



FINAL DECISION
Endeavour Energy distribution
determination
2015–16 to 2018–19

Attachment 2 – Regulatory
asset base

April 2015

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Note

This attachment forms part of the AER's final decision on Endeavour Energy's regulatory proposal 2015–19. It should be read with other parts of the final decision.

The final decision includes the following documents:

Overview

Attachment 1 - Annual revenue requirement

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 - Demand management incentive scheme

Attachment 13 - Classification of services

Attachment 14 - Control mechanism

Attachment 15 - Pass through events

Attachment 16 - Alternative control services

Attachment 17 - Negotiated services framework and criteria

Attachment 18 - Connection policy

Attachment 19 - Analysis of financial viability

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Shortened forms

Shortened form	Extended form
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
augex	augmentation expenditure
capex	capital expenditure
CCP	Consumer Challenge Panel
CESS	capital expenditure sharing scheme
CPI	consumer price index
DRP	debt risk premium
DMIA	demand management innovation allowance
DMIS	demand management incentive scheme
distributor	distribution network service provider
DUoS	distribution use of system
EBSS	efficiency benefit sharing scheme
ERP	equity risk premium
Expenditure Assessment Guideline	expenditure forecast assessment Guideline for electricity distribution
F&A	framework and approach
MRP	market risk premium
NEL	national electricity law
NEM	national electricity market
NEO	national electricity objective
NER	national electricity rules
NSP	network service provider
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

Shortened form	Extended form
RIN	regulatory information notice
RPP	revenue and pricing principles
SAIDI	system average interruption duration index
SAIFI	system average interruption frequency index
SLCAPM	Sharpe-Lintner capital asset pricing model
STPIS	service target performance incentive scheme
WACC	weighted average cost of capital

2 Regulatory asset base

We are required to make a decision on Endeavour Energy's opening regulatory asset base (RAB) as at 1 July 2014.¹ We use the RAB at the start of each regulatory year to determine the return of capital (regulatory depreciation) and return on capital building block allowances. This attachment presents our final decision on the opening RAB value as at 1 July 2014 for Endeavour Energy and roll forward of the forecast RAB values over the 2014–19 period.

2.1 Final decision

We accept Endeavour Energy's revised proposed opening RAB of \$5581.3 million (\$ nominal) as at 1 July 2014. Endeavour Energy adopted our draft decision amendments in its revised proposal.² The only change to the draft decision was updating 2013–14 estimated capex with actuals consistent with the annual reporting RIN for that year.

We note Endeavour Energy's revised proposal adopted our draft decision on the use of forecast depreciation for establishing the RAB at the commencement of the regulatory control period from 1 July 2019.³ We therefore maintain our draft decision position on this issue for this final decision.

Table 2.1 sets out our final decision on the roll forward of the RAB values for the 2009–14 regulatory control period.

We determine a forecast closing RAB value at 30 June 2019 of \$6859.9 million (\$ nominal). This is \$53.7 million (or 0.8 per cent) lower than the amount of \$6913.6 million (\$ nominal) in Endeavour Energy's revised proposal. Our final decision on the forecast closing RAB reflects our adjustments to Endeavour Energy's forecast regulatory depreciation (attachment 5) and the forecast inflation rate (attachment 3).

Table 2.2 sets out our final decision on the forecast RAB values for Endeavour Energy over the 2014–19 period.

¹ NER, cl. 6.12.1(6).

² Endeavour Energy, *Revised regulatory proposal*, January 2015, Attachment 4.02.

³ Endeavour Energy, *Revised regulatory proposal*, January 2015, p. 69.

Table 2.1 AER's final decision on Endeavour Energy's RAB for the 2009–14 regulatory control period (\$ million, nominal)

	2009–10	2010–11	2011–12	2012–13	2013–14
Opening RAB	3690.0	3940.3	4342.1	4910.3	5346.0
Capital expenditure ^a	423.1	509.4	647.9	581.7	542.4
Inflation indexation on opening RAB	67.2	112.1	147.2	86.6	131.0
Less: straight-line depreciation	239.9	219.7	226.8	232.6	231.5
Closing RAB	3940.3	4342.1	4910.3	5346.0	5787.8
Difference between estimated and actual capex (1 July 2008 to 30 June 2009)					-116.6
Return on difference for 2008–09 capex					-71.2
Closing RAB as at 30 June 2014					5600.1
Meters moved to alternative control services					-18.8
Opening RAB as at 1 July 2014					5581.3

Source: AER analysis.

(a) Net of disposals and capital contributions, and adjusted for CPI.

Table 2.2 AER's final decision on Endeavour Energy's RAB for the 2014–19 period (\$ million, nominal)

	2014–15	2015–16	2016–17	2017–18	2018–19
Opening RAB	5581.3	5944.3	6223.7	6444.0	6658.5
Capital expenditure ^a	432.3	358.3	310.0	308.2	301.5
Inflation indexation on opening RAB	132.8	141.5	148.1	153.4	158.5
Less: straight-line depreciation	202.1	220.4	237.8	247.2	258.5
Closing RAB	5944.3	6223.7	6444.0	6658.5	6859.9

Source: AER analysis.

(a) Net of forecast disposals and capital contributions.

2.2 Endeavour Energy's revised proposal

Endeavour Energy's revised proposal submitted an opening RAB value as at 1 July 2014 of \$5581.3 million (\$ nominal). Endeavour Energy adopted all our draft decision adjustments to roll forward the opening RAB from 1 July 2009 to 30 June 2014.⁴

⁴ Endeavour Energy, *Revised regulatory proposal*, January 2015, Attachment 4.02.

Endeavour Energy also updated the revised proposed opening RAB to reflect actual capex for 2013–14.

Endeavour Energy's revised proposal submitted a forecast closing RAB as at 30 June 2019 of \$6913.6 million (\$ nominal). This value reflects its revised opening RAB, forecast capex and forecast depreciation (based on forecast capex) over the 2014–19 period. Endeavour Energy's projected RAB over the 2014–19 period is shown in Table 2.3.

Table 2.3 Endeavour Energy's revised proposed RAB for the 2014–19 period (\$ million, nominal)

	2014–15	2015–16	2016–17	2017–18	2018–19
Opening RAB	5581.3	5952.9	6243.3	6474.6	6700.4
Capital expenditure ^a	434.4	362.6	314.0	312.6	306.1
Inflation indexation on opening RAB	139.5	148.8	156.1	161.9	167.5
Less: straight-line depreciation	202.4	221.0	238.8	248.6	260.4
Closing RAB	5952.9	6243.3	6474.6	6700.4	6913.6

Source: Endeavour Energy, *Revised regulatory proposal*, January 2015, Attachment 4.01a.

(a) Net of forecast disposals and capital contributions.

2.3 AER's assessment approach

We did not change our assessment approach for the RAB from our draft decision. Section 2.3 of our draft decision details that approach.⁵

2.4 Reasons for final decision

We accept Endeavour Energy's revised proposed opening RAB value of \$5581.3 million (\$ nominal) as at 1 July 2014. Based on the approved opening RAB we forecast a closing RAB value of \$6859.9 million (\$ nominal) by 30 June 2019. This represents a reduction of \$53.7 million, or 0.8 per cent compared to the revised proposal. The reasons for our decision are discussed below.

2.4.1 Opening RAB as at 1 July 2014

We accept Endeavour Energy's revised proposed opening RAB value of \$5581.3 million (\$ nominal) as at 1 July 2014.

In the draft decision, we made adjustments to the disposal values in Endeavour Energy's roll forward of its RAB over the 2009–14 regulatory control period. We noted

⁵ AER, *Draft decision - Endeavour Energy distribution determination attachment 2 - Regulatory asset base*, November 2014, pp. 10–13.

the roll forward of Endeavour Energy's RAB included an estimated capex value for 2013–14. We stated we would update the 2013–14 estimated capex value for the final decision.

Endeavour Energy's revised proposal adopted our draft decision adjustments to roll forward the opening RAB from 1 July 2009 to 1 July 2014. Endeavour Energy also updated the 2013–14 estimated capex adopted in the draft decision to reflect actual capex for that year. We have reconciled the 2013–14 capex in the revised proposal against Endeavour Energy's audited annual RIN for 2013–14. We therefore accept the actual capex for 2013–14, and the revised proposed opening RAB as at 1 July 2014.

PIAC raised concerns with the size of Endeavour Energy's opening RAB in its submission to the draft decision.⁶ Its submission suggested the potential for writing off some parts of the RAB. We note that the opening RAB reflects the capex incurred during the previous regulatory control periods. In the previous two regulatory control periods there was a significant increase in capex that only began to tail off in more recent years. We have no ability to adjust for past capex or to optimise/write down the opening RAB for efficiency considerations. Under the transitional rules, the review of past capex does not apply to Endeavour Energy prior to 1 July 2015.⁷ Therefore, for the purposes of this final decision, we are required to add Endeavour Energy's actual capex from the 2009–14 regulatory control period to the RAB. However, with rule changes in 2012, we will have the ability to exclude inefficient capex incurred during the 2015–19 regulatory control period in future resets if it exceeds the approved forecast and if we consider it does not reasonably reflect the capital expenditure criteria.⁸ The details of our assessment approach for inefficient capex are set out in the *Capital expenditure incentive guideline*.⁹

2.4.2 Forecast closing RAB as at 30 June 2019

We forecast a closing RAB value of \$6859.9 million by 30 June 2019 for Endeavour Energy. This represents a reduction of \$53.7 million, or 0.8 per cent to Endeavour Energy's revised proposal. This reduction reflects our final decision on the required inputs for determining the forecast RAB in the post-tax revenue model (PTRM). To determine the forecast RAB value, we amended the following PTRM inputs:

- We increased Endeavour Energy's revised proposal forecast regulatory depreciation for the 2014–19 period by \$34.3 million or 8.6 per cent (attachment 5).
- We reduced Endeavour Energy's revised proposed forecast inflation rate of 2.50 per cent per annum to 2.38 per cent per annum (attachment 3).

⁶ PIAC, *Submission on NSW draft decisions*, 14 February 2015, p. 60–61.

⁷ NER, cl. 11.56.5.

⁸ Under the NER, cl S6.2.2A(b), the exclusion of inefficient capex could only come from three areas including overspend in capex, margin paid to third party and capitalisation of opex as defined in cl S6.2.2A(c), (d) and (e) of the NER.

⁹ AER, *Capital expenditure Incentive guideline*, November 2013, pp. 12–20.