



**DRAFT DECISION**  
**Powerlink transmission**  
**determination**  
**2017–18 to 2021–22**

**Attachment 14 – Negotiated**  
**services**

September 2016

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## Note

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.

The draft decision includes the following documents:

Overview

Attachment 1 – Maximum allowed revenue

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Value of imputation credits

Attachment 5 – Regulatory depreciation

Attachment 6 – Capital expenditure

Attachment 7 – Operating expenditure

Attachment 8 – Corporate income tax

Attachment 9 – Efficiency benefit sharing scheme

Attachment 10 – Capital expenditure sharing scheme

Attachment 11 – Service target performance incentive scheme

Attachment 12 – Pricing methodology

Attachment 13 – Pass through events

Attachment 14 – Negotiated services

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## Shortened forms

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

| Shortened form | Extended form                               |
|----------------|---|
| RPP            | revenue and pricing principles              |
| SLCAPM         | Sharpe-Lintner capital asset pricing model  |
| STPIS          | service target performance incentive scheme |
| TNSP           | transmission network service provider       |
| TUoS           | transmission use of system                  |
| WACC           | weighted average cost of capital            |

## 14 Negotiated services

This attachment sets out our determination on Powerlink's negotiating framework for the 2017–22 regulatory control period.<sup>1</sup> We also specify the negotiated transmission service criteria (NTSC) that are to apply to Powerlink.<sup>2</sup>

In contrast to our regulation of prescribed transmission services, the provision of negotiated transmission services is less directly regulated by the AER. Instead, under the National Electricity Rules (NER), negotiated transmission services are subject to negotiation between parties or, alternatively, arbitration and dispute resolution by a commercial arbitrator.

For the purpose of facilitating such negotiation and arbitration, a transmission business must prepare, for our approval, a negotiating framework which sets out procedures for negotiating the terms and conditions of access to a negotiated transmission service.<sup>3</sup> In addition, we specify for each transmission business the negotiated transmission service criteria (NTSC) that it must apply in negotiating terms and conditions of access, including the prices and access charges for negotiated transmission services.<sup>4</sup> The NTSC also contains the criteria that a commercial arbitrator must apply to resolve disputes about such terms and conditions and/or access charges.<sup>5</sup> The NTSC for Powerlink is identical to the criteria we developed and applied for other TNSPs.

### 14.1 Draft decision

We approve Powerlink's proposed negotiating framework.<sup>6</sup>

We will also apply to Powerlink the NTSC we published in February 2016.<sup>7</sup>

### 14.2 Powerlink's proposal

Powerlink stated that its proposed negotiating framework for the 2018-22 regulatory period is largely consistent with, or fundamentally the same as, its current AER approved negotiating framework.<sup>8</sup>

Powerlink stated that it has proposed an amendment to one phrase in the document. Specifically, in relation to the termination (if any) of negotiations between Powerlink and a service applicant, Powerlink has replaced the phrase “believes on reasonable

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<sup>1</sup> NER, cl. 6A.2.2(2); 6A.14.1(6).

<sup>2</sup> NER, cl. 6A.2.2(3). 6A.14.1(7).

<sup>3</sup> NER, cl. 6A.9.5(a).

<sup>4</sup> NER, cl. 6A.9.4(a)(1).

<sup>5</sup> NER, cl. 6A.9.4(a)(2).

<sup>6</sup> Powerlink, *2018-22 Powerlink Queensland Revenue Proposal, Appendix 17.01, Negotiating Framework for Negotiated Transmission Services, Version 2 dated October 2015*, January 2016.

<sup>7</sup> AER, *Negotiated transmission service criteria for Powerlink – Call for submissions*, February 2016.

<sup>8</sup> Powerlink, *2018-22 Powerlink Queensland Revenue Proposal*, January 2016, p. 129.

grounds” with the phrase “is of the reasonable opinion.” Powerlink stated that it considers that the amendment more appropriately reflects that in these circumstances, it would be providing an opinion.<sup>9</sup>

11.2.1 Powerlink ~~is of the reasonable opinion~~ believes on reasonable grounds that the Service Applicant is not conducting the negotiation under this negotiating framework in good faith;<sup>10</sup>

Further, Powerlink has proposed a small number of typographical changes to its current negotiating framework document.

Powerlink stated it considers that its negotiating framework meets all regulatory requirements, given that it includes all relevant information prescribed under the NER and the reset RIN.<sup>11</sup>

### 14.3 Assessment approach

In reaching our draft decision, we considered whether:

- Powerlink’s proposed negotiating framework specified the minimum requirements in clause 6A.9.5(c) of the NER<sup>12</sup>
- the NTSC reflects the negotiated transmission service principles in clause 6A.9.1 of the NER.<sup>13</sup>

### 14.4 Reasons for draft decision

We approve Powerlink’s proposed negotiating framework because it specifies and meets the minimum NER requirements.<sup>14</sup> These include, among other things, a requirement for Powerlink (and the service applicant) to negotiate in good faith, and that all disputes between the parties will be dealt with in accordance with the NER.<sup>15</sup>

Table 14.1 summarises our assessment of Powerlink’s proposed negotiating framework. It shows that each of the requirements under the NER for a negotiating framework is satisfactorily addressed.

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<sup>9</sup> Powerlink, *2018-22 Powerlink Queensland Revenue Proposal*, January 2016, p. 129.

<sup>10</sup> Powerlink, *2018-22 Powerlink Queensland Revenue Proposal, Appendix 17.01, Negotiating Framework for Negotiated Transmission Services, Version 2 dated October 2015*, January 2016, p. 12.

<sup>11</sup> Powerlink, *2018-22 Powerlink Queensland Revenue Proposal*, January 2016, p. 129.

<sup>12</sup> NER, cl. 6A.9.5(b)(2); 6A.14.3(f).

<sup>13</sup> NER, cl. 6A.9.4(b).

<sup>14</sup> NER, cl. 6A.9.5(c).

<sup>15</sup> NER, Part K Commercial arbitration for disputes about terms and conditions of access for prescribed and negotiated transmission services, cl. 6A.30 to 6A.30.8.



**Table 14.1 AER's assessment of Powerlink's proposed negotiating framework<sup>16</sup>**

| NER requirements   | AER assessment   |
|--|--|
| Requirement for Powerlink and the applicant for a negotiated transmission service to negotiate in good faith—clause 6A.9.5(c)(1)   | Paragraph 2 of Powerlink's proposed negotiating framework complies with this requirement.                |
| Requirement for Powerlink to provide all such commercial information reasonably required to enable the applicant of a negotiated transmission service to engage in effective negotiations—clause 6A.9.5(c)(2)  | Paragraph 6 of Powerlink's proposed negotiating framework complies with this requirement.                |
| Requirement for Powerlink to identify and inform the negotiated transmission service applicant of the reasonable costs of providing the negotiated service; and demonstrate that charges reflect costs—clause 6A.9.5(c)(3)                                 | Paragraphs 6.1.2 and 6.1.3 of Powerlink's proposed negotiating framework complies with this requirement. |
| Requirement for a negotiated transmission service applicant to provide all such commercial information reasonably required to enable Powerlink to engage in effective negotiation—clause 6A.9.5(c)(4)  | Paragraphs 4 and 5 of Powerlink's proposed negotiating framework complies with this requirement.         |
| Requirement to specify a reasonable period of time for commencing, progressing and finalising negotiations; and a requirement for each party to use their reasonable endeavours to adhere to those time periods during the negotiation—clause 6A.9.5(c)(5) | Paragraphs 3 and 8 of Powerlink's proposed negotiating framework complies with this requirement.         |
| Requirement to specify a process for disputes to be dealt with in accordance with the relevant provisions for dispute resolution —clause 6A.9.5(c)(6)  | Paragraphs 9 and 8.1.2 of Powerlink's proposed negotiating framework complies with this requirement.     |
| Requirement to specify arrangements for the payment of Powerlink's reasonable direct expenses incurred in processing the application to provide the negotiated transmission service—clause 6A.9.5(c)(7)  | Paragraph 10 of Powerlink's proposed negotiating framework complies with this requirement.               |
| Requirement for Powerlink to determine the potential impact of the provision of a negotiated transmission service on other network users—clause 6A.9.5(c)(8)   | Paragraph 7.1 of Powerlink's proposed negotiating framework complies with this requirement.              |
| Requirement for Powerlink to notify and consult with any affected network user and ensure the negotiated transmission service does not result in noncompliance with obligations in relation to other network users under                                   | Paragraph 7.2 of Powerlink's proposed negotiating framework complies with this requirement.              |

<sup>16</sup> Powerlink, 2018-22 Powerlink Queensland Revenue Proposal, Appendix 17.01, Negotiating Framework for Negotiated Transmission Services, Version 2 dated October 2015, January 2016.

Source: AER analysis

## 14.5 Negotiated transmission service criteria

Our draft decision NTSC is set out in Appendix A of this attachment.

In February 2015, we published an invitation for submissions on the NTSC that we considered should be applied to Powerlink. The NSTC we published consisted of the same criteria set out in Appendix A.

We consider the proposed negotiating framework is consistent with the requirements of the NER as set out in the Table 14.1 above. Further, we consider the NTSC we published is consistent with previous criteria we have applied for other TNSPs and consistent with the negotiated transmission services principles.<sup>17</sup> However, in response to our proposed NTSC, we received a submission from Aurizon Operations Limited (Aurizon) which stated it had a number of concerns with the proposed NTSC and sought several amendments to the criteria. These are discussed below together with our preliminary views on the Aurizon proposed amendments. Our draft position is that the proposed amendments are not consistent with the negotiated transmission services principles.

### 14.5.1 Background

We are required to specify the NTSC to be applied to Powerlink in the 2017–22 regulatory control period. The NTSC set out the criteria to be applied by Powerlink in negotiating terms and conditions of access for negotiated transmission services and any access charges. The NTSC also sets out the criteria to be applied by a commercial arbitrator in resolving any dispute in relation to those matters.<sup>18</sup> When developing the NTSC, we must specify criteria that give effect to and are consistent with the Negotiated Transmission Service Principles in clause 6A.9.1 of the NER.<sup>19</sup>

### 14.5.2 Submission: proposed amended criteria

We received a submission from Aurizon on the NTSC we published in February 2016.<sup>20</sup> Aurizon provides ‘electric traction’ for train operators in the Central Queensland coal network. It draws its energy from the national electricity market via connection agreements with Powerlink and Ergon Energy.

In its submission, Aurizon stated that a significant number of its connections with Powerlink are subject to clause 11.6.11 of the NER. This clause grandfathers as

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<sup>17</sup> NER, clause 6A.9.1

<sup>18</sup> NER, clause 6A.9.4(a)

<sup>19</sup> NER, clause 6A.9.4(b)

<sup>20</sup> Aurizon – Submission on Powerlink regulatory proposal 2017–22, 28 April 2016.

‘prescribed connections services’, connection services which were provided by assets that were in Powerlink’s regulatory asset base (or committed to be constructed) as at 9 February 2006. But for clause 11.6.11, these connection services would be ‘negotiated transmission services’ subject to a lighter form of regulation, being the commercial negotiation/arbitration regime.

Aurizon’s submission noted that it may be required to renegotiate its connection agreement with Powerlink during the 2017–22 regulatory control period. If this happens the NER provides that the grandfathering provisions in clause 11.6.11 would no longer apply.<sup>21</sup> The effect of this would be that the connection services that Aurizon receives would move from a prescribed to a negotiated transmission service.

With the potential for this transition to occur, Aurizon’s submission proposed amendments to the NTSC we published. Table 14.2 contains each of the amendments it proposed together with our draft decision. Our reasons are set out further below.

**Table 14.2 Assessment of Aurizon Networks’ proposed amendments**

| Proposed amendments   | Draft decision   |
|---|--|
|   | <p><u>Amendment 1</u></p> <p>The value of the eligible assets that are to be removed from the regulatory asset base.</p>   |
|   | <p><u>Amendment 2</u></p> <p>The costs that were previously allocated to the prescribed transmission service.</p>  |
| <p>The price for a negotiated transmission service that ceases to be a prescribed transmission service due to the expiry of the term of the connection agreement must have regard to:</p> | <p><u>Amendment 3</u></p> <p>The direct costs attributable to the continuous provision of the negotiated transmission service.</p>                               |
|   | <p><u>Amendment 4</u></p> <p>The relativity of the price of the negotiated transmission service to the current price of the prescribed transmission service.</p> |
|   | <p><u>Amendment 5</u></p> <p>The likely impacts of the price on demand for electricity consumers in the affected downstream market.</p>                          |

Source: Aurizon, *Submission on Powerlink regulatory proposal 2017–22*, 28 April 2016; AER analysis.

As shown in Table 14.2 above, our draft decision is not to accept any of Aurizon’s proposed amendments to the NTSC. Our assessment has been based on the

<sup>21</sup> NER, clause 11.6.11(a).

negotiated transmission service principles that apply to such services. Among these principles is the requirement in clause 6A.9.1(1) of the NER that ‘the price for a negotiated transmission service should be based on the costs incurred in providing that service’.<sup>22</sup> We refer to this as the ‘cost reflectivity’ principle in this draft decision.

We are not satisfied that amendments 1 and 2 are consistent with the cost reflectivity principle. These amendments mean that when a service transitions from a prescribed to a negotiated transmission service, the price must be set with regard to certain factors. These are the value of the assets removed from the RAB and the costs that were previously allocated to the prescribed transmission service. Since these factors may not necessarily relate to the relevant cost of providing a negotiated transmission service to a customer, we conclude that amendments 1 and 2 are not consistent with the cost reflectivity principle set out in clause 6A.9.1(1) of the NER.<sup>23</sup>

We do not consider amendments 3 and 4 are consistent with the cost-reflectivity principle either. These amendments would require the price of negotiated services to be based on ‘direct costs’ and bear some ‘relativity’ to the price of the prescribed transmission services. In our view it is not clear how basing the charge for negotiated services at least in part on the cost of prescribed services is consistent with the cost reflectivity principle in the NER.<sup>24</sup> While the direct costs of providing a negotiated transmission service to a customer are relevant, it is not clear how having regard to the relative cost of a previously provided prescribed service would lead to prices that are cost reflective.

We consider that amendment 5 would not give effect to the negotiated transmission service principles. It seeks to have the price of a negotiated service determined by reference to the likely impact on demand for electricity by consumers in downstream markets. With respect to Aurizon, the relevant downstream market would be the supply of electric traction to rail haulage customers. Our view is that such considerations are not consistent with the cost reflectivity principle in the NER. This is because it suggests that prices could be reduced below a cost reflective level if the impact on a downstream market was substantial. We therefore consider that amendment 5 should not form part of the NTSC.

In this draft decision, we do not accept any of the amendments proposed by Aurizon since we are not satisfied that they are consistent with the cost reflectivity principle in clause 6A.9.1(1) of the NER. We further note that Aurizon’s proposal seeks to introduce criteria in the NTSC that would lead to a certain class of customers having the price of a negotiated service set differently. In particular, customers which received prescribed connection services under grandfathering arrangements would have their prices set differently to other customers well after the grandfathering period expires.

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<sup>22</sup> NER, clause 6A.9.1(1).

<sup>23</sup> NER, clause 6A.9.1(1).

<sup>24</sup> NER, clause 6A.9.1(1).

Our view is that this proposal is not consistent with the non–discriminatory principle in the NER, which states:<sup>25</sup>

the price for a negotiated transmission service must be the same for all Transmission Network Users unless there is a material difference in the costs of providing the negotiated transmission service to different Transmission Network Users or classes of Transmission Network Users.

In our view the amendments proposed by Aurizon should not be included in our NTSC determination because they are not consistent with the cost reflectivity and non–discriminatory principles in the NER. Although we have not accepted any of the proposed amendments, we are open to further submissions on the NTSC for the purposes of making our final decision.

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<sup>25</sup> NER, clause 6A.9.1(5).

# A Negotiated transmission service criteria

## *National Electricity Objective*

1. The terms and conditions of access for a negotiated transmission service, including the price that is to be charged for the provision of that service and any access charges, should promote the achievement of the National Electricity Objective.

## *Criteria for terms and conditions of access*

### *Terms and conditions of access*

2. The terms and conditions of access for a negotiated transmission service must be fair, reasonable and consistent with the safe and reliable operation of the power system in accordance with the NER.
3. The terms and conditions of access for negotiated transmission services, particularly any exclusions and limitations of liability and indemnities, must not be unreasonably onerous. Relevant considerations include the allocation of risk between the TNSP and the other party, the price for the negotiated transmission service and the cost to the TNSP of providing the negotiated service.
4. The terms and conditions of access for a negotiated transmission service must take into account the need for the service to be provided in a manner that does not adversely affect the safe and reliable operation of the power system in accordance with the NER.

### *Price of services*

5. The price of a negotiated transmission service must reflect the cost that Powerlink has incurred or incurs in providing that service, and must be determined in accordance with the principles and policies set out in Powerlink's Cost Allocation Methodology.
6. Subject to criteria 7 and 8, the price for a negotiated transmission service must be at least equal to the avoided cost of providing that service but no more than the cost of providing it on a stand alone basis.
7. If the negotiated transmission service is a shared transmission service that:
  - a. exceeds any network performance requirements which it is required to meet under any relevant electricity legislation; or
  - b. exceeds the network performance requirements set out in Schedules 5.1a and 5.1 of the NER<sup>26</sup>

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<sup>26</sup> NER, Schedule 5.1a System standards, and Schedule 5.1 Network Performance Requirements to be provided or Co-ordinated by Network Service Providers.

then the difference between the price for that service and the price for the shared transmission service which meets network performance requirements must reflect the Powerlink's incremental cost of providing that service (as appropriate).

8. For shared transmission services, the difference in price between a negotiated transmission service that does not meet or exceed network performance requirements and a service that meets those requirements should reflect Powerlink's avoided costs. Schedules 5.1a and 5.1 of the NER or any relevant electricity legislation must be considered in determining whether any network service performance requirements have not been met or exceeded.
9. The price for a negotiated transmission service must be the same for all Transmission Network Users. The exception is if there is a material difference in the costs of providing the negotiated transmission service to different Transmission Network Users or classes of Transmission Network Users.
10. The price for a negotiated transmission service must be subject to adjustment over time to the extent that the assets used to provide that service are subsequently used to provide services to another person. In such cases, the adjustment must reflect the extent to which the costs of that asset are being recovered through charges to that other person.
11. The price for a negotiated transmission service must be such as to enable Powerlink to recover the efficient costs of complying with all regulatory obligations associated with the provision of the negotiated transmission service.

### ***Criteria for access charges***

#### *Access charges*

12. Any access charges must be based on the costs reasonably incurred by Powerlink in providing Transmission Network User access. This includes the compensation for forgone revenue referred to in clauses 5.4A(h) to (j) of the NER and the costs that are likely to be incurred by a person referred to in clauses 5.4A(h) to (j) of the NER (as appropriate).