AUSTRALIAN ENERGY REGULATOR

Draft decision: TasNetworks 2019–24

We have made a draft revenue decision for TasNetworks, the electricity transmission and distribution network operator in Tasmania. Our draft decision allows TasNetworks to recover $2095.8 million ($nominal) from its transmission and distribution customers over five years commencing 1 July 2019.

Estimated impact on customer bills

The revenue we determine affects the distribution and transmission component of a customer's electricity bill. TasNetworks' network charges make up around 46 per cent of the electricity bill paid by residential customers in Tasmania.

We estimate that under our draft decision for transmission and distribution networks, the average annual residential electricity bill in the first year of the 2019–24 period would be 0.6 per cent lower than the current 2018–19 level (in nominal terms).

In dollar terms, we estimate the overall impact for residential customers is an $80 increase in the electricity bill over the five year period (in nominal terms). For small business customers, we estimate the overall impact is a $254 ($nominal) increase in the electricity bill over the five year period (in nominal terms).

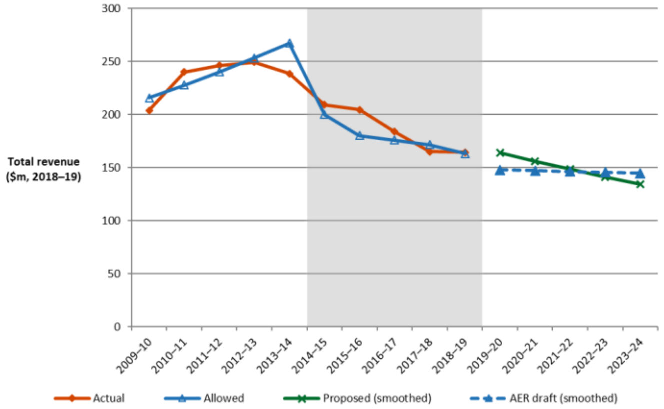
Overview

We, the Australian Energy Regulator (AER), regulate the revenues of TasNetworks by setting the total revenue it may recover from its customers.

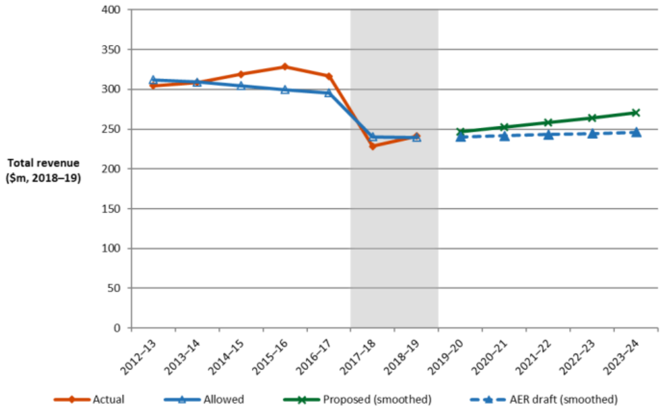
Although TasNetworks has submitted joint regulatory proposals for its distribution and transmission networks, we must undertake separate assessments and make separate transmission and distribution determinations.

Our draft decisions result in a relatively flat revenue path over the 2019–24 regulatory control period compared to TasNetworks' proposal (in real terms). This is the combined effect of our separate transmission and distribution determinations as reflected in the figures below–our transmission revenue will fall in the first year and then remain largely constant for subsequent years, whereas, our distribution revenue provides a relatively flat revenue impact each year of the 2019–24 regulatory control period.

TasNetworks' past and proposed total revenue and AER draft decision revenue allowance for transmission ($million, 2018–19)



TasNetworks' past and proposed total revenue and AER draft decision revenue allowance for distribution ($million, 2018–19)



Our draft decision allows TasNetworks to recover $787.5 million ($nominal) in transmission revenue, and $1308.3 million in distribution revenue in the next period. This is a 1.5 per cent reduction from TasNetworks' proposed revenue recovery of $799.6 million ($nominal) for transmission and a 6.1 per cent reduction from the proposed distribution revenue recovery of $1392.7 ($nominal).

Key elements of our draft decision

We have made a number of adjustments that result in a lower revenue requirement. The key differences between our draft decision and TasNetworks' proposal are the return on its investments (rate of return) and the value of imputation credits (gamma), and the forecast capital expenditure (capex). The rate of return is a forecast of the costs of funds a network business requires to invest in the network. Capex refers to TasNetworks' investment to build or upgrade its fixed assets (such as its lines and transformers).

Our draft decision is to accept TasNetworks' forecast transmission and distribution opex– the forecast operating, maintenance and other non-capital costs incurred in providing network services.

TasNetworks will now have the opportunity to respond to our concerns in its revised proposal. We will continue to work with TasNetworks and stakeholders to ensure that our final decision is in the long term interests of consumers and that TasNetworks' customers are paying no more than they should for safe and reliable electricity.

Rate of return and gamma

The biggest contributor to the difference between our draft decision and TasNetworks' proposal is our proposed change to the rate of return (and therefore the return on capital). The rate of return is a forecast of the costs of funds a network business requires to invest in the network. TasNetworks' proposal applied a rate of return of 5.89 per cent for both transmission and distribution.

Our draft decision rate of return for transmission is 5.77 per cent (nominal vanilla, indicative) and for distribution is 5.51 per cent (nominal vanilla, indicative), for the first year of the 2019–24 regulatory control period.

These are a placeholder, subject to change because:

- we estimated our draft decision allowed rate of return using the approach set out in our draft 2018 rate of return guidelines and consultation on this is ongoing, and expected to conclude in December 2018
- there will be updates with more recent data at key milestones throughout this review (TasNetworks' revised proposal and our final decision).

Our draft decision is to maintain the current transition paths for TasNetworks' transmission and distribution networks and not align the two as proposed by TasNetworks. This is consistent with our 2018 rate of return guideline draft decision to apply a consistent rate of return and transition approach to all networks.

Further, our draft decision is to apply a value of imputation credits (gamma) of 0.5 as reflected in our 2018 rate of return guideline draft decision.

Capital expenditure

TasNetworks' proposed a 23 per cent increase in transmission capex from its average capex in the current period to $260.0 million ($2018–19). Our draft decision transmission capex allowance is $222.6 million ($2018–19).

For distribution, TasNetworks' proposed a 29 per cent increase in capex from its average capex in the current period to $734.4 million ($2018–19). Our draft decision distribution capex allowance is $550.9 million ($2018–19).

We have not accepted TasNetworks' proposed capex because we are not currently satisfied that all of TasNetworks' forecast capex represents an efficient level of expenditure that needs to proceed in the next period. We have made reductions to TasNetworks' network replacement and distribution non-network expenditure (e.g. spending on information and communication technology)

It is important to note that the capital expenditure we allow TasNetworks could change in our final decision, based on responses from TasNetworks and other stakeholders.

TasNetworks also proposed five transmission contingent projects to address uncertain future investment, including the potential for a second Bass Strait interconnector. At this stage, based on the information before us, we do not consider the projects are probable to occur in the 2019–24 regulatory control period. TasNetworks has the opportunity to provide further supporting information for the contingent projects in its revised proposal.

Next steps

TasNetworks' revised regulatory proposal is due 29 November 2018. We will assess this proposal and it could lead to significant differences between our draft and final decision.

Stakeholders may make written submissions on our draft decision and TasNetworks' revised proposal by 11 January 2019. Our final decision is due for release by the end of April 2019.

More information on TasNetworks' proposal, our draft decision and how to make a submission is on our website: www.aer.gov.au.