



FINAL DECISION
Directlink transmission
determination
2015–16 to 2019–20

Attachment 13 – Pass through
events

April 2015

© Commonwealth of Australia 2015

This work is copyright. In addition to any use permitted under the Copyright Act 1968, all material contained within this work is provided under a Creative Commons Attributions 3.0 Australia licence, with the exception of:

- the Commonwealth Coat of Arms
- the ACCC and AER logos
- any illustration, diagram, photograph or graphic over which the Australian Competition and Consumer Commission does not hold copyright, but which may be part of or contained within this publication. The details of the relevant licence conditions are available on the Creative Commons website, as is the full legal code for the CC BY 3.0 AU licence.

Requests and inquiries concerning reproduction and rights should be addressed to the Director, Corporate Communications, Australian Competition and Consumer Commission, GPO Box 4141, Canberra ACT 2601 or publishing.unit@acc.gov.au.

Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Tel: (03) 9290 1444
Fax: (03) 9290 1457

Email: AERInquiry@aer.gov.au

AER reference: 53446

Note

This attachment forms part of the AER's final decision on Directlink's revenue proposal 2015–20. It should be read with other parts of the final decision.

The final 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 and negotiated services

Attachment 13 – pass through events

Contents

Note	13-2
Contents	13-3
Shortened forms	13-4
13 Pass through events	13-6
13.1 Final decision	13-6
13.2 Directlink’s revised proposal	13-8
13.3 AER’s assessment approach	13-8
13.3.1 Interrelationships	13-8
13.4 Reasons for final decision	13-8

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
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

Shortened form	Extended form
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
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

13 Pass through events

The cost pass through mechanism of the NER recognises that a TNSP can be exposed to risks beyond its control. These risks may have a material impact on the TNSP's costs or the manner in which it provides prescribed transmission services. A cost pass through enables a TNSP to recover (or pass through) the costs of defined, unpredictable, high cost events that are not built into our transmission determination. The NER includes the following prescribed pass through events for all TNSPs:

- a regulatory change event
- a service standard event
- a tax change event
- an insurance event, and
- in addition to those defined events, an event specified in a determination for a regulatory control period (nominated pass through event).¹

This attachment sets out our final decision on the nominated pass through events that will apply to Directlink during the 2015–20 regulatory control period.

13.1 Final decision

Our final decision is to allow the following nominated pass through events to apply to Directlink for the 2015–20 regulatory control period:

- insurance cap event
- terrorism event, and
- natural disaster event.

These events have the definitions listed in Table 13.1 below.

Table 13.1 Accepted pass through event definitions

Pass through event	Definition
Insurance cap event	An insurance cap event occurs if: <ol style="list-style-type: none">1. Directlink makes a claim or claims and receives the benefit of a payment or payments under a relevant insurance policy,2. Directlink incurs costs beyond the relevant policy limit, and3. the costs beyond the relevant policy limit materially increase the costs to Directlink in providing prescribed transmission services.

¹ NER, clause 6A.7.3(a1).

For this insurance cap event:

4. the relevant policy limit is the greater of:

- a. Directlink's actual policy limit at the time of the event that gives, or would have given, rise to a claim, and
- b. the policy limit that is explicitly or implicitly commensurate with the allowance for insurance premiums that is included in the forecast operating expenditure allowance approved in the AER's final decision for the regulatory control period in which the insurance policy is issued.

5. A relevant insurance policy is an insurance policy held during the 2015-20 regulatory control period or a previous regulatory control period in which Directlink was regulated.

Note for the avoidance of doubt, in assessing an insurance cap event cost pass through application under rule 6A.7.3, the AER will have regard to:

- i. the insurance policy for the event, and
- ii. the level of insurance that an efficient and prudent NSP would obtain in respect of the event.

Terrorism event

A terrorism event occurs if:

An act (including, but not limited to, the use of force or violence or the threat of force or violence) of any person or group of persons (whether acting alone or on behalf of or in connection with any organisation or government), which from its nature or context is done for, or in connection with, political, religious, ideological, ethnic or similar purposes or reasons (including the intention to influence or intimidate any government and/or put the public, or any section of the public, in fear) and which materially increases the costs to Directlink in providing prescribed transmission services.

In assessing a terrorism event pass through application, the AER will have regard to, amongst other things:

- i. whether Directlink has insurance against the event,
- ii. the level of insurance that an efficient and prudent NSP would obtain in respect of the event, and
- iii. whether a declaration has been made by a relevant government authority that a terrorism event has occurred.

Natural disaster event

A natural disaster event occurs if:

Any major fire, flood, earthquake or other natural disaster occurs during the 2015-20 regulatory control period and materially increases the costs to Directlink in providing prescribed transmission services, provided the fire, flood or other event was not a consequence of the acts or omissions of the NSP.

The term 'major' in the above paragraph means an event that is serious and significant. It does not mean material as that term is defined in the NER (that is 1 per cent of the TNSP's maximum allowed revenue for that regulatory year).

In assessing a natural disaster event pass through application,

the AER will have regard to, amongst other things:

- i. whether Directlink has insurance against the event,
- ii. the level of insurance that an efficient and prudent NSP would obtain in respect of the event, and
- iii. whether a relevant government authority has made a declaration that a natural disaster has occurred.

13.2 Directlink’s revised proposal

Directlink did not comment on our draft decision on pass through events in its revised proposal.

13.3 AER’s assessment approach

Our assessment approach was explained in detail in attachment 13 of our draft decision.²

Our approach has been guided by the NEO and the RPP. It provides the NSP with a reasonable opportunity to recover at least the efficient costs the operator incurs³, while also providing effective incentives to promote economic efficiency.⁴ It promotes a balance between the economic costs and risks for promoting efficient investment.⁵

We maintained this approach for the final decision.

13.3.1 Interrelationships

As we discussed in the draft decision, the nominated pass through events are interrelated with other parts of this determination, in particular with Directlink’s proposed opex and capex allowances and the rate of return.⁶ These interrelationships require the AER to balance the incentives to Directlink in the various parts of our decision.

13.4 Reasons for final decision

Directlink did not comment on our draft decision on pass through events in its revised proposal.

In our draft decision, we set out in detail our reasons for:

² AER, *Draft decision, Directlink transmission determination 2015–20, attachment 13*, November 2014, pp. 8, 9, 10.

³ NEL, s. 7A(2).

⁴ NEL, s. 7A(3).

⁵ NEL, s. 7A(6).

⁶ AER, *Draft Decision, Directlink transmission determination 2015-20, attachment 13, November 2014*, p. 10.

- amending Directlink's proposed definitions of insurance cap event, terrorism event and the natural disaster event,⁷ and
- not accepting the insurer's credit risk event and carbon cost event as pass through events.⁸

Those reasons remain the same for this final decision on Directlink's cost pass through events. For clarity, we have made two minor drafting changes to the definitions of all of Directlink's pass through events. Specifically, we have removed the following final sentence from the factors we will consider when assessing a pass through application:

the extent to which a prudent provider could reasonably mitigate the impact of the event.⁹

This is because after further review we consider that it is unnecessary to include this in the definition as it is already a specified requirement in clause 6A7.3(j)(3) of the NER. That clause provides that we must take into account the efficiency of the NSP's decisions and actions when assessing cost pass through applications.

We have also consistently adopted the term "prescribed transmission services" as used in the NER across all three nominated pass through events.

Aside from these minor drafting amendments, our final decision is to maintain the position for the reasons set out in our draft decision.

⁷ AER, *Draft Decision, Directlink transmission determination 2015-20, attachment 13*, November 2014, pp. 14, 15, 16, 17.

⁸ AER, *Draft Decision, Directlink transmission determination 2015-20, attachment 13*, November 2014, pp. 13, 14.

⁹ AER, *Draft Decision, Directlink transmission determination 2015-20, attachment 13*, November 2014, pp. 14, 15.