

 DRAFT DECISION

Powerlink transmission determination

 2017−18 to 2021−22

Attachment 1 – Maximum allowed revenue

September 2016

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1. Note
2. This attachment forms part of the AER's draft decision on Powerlink's transmission determination for 2017–22. It should be read with all other parts of the draft decision.
3. The draft decision includes the following documents:
4. Overview
5. Attachment 1 – Maximum allowed revenue
6. Attachment 2 – Regulatory asset base
7. Attachment 3 – Rate of return
8. Attachment 4 – Value of imputation credits
9. Attachment 5 – Regulatory depreciation
10. Attachment 6 – Capital expenditure
11. Attachment 7 – Operating expenditure
12. Attachment 8 – Corporate income tax
13. Attachment 9 – Efficiency benefit sharing scheme
14. Attachment 10 – Capital expenditure sharing scheme
15. Attachment 11 – Service target performance incentive scheme
16. Attachment 12 – Pricing methodology
17. Attachment 13 – Pass through events
18. Attachment 14 – Negotiated services

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1. Shortened forms

| Shortened form | Extended form |
| --- | --- |
| 1. AARR
 | 1. aggregate annual revenue requirement
 |
| 1. AEMC
 | 1. Australian Energy Market Commission
 |
| 1. AEMO
 | 1. Australian Energy Market Operator
 |
| 1. AER
 | 1. Australian Energy Regulator
 |
| 1. ASRR
 | 1. annual service revenue requirement
 |
| 1. augex
 | 1. augmentation expenditure
 |
| 1. capex
 | 1. capital expenditure
 |
| 1. CCP
 | 1. Consumer Challenge Panel
 |
| 1. CESS
 | 1. capital expenditure sharing scheme
 |
| 1. CPI
 | 1. consumer price index
 |
| 1. DMIA
 | 1. demand management innovation allowance
 |
| 1. DRP
 | 1. debt risk premium
 |
| 1. EBSS
 | 1. efficiency benefit sharing scheme
 |
| 1. ERP
 | 1. equity risk premium
 |
| 1. MAR
 | 1. maximum allowed revenue
 |
| 1. MRP
 | 1. market risk premium
 |
| 1. NEL
 | 1. national electricity law
 |
| 1. NEM
 | 1. national electricity market
 |
| 1. NEO
 | 1. national electricity objective
 |
| 1. NER
 | 1. national electricity rules
 |
| 1. NSP
 | 1. network service provider
 |
| 1. NTSC
 | 1. negotiated transmission service criteria
 |
| 1. opex
 | 1. operating expenditure
 |
| 1. PPI
 | 1. partial performance indicators
 |
| 1. PTRM
 | 1. post-tax revenue model
 |
| 1. RAB
 | 1. regulatory asset base
 |
| 1. RBA
 | 1. Reserve Bank of Australia
 |
| 1. repex
 | 1. replacement expenditure
 |
| 1. RFM
 | 1. roll forward model
 |
| 1. RIN
 | 1. regulatory information notice
 |
| 1. RPP
 | 1. revenue and pricing principles
 |
| 1. SLCAPM
 | 1. Sharpe-Lintner capital asset pricing model
 |
| 1. STPIS
 | 1. service target performance incentive scheme
 |
| 1. TNSP
 | 1. transmission network service provider
 |
| 1. TUoS
 | 1. transmission use of system
 |
| 1. WACC
 | 1. weighted average cost of capital
 |

# Maximum allowed revenue

This attachment sets out the AER's draft decision on the maximum allowed revenue (MAR) for the provision of prescribed transmission services for each year of Powerlink's 2017–22 regulatory control period. Specifically, the attachment addresses:[[1]](#footnote-1)

* the estimated total revenue cap, which is the sum of the annual expected MAR
* the annual building block revenue requirement
* the annual expected MAR
* the X factor.

We determine the TNSP's annual building block revenue requirement using a building block approach. We determine the X factors by smoothing the annual building block revenue requirement over the regulatory control period. The X factor is used in the CPI–X methodology to determine the annual expected MAR (smoothed).

## Draft decision

We do not accept Powerlink’s proposed annual building block revenue requirement, annual expected MAR and total revenue cap. For the reasons discussed in the attachments to this draft determination, our decisions on Powerlink’s proposed building block costs have a consequential impact on its annual building block revenue requirement. We have calculated the X factor and the annual expected MAR (smoothed) to reflect our draft decision on Powerlink’ annual building block revenue requirement.

We determine a total annual building block revenue requirement for Powerlink of $3724.2 million ($ nominal) for the 2017–22 regulatory control period. This is a reduction of $297.9 million ($ nominal) or 7.4 per cent to Powerlink’ proposal and reflects the impact of our draft decisions on the various building block costs.

As a result of our smoothing of the annual building block revenue requirement, our draft decision on the annual expected MAR and X factor for each regulatory year of the 2017–22 regulatory control period is set out in table 1.1. Our draft decision is to approve an estimated total revenue cap of $3720.8 million ($ nominal) for Powerlink for the 2017–22 regulatory control period. Our approved X factor for 2018–19 to 2021–22 is 0.15 per cent per annum.[[2]](#footnote-2)

Table 1.1 sets out our draft decision on Powerlink’s annual building block revenue requirement, the X factor, the annual expected MAR and the estimated total revenue cap for the 2017–22 regulatory control period.

Table .1 AER's draft decision on Powerlink’s annual building block revenue requirement, annual expected MAR, estimated total revenue cap and X factor ($ million, nominal)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|   | 2017–18 | 2018–19 | 2019–20 | 2020–21 | 2021–22 | Total |
| Return on capital | 392.3 | 396.1 | 399.3 | 401.8 | 404.0 | 1993.5 |
| Regulatory depreciationa | 93.4 | 108.2 | 125.1 | 136.6 | 142.5 | 605.8 |
| Operating expenditureb | 201.7 | 205.8 | 209.8 | 214.2 | 219.3 | 1050.7 |
| Revenue adjustmentsc | –0.8 | –7.1 | –3.2 | 3.0 | 0.0 | –8.1 |
| Net tax allowance | 11.7 | 14.2 | 17.7 | 19.2 | 19.3 | 82.2 |
| Annual building block revenue requirement(unsmoothed)d | 698.3 | 717.2 | 748.8 | 774.8 | 785.1 | 3724.2 |
| **Annual expected MAR (smoothed)** | **710.8** | **727.1** | **743.8** | **760.9** | **778.3** | **3720.8**c |
| X factor (%)e | n/af | 0.15% | 0.15% | 0.15% | 0.15% | n/a |

Source: AER analysis.

(a) Regulatory depreciation is straight-line depreciation net of the inflation indexation on the opening RAB.

(b) Operating expenditure includes debt raising costs.

(c) Includes efficiency benefit sharing scheme amounts.

(d) The estimated total revenue cap is equal to the total annual expected MAR.

(e) The X factors will be revised to reflect the annual return on debt update. Under the CPI–X framework, the X factor measures the real rate of change in annual expected revenue from one year to the next. A negative X factor represents a real increase in revenue. Conversely, a positive X factor represents a real decrease in revenue.

(f) Powerlink is not required to apply an X factor for 2017–18 because we set the 2017–18 MAR in this decision. The MAR for 2017–18 is around 32.6 per cent lower than the approved MAR for 2016–17 in real terms, or 30.9 per cent lower in nominal terms.

## Powerlink’s proposal

Powerlink proposed a total (smoothed) revenue cap of $4017.2 million ($ nominal) for the 2017–22 regulatory control period.

Table 1.2 sets out Powerlink’s proposed annual building block revenue requirement, the X factor, the annual expected MAR and the estimated total revenue cap.

Table .2 Powerlink’s proposed annual building block revenue requirement, annual expected MAR, estimated total revenue cap and X factor ($ million, nominal)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|   | 2017–18 | 2018–19 | 2019–20 | 2020–21 | 2021–22 | Total |
| Return on capital | 437.2 | 444.0 | 449.8 | 454.7 | 459.2 | 2244.8 |
| Regulatory depreciationa | 94.3 | 110.4 | 128.9 | 141.3 | 148.2 | 623.2 |
| Operating expenditureb | 201.7 | 205.8 | 209.8 | 214.2 | 219.3 | 1050.7 |
| Revenue adjustmentsc | –0.8 | –7.1 | –3.2 | 3.0 | 0.0 | –8.1 |
| Net tax allowance | 18.9 | 19.7 | 23.2 | 24.7 | 25.0 | 111.5 |
| Annual building block revenue requirement(unsmoothed)d | 751.3 | 772.7 | 808.6 | 837.9 | 851.6 | 4022.1 |
| **Annual expected MAR (smoothed)** | **767.4** | **785.0** | **803.0** | **821.5** | **840.3** | **4017.2** |
| X factor (%) | n/af | 0.15% | 0.15% | 0.15% | 0.15% | n/a |

Source: Powerlink, Revenue proposal, January 2016, p. 101.

(a) Regulatory depreciation is straight-line depreciation net of the inflation indexation on the opening RAB.

(b) Operating expenditure includes debt raising costs.

(c) Includes efficiency benefit sharing scheme amounts.

(d) The estimated total revenue cap is equal to the total annual expected MAR

(f) Powerlink is not required to apply an X factor for 2017–18 because we set the 2017–18 MAR in this decision.

## Assessment approach

In this section, we describe the building block approach used to determine the TNSP’s expected MAR. We also set out the annual revenue adjustment to be applied to Powerlink’s MAR over the 2017–22 regulatory control period.

### The building block approach

The MAR is calculated using the post-tax revenue model (PTRM).[[3]](#footnote-3) The PTRM must be such that the expected MAR for each year of the regulatory control period is equal to the net present value (NPV) of the annual building block revenue requirement for the TNSP for each year, and the total revenue cap is the sum of the MARs for each year.[[4]](#footnote-4) In turn, the annual building block revenue requirement must be determined using a building block approach.[[5]](#footnote-5) Therefore, we adopt a building block approach when making our decision on a TNSP's total revenue cap and expected MAR for each regulatory year of the regulatory control period. Under this approach we determine the value of the building block costs that make up the annual building block revenue requirement for each regulatory year. These building block costs are set out in section 1.3.2.

We developed the PTRM, which brings together the various building block costs and calculates the annual building block revenue requirement for each year of the regulatory control period.[[6]](#footnote-6) The PTRM also calculates the X factors required under the CPI–X methodology which is used to escalate the MAR for each year (other than the first year) of the regulatory control period.[[7]](#footnote-7) Using the X factors and annual building block revenue requirement, the annual expected MAR (smoothed) is forecast for each year of the regulatory control period. A TNSP’s revenue proposal must be prepared using our PTRM.[[8]](#footnote-8)

The annual building block revenue requirement can be lumpy over the regulatory control period. To minimise price shocks, revenues are smoothed within a regulatory control period while maintaining the principle of cost recovery under the building block approach. Smoothing requires diverting some of the cost recovery to adjacent years within the regulatory control period so that the NPV of the annual expected MAR (smoothed revenues) is equal to the NPV of the annual building block revenue requirement (unsmoothed revenues). That is, a smoothed profile of the expected MAR is determined for the regulatory control period under the CPI–X methodology.

The expected MAR for the first year is generally set equal to the annual building block revenue requirement for the first year of the regulatory control period. It may be appropriate to set the expected MAR for the first year to align with the MAR from the last year of the previous regulatory control period to avoid any large revenue variation between periods (or P0):[[9]](#footnote-9)

 MAR1 = AR1 or MARL

where:

 MAR1 = the maximum allowed revenue for year 1 of the next regulatory control period

 AR1 = the annual building block revenue requirement for year 1 of the next regulatory control period

 MARL ~ the maximum allowed revenue for the last year of the previous regulatory control period.

To enable the formula for the annual revenue adjustment process (discussed below in section 0) to operate correctly, we will refer to the MAR determined in this decision using the building block costs as the allowed revenue (AR). This is because the expected MAR determined using the building block costs do not incorporate performance incentive scheme revenue adjustments and pass through amounts that may apply to each regulatory year.

In this determination we first calculate annual building block revenue requirements for each year of the 2017–22 regulatory control period. To do this we consider the various costs facing the TNSP and the trade-offs and interactions between these costs, service quality and across years. This reflects the AER's holistic assessment of the TNSP's proposal.

We understand the trade-offs that occur between building block costs and test the sensitivity of these costs to their various driver elements. These trade-offs are discussed in the interrelationships section of the various attachments to this draft decision and are reflected in the calculations made in the PTRM developed by the AER.[[10]](#footnote-10) Such understanding allows the AER to exercise judgement in determining the final inputs into the PTRM and the annual building block revenue requirements that result from this modelling.

Having determined the total annual building block revenue requirement for the
2017–22 regulatory control period, the annual building block revenue requirements for each regulatory year are smoothed across that period to reduce revenue variations between years and to come up with the expected MAR for each year. This is done through the determination of the X factors.[[11]](#footnote-11) The X factors must equalise (in NPV terms) the total expected revenue cap to be earned by the TNSP with the total building block revenue requirement for the 2017–22 regulatory control period.[[12]](#footnote-12) The X factor must minimise, as far as reasonably possible, the variance between the expected MAR and annual building block revenue requirement for the last regulatory year of the period.[[13]](#footnote-13) We therefore consider a divergence of up to 3 per cent between the expected MAR and annual building block revenue requirement for the last year of the regulatory control period is reasonable, if this can promote smoother price changes over the regulatory control period.

The building block costs (and the elements that drive those costs) used to determine the unsmoothed annual building block revenue requirements are set out below.

### The building block costs

The efficient costs to be recovered by a TNSP can be thought of as being made up of various building block costs. Our draft decision assesses each of the building block costs and the elements that drive these costs. The building block costs are approved reflecting trade-offs and interactions between the cost elements, service quality and across years.

Table 1.3 shows the building block costs that form the annual building block revenue requirement for each year and where discussion on the elements that drive these costs can be found within this draft decision.

Table .3 Building block costs

|  |  |
| --- | --- |
| Building block costs | Attachments where elements are discussed |
| Return on capital | Regulatory asset base (attachment 2)Capex (attachment 6)Rate of return (attachment 3) |
| Regulatory depreciation (return of capital) | Regulatory asset base (attachment 2)Capex (attachment 6)Depreciation (attachment 5) |
| Operating expenditure (opex) | Opex (attachment 7) |
| Efficiency benefits/penalties | Efficiency benefit sharing scheme (attachment 9) |
| Estimated cost of corporate tax | Corporate income tax (attachment 8)Value of imputation credits (attachment 4) |
| Adjustment for shared assets | Maximum allowed revenue (attachment 1) |

Source: AER analysis.

### Annual revenue adjustment process

The PTRM incorporates an expected inflation rate to calculate the expected MAR (excluding performance incentive scheme revenue adjustments and pass through amount that may apply to each regulatory year) in nominal dollar terms, whereas the actual MAR for each year is adjusted for actual inflation. As discussed in the return on debt appendix of attachment 3,[[14]](#footnote-14) we will update Powerlink’s return on debt annually. This means the actual MAR for each year will also be adjusted for revised X factors after the annual return on debt update. This annual revenue adjustment process is set out below.

The MAR for the subsequent year of the regulatory control period requires an annual adjustment based on the previous year’s allowed revenue.[[15]](#footnote-15) That is, the subsequent year’s allowed revenue is determined by adjusting the previous year’s allowed revenue for actual inflation and the X factor determined after the annual return on debt update:

|  |  |  |
| --- | --- | --- |
| ARt | = |  |

where:

|  |  |  |
| --- | --- | --- |
| AR | = | the allowed revenue |
| t | = | time period/financial year (for t = 2 (2018–19), 3 (2019–20), 4 (2020–21), 5 (2021–22)) |
| **∆CPI** | = | the annual percentage change in the ABS Consumer price index all groups, weighted average of eight capital cities from December in year t – 2 to December in year t – 1[[16]](#footnote-16) |
| **X** | = | the smoothing factor determined in accordance with the PTRM as approved in the AER's final decision, and annually revised for the return on debt update in accordance with the formula specified in the return on debt appendix[[17]](#footnote-17) calculated for the relevant year. |

The MAR is determined annually in accordance with the NER by adding to (or deducting from) the allowed revenue:

* the service target performance incentive scheme revenue increment (or revenue decrement)[[18]](#footnote-18)
* any approved pass through amounts.[[19]](#footnote-19)

Table 1.4 sets out the timing of the annual calculation of the AR and performance incentive:

|  |  |  |
| --- | --- | --- |
| **MAR***t* | = | (allowed revenue) + (performance incentive) + (pass through) |
|  | = |  |

where:

|  |  |  |
| --- | --- | --- |
| **MAR** | = | the maximum allowed revenue |
| **AR** | = | the allowed revenue |
| **S** | = | the revenue increment or decrement determined in accordance with the service target performance incentive scheme |
| **P** | = | the pass through amount (positive or negative) that the AER has determined in accordance with clauses 6A.7.2 and 6A.7.3 of the NER |
| ***t*** | = | time period/financial year (for t = 2 (2018–19), 3 (2019–20), 4 (2020–21), 5 (2021–22)) |
| ***ct*** | = | time period/calendar year (for t = 2 (2017), 3 (2018), 4 (2019), 5 (2020)). |

Under the NER, a TNSP may also adjust the MAR for under or over-recovery amounts.[[20]](#footnote-20) That is, the revenue amounts recovered higher or lower than the approved MAR for each year would be included in the subsequent year's MAR. In the case of an under-recovery, the amount would be added to the future year's MAR. In the case of an over-recovery, the amount would be subtracted from the future year's MAR.

Table .4 Timing of the calculation of allowed revenues and the performance incentive for Powerlink

|  |  |  |  |
| --- | --- | --- | --- |
| t | Allowed revenue (financial year) | ct | Performance incentive (calendar year) |
| 2 | 1 July 2018– 30 June 2019 | 2 | 1 January 2017– 31 December 2017 |
| 3 | 1 July 2018– 30 June 2020 | 3 | 1 January 2018– 31 December 2018 |
| 4 | 1 July 2018– 30 June 2021 | 4 | 1 January 2019– 31 December 2019 |
| 5 | 1 July 2018– 30 June 2022 | 5 | 1 January 2020– 31 December 2020 |

Note: The performance incentive for 1 January 2016–31 December 2016 is to be applied to the AR determined for
2017–18 (AR1).

### Average transmission charges

The NER does not require an estimate of transmission charges for a revenue determination of a TNSP. Nonetheless, we typically provide some indicative transmission charges (and the resulting impact on annual electricity bills) flowing from the revenue determination as discussed in section 1.4.3. Although we assess Powerlink’s proposed pricing methodology as part of this determination, actual transmission charges established at particular connection points are not determined by us. Powerlink establishes the transmission charges in accordance with its approved pricing methodology and the NER.[[21]](#footnote-21)

## Reasons for draft decision

We determine a total annual building block revenue requirement of $3724.2 million ($ nominal) for Powerlink for the 2017–22 regulatory control period. This compares to Powerlink’s proposed total annual building block revenue requirement of $4022.1 million ($ nominal) for this period.

Figure 1.1 shows the building block components from our determination that make up the annual building block revenue requirement for Powerlink, and the corresponding components from its proposal.

The most significant changes to Powerlink's proposal include:

* a reduction in the return on capital allowance of 11.2 per cent (attachments 2 and 3)
* a reduction in the regulatory depreciation allowance of 2.8 per cent (attachment 5)
* a reduction in the capex allowance of 19.4 per cent (attachment 6)
* a reduction in the cost of corporate income tax allowance of 26.2 per cent (attachment 8).

Figure .1 AER's draft decision and Powerlink’s proposed annual building block revenue requirement ($ million, nominal)



Source: AER analysis.

### X factor, annual expected MAR and estimated total revenue cap

For this draft decision, we determine an X factor for Powerlink of 0.15 per cent per annum for the four years of the regulatory control period from 2018–19 to 2021–22.[[22]](#footnote-22) The NPV of the annual building block revenue requirement is $3172.2 million ($ nominal) as at 1 July 2017. Based on this NPV and applying the CPI–X method, we determine that the annual expected MAR (smoothed) for Powerlink increases from $710.8 million in 2017–18 to $778.3 million in 2021–22 ($ nominal). The resulting estimated total revenue cap for Powerlink is $3720.8 million for the 2017–22 regulatory control period.

Figure 1.2 shows our draft decision on Powerlink’s annual expected MAR (smoothed revenue) and the annual building block revenue requirement (unsmoothed revenue) for the 2017–22 regulatory control period.

Figure .2 AER's draft decision on Powerlink’s annual expected MAR (smoothed) and annual building block revenue requirement (unsmoothed) ($ million, nominal)



Source: AER analysis.

To determine the expected MAR for Powerlink, we have set the MAR for the first regulatory year at $710.8 million ($ nominal) which is $12.5 million higher than the annual building block revenue requirement. We then applied a CPI of 2.45 per cent per annum and an X factor of 0.15 per cent per annum to determine the expected MAR in subsequent years.[[23]](#footnote-23) We consider that our profile of X factors results in an expected MAR in the last year of the regulatory control period that is as close as reasonably possible to the annual building block revenue requirement for that year.[[24]](#footnote-24)

The average decrease in our approved expected MAR is 4.4 per cent per annum ($ nominal) over the 2017–22 regulatory control period.[[25]](#footnote-25) This consists of an initial decrease of 30.9 per cent from 2016–17 to 2017–18, followed by average annual increases of 2.3 per cent during the remainder of the 2017–22 regulatory control period.[[26]](#footnote-26) Our draft decision results in a decrease of 28.9 per cent in real terms ($2016–17) to Powerlink’s average annual allowed revenue relative to that in the 2012–17 regulatory control period. This decrease is primarily because of a lower rate of return, capex and corporate income tax allowance applied in this draft decision for the 2017–22 regulatory control period than were approved in the 2012–17 determination.

Figure 1.3 compares our draft decision building blocks for Powerlink’s 2017–22 regulatory control period with Powerlink’s proposed revenue requirement for the same period, and the approved revenue for the 2012–17 regulatory control period.

Figure .3 Annual average of AER's draft decision building blocks compared to Powerlink’s proposed revenue requirement and approved revenue for 2012–17 ($ million, 2016–17)



Source: AER analysis.

### Shared assets

Service providers, such as Powerlink, may use assets to provide both prescribed transmission services we regulate and unregulated services. These assets are called 'shared assets'.[[27]](#footnote-27) Of the unregulated revenues a service provider earns from shared assets, 10 per cent will be used to reduce the service provider's prices for prescribed transmission services.[[28]](#footnote-28)

Shared asset revenue reductions are subject to a materiality threshold. Unregulated use of shared assets is material when a service provider's unregulated revenues from shared assets in a specific regulatory year are expected to be greater than 1 per cent of its MAR for that regulatory year.[[29]](#footnote-29)

Powerlink submitted its shared asset unregulated revenues are forecast to be 0.4 per cent of its proposed total revenues in each year of the 2017–22 regulatory control period.[[30]](#footnote-30) Powerlink therefore proposed no reduction in its total revenues for each year of that period.

We consider Powerlink’s forecasts are reasonable, based on its reporting of historical shared assets revenue and our assessment of this revenue source for other service providers.[[31]](#footnote-31) However, Powerlink’s forecast unregulated revenues must be compared to the regulated revenues we determine, rather than those proposed by Powerlink. Our draft decision sets lower expected MARs than Powerlink’s proposal, so we estimate that the unregulated revenues will be between 0.37 per cent to 0.41 per cent of its expected MARs in each year of the 2017–22 regulatory control period. Hence, the materiality threshold is not met in any year of the 2017–22 regulatory control period and we do not apply a shared asset revenue adjustment.

1. We note unregulated revenues from shared assets may in future become material.[[32]](#footnote-32) We will monitor Powerlink's shared asset unregulated revenues for future regulatory control periods.

### Indicative transmission charges and impact on electricity bills

Our draft decision on Powerlink's expected MAR ultimately affects the annual electricity bills paid by customers in Queensland. There are several steps required to translate our revenue decision into indicative transmission charges, and then to estimate bill impact.

Since we regulate Powerlink's prescribed transmission services under a revenue cap, changes in the consumption of electricity will affect the transmission charges ultimately paid by consumers. We estimate the indicative effect of our draft decision on forecast average transmission charges in Queensland by:

* taking Powerlink's annual expected MAR determined in this draft decision, and
* dividing it by the forecast annual energy delivered in Queensland.[[33]](#footnote-33)

Based on this approach, we estimate that this draft decision will result in a decrease in annual average transmission charges from 2016–17 to 2021–22.[[34]](#footnote-34) Figure 1.4 shows the indicative average transmission charges resulting from this draft decision compared with the average transmission charges from 2012 to 2017 in nominal dollar terms. The average transmission charges are forecast to decrease from around $19.6 per MWh in 2016–17 to $14.4 per MWh in 2021–22.

Figure .4 Indicative transmission price path from 2012–13 to 2021–22 for Queensland ($/MWh, nominal)



Source: AER analysis.

We then estimate the indicative impact of transmission charges on electricity bills. In Queensland, transmission charges represent approximately 9.3 per cent on average of a typical residential customer's annual electricity bill.[[35]](#footnote-35) This small percentage largely explains the relatively modest average annual electricity bill impacts arising from our draft decision. We expect that our draft decision—other things being equal—will result in average residential customer's annual electricity bill in Queensland decrease moderately over the 2017–22 regulatory control period.

The transmission component of the average residential customer's annual electricity bill in 2021–22 is expected to reduce by about $40 ($ nominal) or 2.5 per cent below the 2016–17 level. By comparison, had we accepted Powerlink’s proposal, the expected transmission component of the average annual residential electricity bill in 2021–22 would decrease by approximately $31 ($ nominal) or 1.9 per cent below the 2016–17 level.

Our estimated potential impact is based on the typical annual electricity usage of 5173 kWh per annum for a residential customer in Queensland.[[36]](#footnote-36) Customers with different usage will experience different changes in their bills. We also note that there are other factors, such as distribution network costs, wholesale and retail costs, which affect electricity bills.

Similarly, for small business customers in Queensland—for which transmission charges represent approximately 9.3 per cent of a typical annual electricity bill—we have estimated the bill impact for two customer categories:[[37]](#footnote-37)

* Small business customers consuming 10 000 kWh per annum
* Small business customers consuming 20 000 kWh per annum.

We expect our draft decision will result in the transmission component of the average annual electricity bill for the small business customer with consumption of 10 000 kWh per annum in 2021–22 to reduce by about $75 ($ nominal) or 2.5 per cent below the 2016–17 level. By comparison, had we accepted Powerlink's proposal, the expected transmission component of the average annual electricity bill for this type of small business customer in 2021–22 would decrease by approximately $58 ($ nominal) or 1.9 per cent below the 2016–17 level. Likewise, the transmission component of the average annual electricity bill for the small business customer with annual consumption of 20 000 kWh per annum in 2021–22 is expected to be about $130 ($ nominal) or 2.5 per cent below the 2016–17 level as a result of our draft decision. By comparison, had we accepted Powerlink's proposal, the expected transmission component of the average annual electricity bill for this type of small business customer in 2021–22 would decrease by approximately 102 ($ nominal) or 1.9 per cent below the 2016–17 level.

Table 1.5 shows our estimated impact of this draft decision over the 2017–22 regulatory control period compared with Powerlink's proposal on the average annual electricity bills for residential and small business customers in Queensland.

Table .5 AER's estimated impact of our final decision and Powerlink’s proposal on the average annual electricity bills for the 2017–22 regulatory control period ($ nominal)

|  | 2016–17 | 2017–18 | 2018–19 | 2019–20 | 2020–21 | 2021–22 |
| --- | --- | --- | --- | --- | --- | --- |
| **AER draft decision** |   |   |   |   |   |   |
| Residential annual bill | 1611a | 1562 | 1564 | 1566 | 1569 | 1571 |
| Annual changec |   | -49 (-3.1%) | 2 (0.1%) | 2 (0.1%) | 3 (0.2%) | 2 (0.1%) |
| Small business with 10 000 kWh consumption annual bill | 3014b | 2921 | 2925 | 2930 | 2935 | 2939 |
| Annual changec |   | -93 (-3.1%) | 4 (0.1%) | 4 (0.1%) | 6 (0.2%) | 4 (0.1%) |
| Small business with 20 000 kWh consumption annual bill | 5249b | 5088 | 5094 | 5102 | 5111 | 5119 |
| Annual changec |   | -161 (-3.1%) | 7 (0.1%) | 7 (0.1%) | 10 (0.2%) | 7 (0.1%) |
| **Powerlink proposal** |   |   |   |   |   |   |
| Residential annual bill | 1611a | 1570 | 1572 | 1574 | 1578 | 1580 |
| Annual changec |   | -41 (-2.6%) | 2 (0.1%) | 2 (0.2%) | 3 (0.2%) | 2 (0.1%) |
| Small business with 10 000 kWh consumption annual bill | 3014b | 2936 | 2941 | 2945 | 2951 | 2956 |
| Annual changec |   | -78 (-2.6%) | 4 (0.1%) | 5 (0.2%) | 6 (0.2%) | 4 (0.1%) |
| Small business with 20 000 kWh consumption annual bill | 5249b | 5114 | 5121 | 5129 | 5139 | 5147 |
| Annual changed |   | -135 (-2.6%) | 7 (0.1%) | 8 (0.2%) | 10 (0.2%) | 8 (0.1%) |

Source: AER analysis; AEMC, 2015 Residential electricity price trends, December 2015, p. 105; and Powerlink, Revenue proposal, PTRM, January 2016.

(a) Based on Powerlink, Revenue proposal, Consolidated Reset RIN, January 2016, checked against offers at June 2016 from the [Energy Made Easy](http://www.energymadeeasy.gov.au) website (postcode:4000, 4810) using consumption of 5173 kWh per annum.

(b) Based on Powerlink, Revenue proposal, Consolidated Reset RIN, January 2016.

(c) Annual change amounts and percentages are indicative. They are derived by varying the transmission component of 2016–17 bill amounts in proportion to yearly expected revenue divided by Powerlink's forecast demand. Actual bill impacts will vary depending on electricity consumption and tariff class.

1. NER, cll. 6A.4.2(a)(1)–(3), 6A.5.3(c) and 6A.6.8. [↑](#footnote-ref-1)
2. Powerlink is not required to apply an X factor for 2017–18 because we set the 2017–18 MAR in this decision. [↑](#footnote-ref-2)
3. NER, cll.6A.5.1 and 6A.5.3. [↑](#footnote-ref-3)
4. NER, cll. 6A.5.3(c)(1) and (4). [↑](#footnote-ref-4)
5. NER, cl. 6A.5.4. [↑](#footnote-ref-5)
6. NER, cl. 6A.5. [↑](#footnote-ref-6)
7. NER, cll. 6A.5.3 and 6A.6.8. [↑](#footnote-ref-7)
8. NER, cl. 6A.5.1(a). [↑](#footnote-ref-8)
9. The MAR for year 1 of the next regulatory control period may include adjustment for the performance incentive that applied during the previous regulatory control period, and under or over recovery adjustments from previous regulatory years. [↑](#footnote-ref-9)
10. There are trade-offs that are not modelled in the PTRM but are reflected in the inputs to the PTRM. For example, service quality is not explicitly modelled in the PTRM, but the trade-offs between service quality and price are reflected in the forecast capex and opex inputs to the model. Other trade-offs are obvious from the calculations in the PTRM. For example, while someone may expect a lower regulatory asset base to also lower revenues, the PTRM shows that this will not occur if the reduction in the regulatory asset base is due solely to an increase in the depreciation rate. In such circumstances, revenues increase as the increased depreciation allowance more than offsets the reduction in the return on capital caused by the lower regulatory asset base. [↑](#footnote-ref-10)
11. NER, cl. 6A.6.8(a). [↑](#footnote-ref-11)
12. NER, cl. 6A.6.8(c)(1). [↑](#footnote-ref-12)
13. NER, cl. 6A.6.8(c)(2). [↑](#footnote-ref-13)
14. Please see appendix B of attachment 3 for details. [↑](#footnote-ref-14)
15. In the case of making the annual adjustment for year 2, the previous year's AR would be the same as the approved smoothed revenue for year 1 as contained in the PTRM. [↑](#footnote-ref-15)
16. In the transmission determination for Powerlink's 2012–17 regulatory control period, the CPI required for the annual MAR adjustment process reflects the March quarter CPI, which is typically published by the ABS in late April each year. For this transmission determination we require Powerlink to use the December quarter of the previous calendar year CPI for the annual MAR adjustment for its 2017–22 regulatory control period. December quarter CPI is typically released by the ABS towards the end of January of the following year. As the same set of CPI will be used for the RAB roll forward at the next reset for Powerlink in 2022, this change will allow us to update the actual CPI for RAB roll forward purposes well before the publication date of the AER's final decision at the next reset. We note that there will be an overlapping issue of the March quarter CPI when the transition to the December quarter CPI occurs (this will be in the year 2017–18 for Powerlink). This is because the CPI for March quarter 2017 will be reflected in both 2016–17 and 2017–18. However, we consider this is only a transitional issue and unlikely to have a material impact on the revenue to be recovered by Powerlink. [↑](#footnote-ref-16)
17. Please see appendix B of attachment 3 for details. [↑](#footnote-ref-17)
18. NER, cl. 6A.7.4. [↑](#footnote-ref-18)
19. NER, cll. 6A.7.2 and 6A.7.3. [↑](#footnote-ref-19)
20. NER, cll 6A.23.3(c)(2)(iii) and 6A.24.4(c). [↑](#footnote-ref-20)
21. NER, cl. 6A.24.1(d). [↑](#footnote-ref-21)
22. Powerlink is not required to apply an X factor for 2017–18 because we set the 2017–18 MAR in this decision. [↑](#footnote-ref-22)
23. NER, cl. 6A.5.3(c)(3). [↑](#footnote-ref-23)
24. NER, cl. 6A.6.8(c)(2). We consider a divergence of up to 3 per cent between the expected MAR and annual building block revenue requirement for the last year of the regulatory control period is appropriate, if this can achieve smoother price changes for users over the regulatory control period. In the present circumstances, based on the X factors we have determined for Powerlink, this divergence is around 0.86 per cent. [↑](#footnote-ref-24)
25. In real 2016–17 dollar terms, the average decrease in our approved expected MAR for Powerlink is 7.7 per cent per annum over the 2017–22 regulatory control period. [↑](#footnote-ref-25)
26. In real 2016–17 dollar terms, this consists an initial decrease of 32.6 per cent from 2016–17 to 2017–18, followed by subsequent average annual decreases of 0.15 per cent during the remainder of the 2017–22 regulatory control period. [↑](#footnote-ref-26)
27. NER, cl. 6A.5.5. [↑](#footnote-ref-27)
28. AER, Shared asset guideline, November 2013. [↑](#footnote-ref-28)
29. AER, Shared asset guideline, November 2013, p. 8. [↑](#footnote-ref-29)
30. Powerlink, Revenue proposal, January 2016, p.110. [↑](#footnote-ref-30)
31. This was undertaken when we developed our shared asset guideline, during the 2013 calendar year, as part of our Better Regulation work program. [↑](#footnote-ref-31)
32. We will reassess the materiality of the forecast shared asset unregulated revenues for our final decision. [↑](#footnote-ref-32)
33. Powerlink, Revenue proposal, PTRM, January 2016. [↑](#footnote-ref-33)
34. On average, the draft decision transmission revenues will decrease by 5.4 per cent ($ nominal) per annum from 2016–17 to 2021–22. The forecast energy delivered in Queensland will increase by an average of 0.6 per cent per annum across that period. As a result, the indicative transmission charge will decrease by 6.0 per cent ($ nominal) per annum from 2016–17 to 2021–22. [↑](#footnote-ref-34)
35. Powerlink, Reset RIN – Table 7.6.1, October 2015. [↑](#footnote-ref-35)
36. AEMC, 2015 Residential electricity price trends, December 2015, p. 101. [↑](#footnote-ref-36)
37. Powerlink, Reset RIN – Table 7.6.1, October 2015. [↑](#footnote-ref-37)