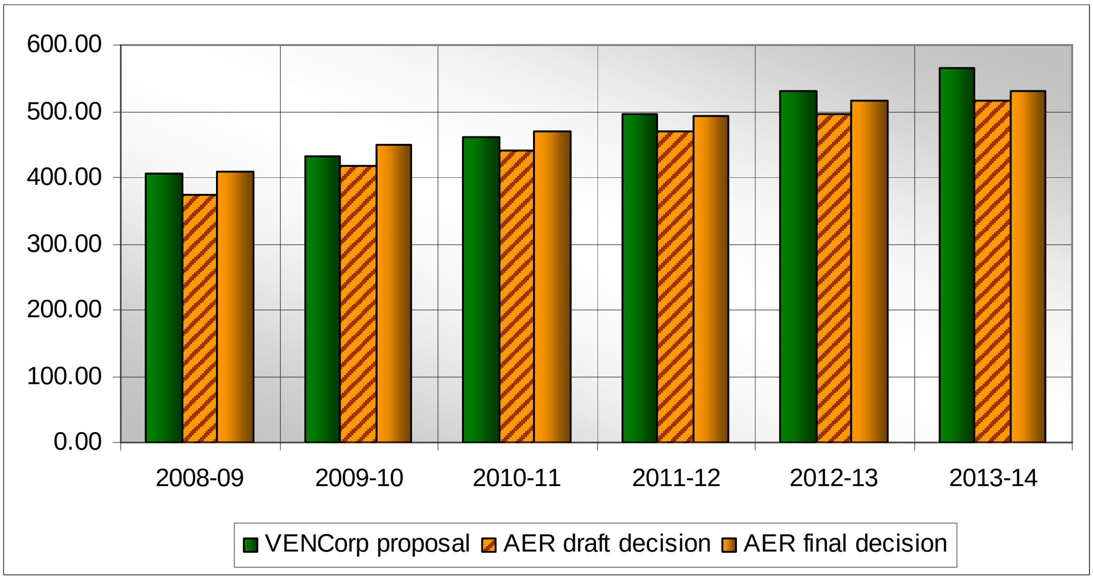
The resultant MAAR is a total of $2 866.46m (nominal) over the six years of the regulatory period. This is an increase of $152.53m (or 5.62%) from the draft decision, attributable predominately to the SP AusNet final decision.

Total adjustments in each year of the regulatory period are shown in the table and figure below.

Table 2.13 Final decision – MAAR, adjustment from draft decision ($nominal)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
VENCorp proposal	**405.00**	**430.50**	**462.00**	**496.70**	**529.90**	**565.70**	**2889.80**
AER adjustment	-31.92	-12.20	-20.02	-27.86	-35.02	-48.85	-175.87
AER draft decision	**373.08**	**418.30**	**441.98**	**468.84**	**494.88**	**516.85**	**2713.93**
AER adjustment	34.51	31.30	27.93	24.15	19.84	14.80	152.53
AER final decision	**407.59**	**449.60**	**469.92**	**492.99**	**514.73**	**531.64**	**2,866.46**

Figure 2.3 Final decision – MAAR, adjustment from draft decision ($nominal)



3 Negotiating framework

3.1 Introduction

The AER's transmission determination for VENCorp must include a determination relating to VENCorp's negotiating framework.

The negotiating framework details the minimum procedures to be followed by VENCorp in determining the terms and conditions of access to negotiated services with a service applicant. Where an access dispute occurs between VENCorp and a service applicant, a commercial arbitrator must have regard to the negotiating framework when settling the dispute.

The AER must approve VENCorp's revised proposed negotiating framework if it meets the requirements set out in cl. 6A.9.5 (c).[15]

The negotiating framework is relevant only to the provision of negotiated services. The pricing of prescribed transmission services is covered by the pricing methodology discussed in chapter 5 of this final decision.

3.2 Draft decision and revised proposal

In its draft decision, the AER assessed VENCorp's proposed negotiating framework against the requirements of cl. 6A.9.5(c) of the NER.

The AER determined that VENCorp's proposed negotiating framework was, in one respect, not compliant with the NER.

VENCorp's proposed negotiating framework required service applicants to pay a fee of $15 000 upon application for access to a negotiated service. This fee was to cover costs associated with processing such an application. The AER required insertion of a clause into VENCorp's negotiating framework stating that where costs are less than $15 000, the difference will be refunded to the service applicant. This amendment was required before the proposed framework could be considered compliant with the NER and approved by the AER.

In response to the draft decision, VENCorp submitted a revised proposed negotiating framework implementing the changes required by the AER.

3.3 Issues and AER considerations

VENCorp has resubmitted its negotiating framework with the amendments required by the AER in its draft decision.

VENCorp has not made further changes to its revised proposed negotiating framework. The information contained in and accompanying the framework does not differ in any respect from that provided in or accompanying the previous framework.

[15] As specified in cl 6A.14.3 (f)

No submissions were received from other parties in relation to this aspect of the draft decision or VENCorp's revised proposed negotiating framework.

3.4 AER's conclusion

For the reasons set out in chapter 6 of the AER's draft decision, the AER has determined that VENCorp's revised proposed negotiating framework, amended as required by that decision, satisfies the requirements of the NER. The AER therefore approves VENCorp's revised proposed negotiating framework.

The AER has determined that VENCorp's revised proposed negotiating framework, which is set out in section 2 of the transmission determination published with this final decision will apply to VENCorp for the regulatory period 1 July 2008 to 30 June 2014. At the conclusion of that period, VENCorp may propose amendments to its negotiating framework when it submits its proposal to the AER for the following period.

4 Negotiated transmission service criteria

4.1 Introduction

The NER require a transmission determination by the AER to include negotiated transmission service criteria (negotiating criteria) applicable to VENCorp for the relevant regulatory period.[16] Unlike other components of a revenue determination, VENCorp is not required to submit proposed negotiating criteria to the AER. Instead, the AER must determine the negotiating criteria in accordance with the NER.

The negotiating criteria must give effect to, and be consistent with, the negotiated transmission service principles set out in cl. 6A.9.1. The negotiated transmission service criteria, set out in the revenue determination, will be applied:[17]

- by the TNSP in negotiating the terms and conditions of access for negotiated transmission services; and
- by a commercial arbitrator in resolving any dispute between a TNSP and a person wishing to receive a negotiated transmission service.

4.2 Issues and AER considerations

The negotiating criteria set out in the draft decision gave effect to, and were consistent with the negotiated transmission service principles,[18] as required by cl. 6A.9.4 (b). In accordance with cl. 6A.11.3, the AER published its proposed criteria for consultation prior to the release the draft decision.[19] The criteria included in the draft decision were determined with regard to submissions received from interested parties.[20]

No submissions were received from VENCorp or other interested parties in relation to the negotiating criteria set out in the draft decision.

4.3 AER's conclusion

The AER sees no cause to alter the negotiating criteria set out in its draft decision.

The negotiated transmission service criteria set out in section 3 of the transmission determination published with this final decision will apply to VENCorp for the forthcoming regulatory period.

[16] NER, cl. 6A.2.2(3)
[17] NER, cl. 6A.9.4(a)
[18] Principles contained in the NER, cl. 6A.9.1
[19] Draft decision published 30 November 2007
[20] ibid., p. 131

5 Pricing methodology

5.1 Introduction

In Victoria, VENCorp is responsible for the pricing of prescribed TUOS services and prescribed common transmission services. As part of its transmission determination the AER is required to assess the pricing methodology proposed by VENCorp.

The NER require that a TNSP's proposed pricing methodology must give effect to and be consistent with the Pricing Principles for Prescribed Transmission Services, and comply with the requirements of, and contain or be accompanied by such information as is required by, the pricing methodology guidelines made for that purpose under rule 6A.25.[21]

5.2 Draft decision and revised proposal

VENCorp's initial proposed pricing methodology was developed under the agreed interim pricing methodology guidelines published on 16 February 2007. The final pricing guidelines were published on 30 October 2007.[22] As permitted by the agreed interim arrangements, VENCorp elected to have the AER assess its pricing methodology against the final guidelines.[23]

In its draft decision, the AER determined that VENCorp's proposed pricing methodology was not compliant with the requirements of the final pricing methodology guidelines. This was largely because the methodology contained references to the interim guidelines, rather than final guidelines. As required by the NER, the draft decision included details of the changes required or matters to be addressed before the AER will approve the proposed methodology.

In order to achieve compliance with the NER, the AER required these references to be updated, and also required further information on certain aspects of the methodology. This further information included:

- an explanation of how the value of 'additional assets' will be calculated as it affects attributable cost shares (cl. 2.1(d)(1)(A));
- compliance with cl. 2.4 of the guidelines and use of priority ordering approach outlined in cl. 6A.23.2(d) of the NER (cl. 2.1(d)(2));
- whether and how the proposed methodology differs from that currently in use (cl. 2.1(r)); and
- whether and how VENCorp will monitor its compliance with its methodology and with Part J of the NER (cl. 2.1(s)).

In response to the draft decision, VENCorp submitted a revised proposed pricing methodology with the following additional information:

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[21] NER cl. 6A.10.1(e)
[22] Final Electricity transmission network service providers Pricing methodology guidelines October 2007
[23] As permitted by cl. 2.3 (a) of the interim pricing guidelines.

- a clause verifying that the cost of 'additional assets' will be calculated using an ORC methodology, as required by cl. 2.1(d)(1)(A);
- statements that the priority ordering approach will be used where assets are attributable to both the prescribed TUOS services and prescribed common transmission service categories, as required by cl. 2.1(d)(2);
- an explanation of how the methodology proposed for the 2008-16 period differs from that currently in place, as required by cl. 2.1(r); and
- a section on how it intends to monitor compliance with Part J of the NER, as required by cl. 2.1(s).

The revised methodology also refers to the requirements of the AER's final pricing guidelines rather than the agreed interim requirements.

5.3 Issues and AER considerations

As noted above, the draft decision set out the changes required or matters to be addressed in VENCorp's proposed pricing methodology before it could be approved under the NER. Where VENCorp's revised proposed pricing methodology contains the changes made by the AER, or otherwise adequately addresses the matters that prompted the AER to require those changes, the AER must approve the revised pricing methodology.[24]

No submissions were received from other parties in relation to this aspect of the draft decision or VENCorp's revised proposed pricing methodology.

The AER has assessed VENCorp's revised pricing methodology against the final pricing guidelines and the pricing principles, and is satisfied that the requirements of the draft decision have been satisfied, such that the revised proposed pricing methodology is now compliant with the requirements of the NER and the pricing guidelines. VENCorp has made only those changes specified by the AER, and the information contained in and accompanying the methodology does not differ in any respect from that provided in or accompanying the previous methodology.

5.4 AER's conclusion

The AER has determined that VENCorp's revised pricing methodology satisfies the requirements of the NER and the pricing guidelines. The AER therefore approves VENCorp's revised proposed pricing methodology.

The AER has determined that VENCorp's revised proposed pricing methodology, which is set out in section 4 of the transmission determination published with this final decision, will apply to VENCorp for the forthcoming regulatory period 1 July 2008 to 30 June 2014. VENCorp may propose amendments to its pricing methodology when it submits its proposal to the AER for the following regulatory period.

[24] NER cl. 6A.14.3 (h)