Draft Decision

Murraylink Transmission Determination 2023 to 2028

(1 July 2023 to 30 June 2028)

Attachment 8
Efficiency benefit sharing scheme

September 2022

AUSTRALIAN ENERGY REGULATOR

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1	30 September 2022	11

Note

This attachment forms part of the AER's draft decision on Murraylink's 2023–28 transmission determination. 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 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency benefit sharing scheme

Attachment 9 – Capital expenditure sharing scheme

Attachment 10 – Service target performance incentive scheme

Attachment 11 – Pricing methodology

Attachment 12 – Negotiated services

Contents

8 Efficiency benefit sharing scheme

The efficiency benefit sharing scheme (EBSS) is intended to provide a continuous incentive for service providers to pursue efficiency improvements in operating expenditure (opex) and provide for a fair sharing of these between transmission businesses and network users. Consumers benefit from improved efficiencies through lower regulated prices.

This attachment sets out our draft decision and reasons on the EBSS carryover amounts Murraylink has accrued over the 2018–23 regulatory control period, and how we will apply the EBSS over the 2023–28 regulatory control period (2023–28 period).

8.1 Draft decision

Our draft decision is to include EBSS carryover amounts totalling –$1.9 million ($2022–23) from the application of the EBSS in the 2018–23 regulatory control period.[1] This is $2.1 million less than Murraylink's proposal of $0.2 million.[2] This difference reflects adjustments we have made to:

- remove cost pass through costs for the three years of 2018–19, 2019–20 and 2020–21
- correct Murraylink's 2020–21 inflation, and update actual and forecast inflation for 2021–23
- update the opex forecast and actual opex for 2015–16
- update the opex forecast and actual opex for five of the remaining six EBSS years.

We set out our draft decision in Table 8.1.

Table 8.1 Draft decision on Murraylink's carryover amounts ($million, 2022–23)

	2023–24	2024–25	2025–26	2026–27	2027–28	Total
Murraylink's proposal	0.1	0.1	–0.1	–	0.1	0.2
AER draft decision	–0.7	–0.2	–0.1	–	–0.9	–1.9
Difference	–0.8	–0.3	0.0	–	–1.0	–2.1

Note: Numbers may not add due to rounding. Amounts of '0.0' and '−0.0' represent small variances and '–' represents no variance.
Source: Murraylink, *Murraylink–Attachment 05–Reset RIN–Workbook 3–EBSS*, 31 January 2022.

We will continue to apply version 2 of the EBSS to Murraylink in the 2023–28 period.[3] Consistent with our previous determination, we will exclude debt raising costs from the scheme because we have forecast them on a category specific basis and will continue doing so in the 2028–33 period. We will also make other adjustments as permitted by the EBSS, such as removing movements in provisions.

1 NER, cl. 6A.5.4(a)(5).
2 Murraylink, *Murraylink–Attachment 05–Reset RIN–Workbook 3–EBSS*, 31 January 2022.
3 AER, *Efficiency benefit sharing scheme for electricity network service providers,* November 2013.

8.2 Murraylink's proposal

8.2.1 Carryover amounts from the 2018–23 regulatory control period

Murraylink included EBSS carryover amounts totalling $0.2 million ($2022–23) in its revenues for the 2023–28 period from the application of the EBSS in the 2018–23 period.[4] Murraylink excluded debt raising costs in calculating its EBSS carryover amounts.[5]

8.2.2 Application in the 2023–28 regulatory control period

Murraylink's proposal made no reference to the application of the EBSS in the 2023–28 period.

8.2.3 Stakeholder submissions

We did not receive any stakeholder submissions on Murraylink's EBSS proposal.

8.3 Assessment approach

Under the National Electricity Rules (NER) we must determine:

- the revenue increments or decrements for each year of the 2023–28 regulatory control period arising from the application of the EBSS during the 2018–23 period[6]
- how the EBSS will apply to Murraylink in the 2023–28 period.[7]

The EBSS must provide for a fair sharing of opex efficiency gains and efficiency losses between Murraylink and network users.[8] We must also have regard to the following matters when implementing the EBSS:[9]

- the need to provide Murraylink with continuous incentives to reduce opex
- the desirability of both rewarding Murraylink for efficiency gains and penalising it for efficiency losses
- any incentives that Murraylink may have to inappropriately capitalise operating expenditure
- the possible effects of the scheme on incentives for the implementation of non-network alternatives.

4 Murraylink, *Murraylink: Transmission Determination Proposal*, 31 January 2022, p.15.

5 Murraylink, *Murraylink–Attachment 05–Reset RIN–Workbook 3–EBSS*, 31 January 2022.

6 NER, cl. 6A.5.4(a)(5).

7 NER, cl. 6A.14.1(1)(iv) and cl. 6A14.3(d)(2).

8 NER, cl. 6A.6.5(a).

9 NER, cl. 6A.6.5(b).

8.3.1 Interrelationships

The EBSS is closely linked to our revealed cost approach to forecasting opex. When we assess or develop our opex forecast, the NER requires us to have regard to whether the opex forecast is consistent with any incentive schemes.[10]

Our opex forecasting method typically relies on using the 'revealed costs' of the service provider in a chosen base year to develop a total opex forecast if the chosen base year opex is not considered to be 'materially inefficient'. Under this approach, a service provider would have an incentive to spend more opex in the expected base year. Also, a service provider has less incentive to reduce opex towards the end of the regulatory control period, where the benefit of any efficiency gains is retained for less time.

The application of the EBSS therefore serves two important functions:

- it removes the incentive for a service provider to inflate opex in the expected base year in order to gain a higher opex forecast for the next regulatory control period
- it provides a continuous incentive for a service provider to pursue efficiency improvements across the regulatory control period.

The EBSS does this by allowing a service provider to retain efficiency gains (or losses) for a total of six years, regardless of the year in which the service provider makes them. Where we do not propose to rely on the single year revealed costs of a service provider in forecasting opex, this has consequences for the service provider's incentives and our decision on how we apply the EBSS.

When a business makes an incremental efficiency gain, it receives a reward through the EBSS, and consumers benefit through a lower revealed cost forecast for the subsequent regulatory control period. This is how efficiency improvements are shared between consumers and the business. If we subject costs to the EBSS that are not forecast using a revealed cost approach, a business would in theory receive a reward for efficiency gains through the EBSS (at a cost to consumers), but consumers would not benefit through a lower revealed cost forecast in the subsequent regulatory control period.

Therefore, we typically exclude costs that we do not forecast using a single year revealed cost forecasting approach.

For these reasons, our decision on how we will apply the EBSS to Murraylink has a strong interrelationship with our decision on its opex (see Attachment 6). We have careful regard to the effect of our EBSS decision when making our opex decision, and our EBSS decision is made largely in consequence of (and takes careful account of) our past and current decisions on Murraylink's opex.

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10 NER, cl. 6A.6.6(e)(8). Further, we must specify and have regard to the relationship between the constituent components of our overall decision: National Electricity Law, s. 16(1)(c).

8.4 Reasons for draft decision

8.4.1 Carryover amounts from the 2018–23 regulatory control period

Our draft decision is to include EBSS carryover amounts totalling –$1.9 million ($2022–23) from the application of the EBSS in the 2018–23 period. This is $2.1 million lower than Murraylink's proposal of $0.2 million. This difference is because we:

- removed connection charges cost pass through amounts from the opex forecast, which decreased total carryovers by $1.9 million
- updated actual inflation for 2020–21 and 2021–22, and forecast inflation for 2022–23, which decreased total carryovers by $0.2 million
- updated forecast and actual opex to align with the 2022 return on debt (RoD) update and Murraylink's regulatory accounts, which increased total carryovers by $0.2 million
- updated opex forecast, actual opex and debt raising costs for 2015–16, which decreased total carryovers by $0.1 million.

We discuss each of these in detail below.

We also note that Murraylink's 2021–22 connection charge cost pass through application is expected after the publication of this draft decision. We will make updates as necessary to include this in the final decision. However, it is estimated that if the future connection charge cost pass throughs are similar to those in the previous two years, Murraylink's total carryover amounts would increase by approximately $0.9 million.

We consider that the EBSS carryover amounts we have calculated provide for a fair sharing of efficiency gains and losses between Murraylink and its network users. It both provides for rewards to Murraylink for any efficiency gains it has made and penalises Murraylink for any efficiency losses. Further, we consider that the benefit to consumers through lower forecast opex is sufficient to warrant the EBSS carryover amounts we have determined.

8.4.1.1 Cost pass through connection charges

The EBSS model Murraylink submitted did not include the negative cost pass throughs Murraylink received in the 2018–23 regulatory control period.[11] These cost pass throughs relate to reductions in connection charges in 2018–19, 2019–20 and 2020–21. As we stated in the 2018–23 determination, we will adjust forecast opex to add any approved revenue increments (or subtract any approved revenue decrements) made after the initial regulatory determination, including approved pass throughs.[12] We have included these costs in the EBSS model to update forecast opex for these three years.

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11 Murraylink, *Murraylink–Attachment 05–Reset RIN–Workbook 3–EBSS*, 31 January 2022.

12 AER, *Draft decision, Murraylink transmission determination 2018 to 2023 Attachment 9 – Efficiency benefit sharing scheme*, September 2017, p. 10.

8.4.1.2 Inflation

Consistent with our standard approach and opex forecast, we used unlagged inflation to convert opex amounts to 2022–23 real terms. Murraylink adopted the same approach in its proposal.[13]

We first corrected the consumer price index (CPI) value in Murraylink's EBSS model for 2020–21, then we updated CPI values that became available after Murraylink submitted its proposal. For 2020–21 and 2021–22, we used the actual headline June quarter 2022 CPI figure published by the Australian Bureau of Statistics.[14] For 2022–23, we used the inflation forecast for the year to June 2023 in the Reserve Bank of Australia's August 2022 Statement on monetary policy.[15]

8.4.1.3 Align opex with RoD update and regulatory accounts

Murraylink's proposed EBSS model has different opex forecasts compared to the 2022–23 RoD update and minor differences in actual opex compared to what is reported in its regulatory accounts. We have made the respective changes to update the EBSS model.

8.4.1.4 Forecast and actual opex for 2015–16

The EBSS model Murraylink submitted did not include the opex forecast, opex actuals and debt raising costs for 2015–16. This was the base year for Murraylink's 2018–23 regulatory control period. We have updated the EBSS model to include these values.

8.4.2 Application in the 2023–28 regulatory control period

Our draft decision is to continue to apply version 2 of the EBSS to Murraylink during the 2023–28 period. We consider applying the scheme will benefit the long-term interests of electricity consumers by providing a continuous incentive for Murraylink to reduce its opex. Provided we forecast Murraylink's future opex using its revealed costs in the 2023–28 period, any efficiency gains that Murraylink achieves will lead to lower future opex forecasts, and thus lower network tariffs.

Version 2 of the EBSS specifies our approach to adjusting forecast or actual opex when calculating carryover amounts.[16] We provide details on these below.

8.4.2.1 Adjustments to forecast or actual opex when calculating carryover amounts

The EBSS allows us to exclude categories of costs that we do not forecast using a single year revealed cost forecasting approach in the following control period. We do this to fairly share efficiency gains and losses. For instance, where a service provider achieves efficiency improvements, it receives a benefit through the EBSS and consumers receive a benefit through lower forecast opex in the next regulatory control period. This is the way consumers and the service provider share in the benefits of an efficiency improvement.

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13 Murraylink, Murraylink–Attachment 16–Operating expenditure model, 31 January 2022.

14 Australian Bureau of Statistics, *Consumer Price Index, Australia*, released on 27 July 2022 (accessed on 28 July 2022).

15 Reserve Bank of Australia, *Statement on monetary policy*, August 2022.

16 AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013.

If we do not use a single year revealed cost forecasting approach, we may not pass the benefits of these revealed efficiency gains to consumers. It follows that consumers should not pay for EBSS rewards where they do not receive the benefits of a lower opex forecast.

We do not forecast debt raising costs using a single year revealed cost forecasting approach. Instead, we provide a benchmark forecast. Accordingly, we have excluded these costs from the EBSS for the 2023–28 regulatory control period since any achieved efficiency gains (or losses) would not be passed on to network users.

In addition to the exclusion of debt raising costs discussed above, we will also make the following adjustments when we calculate the EBSS carryover amounts accrued during the 2023–28 period:

- adjust forecast opex to add (subtract) any approved revenue increments (decrements) made after the initial regulatory determination, such as approved pass through amounts or opex for contingent projects.
- adjust reported actual opex for the 2023–28 period to reverse any movements in provisions.
- adjust reported opex to add capitalised opex that has been excluded from the regulatory asset base.
- adjust forecast opex and actual opex for inflation.[17]
- exclude categories of opex not forecast using a single year revealed cost approach for the regulatory control period beginning in 2023, where doing so better achieves the requirements of clause 6A.6.5 of the NER.[18]

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17 AER, *Efficiency Benefit Sharing Scheme for Electricity Network Service Providers*, November 2013, p. 7.

18 AER, *Explanatory Statement - Efficiency Benefit Sharing Scheme for Electricity Network Service Providers*, November, p. 14.

Glossary

Term	Definition
AER	Australian Energy Regulator
CPI	Consumer price index
EBSS	Efficiency benefit sharing scheme
NER	National Electricity Rules
Opex	Operating expenditure
RoD	Return on debt