

The Australian Energy Regulator



Powerlink Transmission
revenue proposal 2017-22

Draft Decision Public Forum
19 October 2016

Agenda

- AER presentation of draft decision
- Consumer Challenge Panel (CCP) presentation
- Powerlink Transmission presentation
- Q&A
- Next steps

AER presentation of draft decision

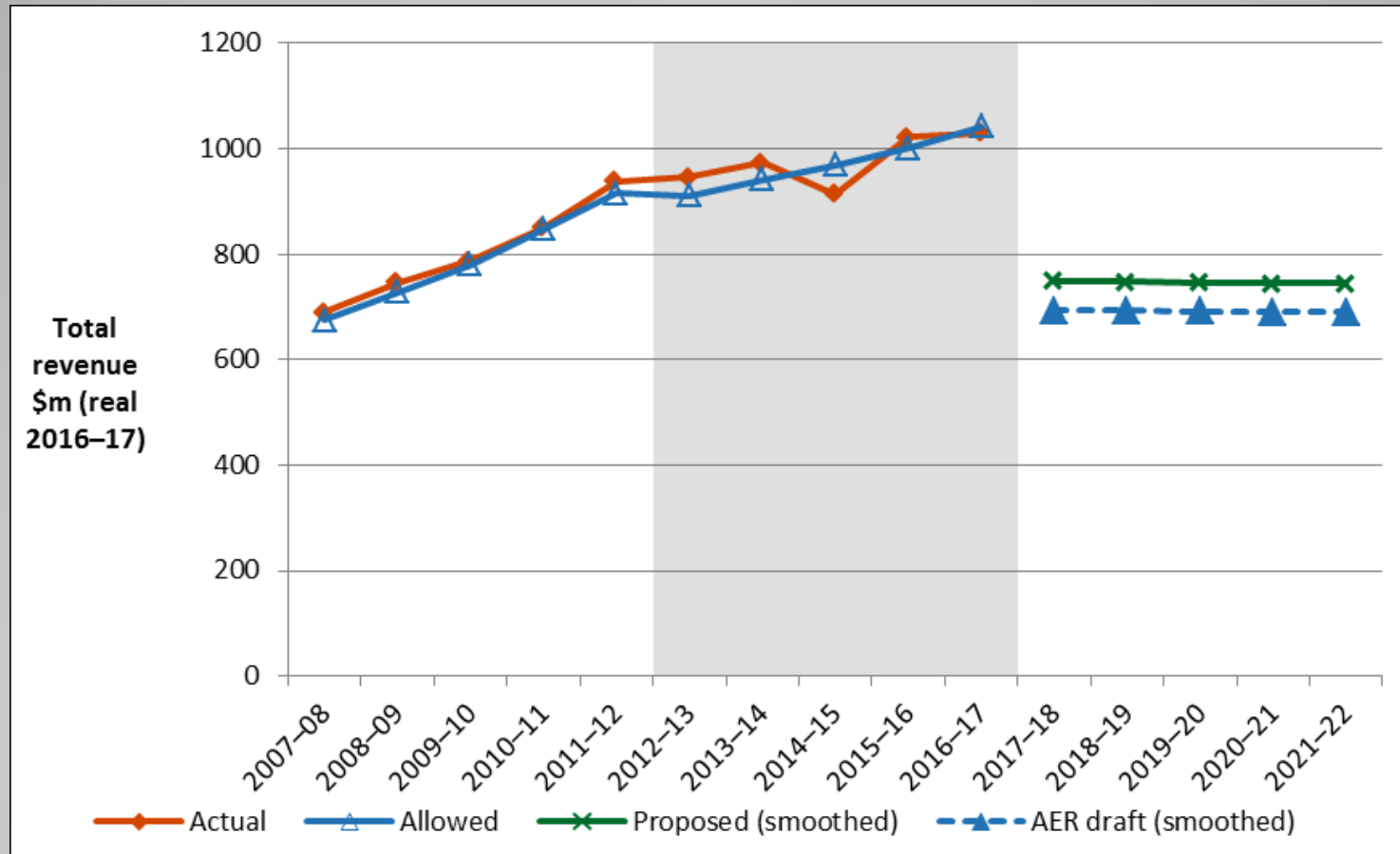
Key points

- The AER published its draft decision on Powerlink's 2017-22 revenue proposal on 29 September 2016
- The draft decision allows Powerlink to recover \$3720.8 million (\$nominal) from its customers. This represents 7.4 per cent less revenue than Powerlink proposed.
- If implemented, our draft decision would result in a decrease to the transmission component of electricity bills in Queensland over the 2017-22 regulatory period.

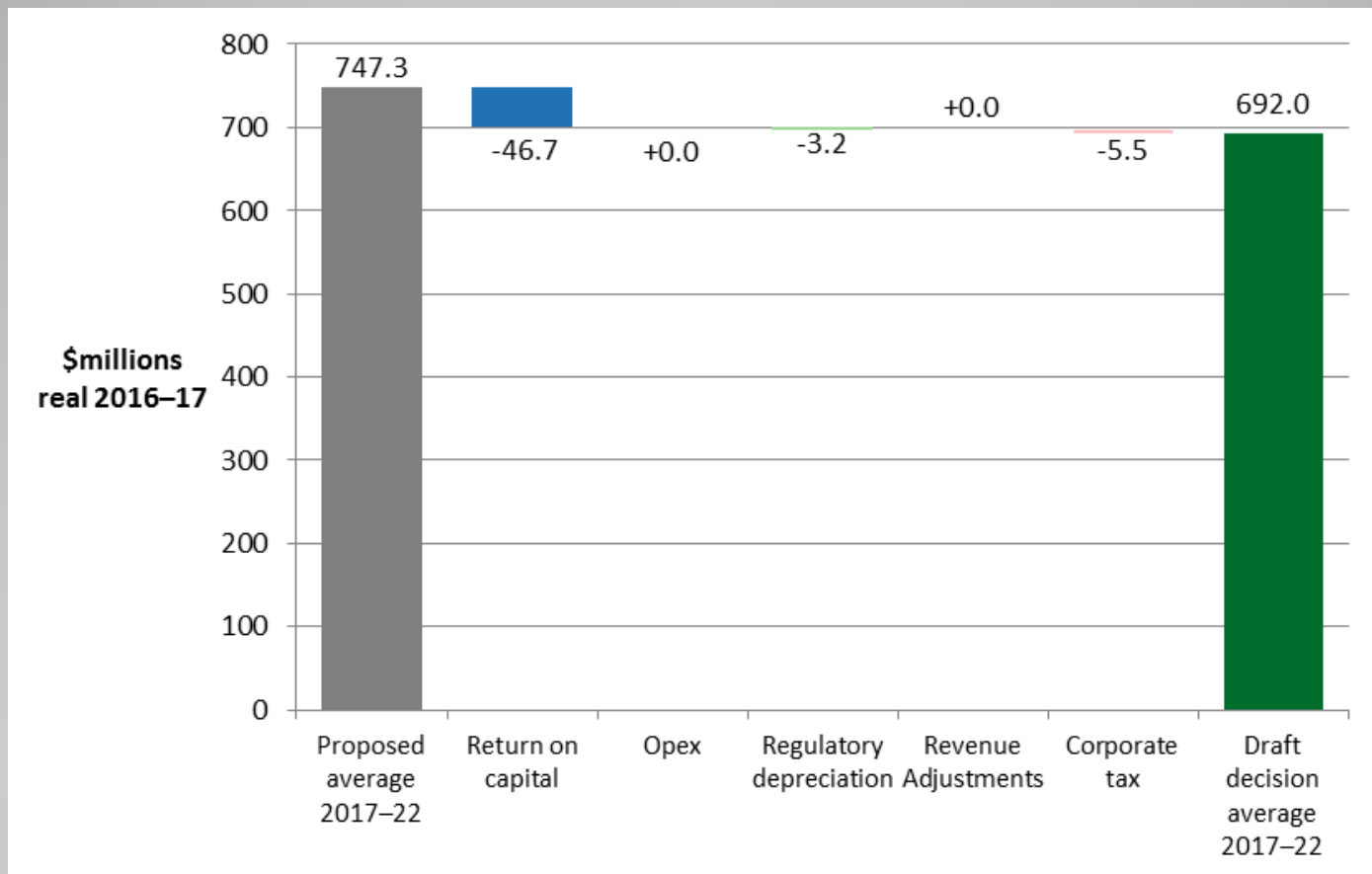
Powerlink reset timeline

| Step | Date |
|--|------------------------------|
| Powerlink submitted its revenue proposal to AER | 28 Jan 2016 |
| AER published issues paper | March 2016 |
| AER held public forum | 15 Mar 2016 |
| Submissions on revenue proposal closed | 28 Apr 2016 |
| AER published draft decision | 29 Sept 2016 |
| AER public forum to explain draft decision | 19 Oct 2016 |
| Submissions due on draft decision | 1 Dec 2016 |
| Powerlink to submit revised proposal to AER | 1 Dec 2016 |
| Further submissions due, including on revised proposal | 23 Dec 2016 |
| AER to publish final decision | No later than 30 Apr 2017 |

Draft decision total revenue requirement (\$m, 2016-17)



AER's draft decision and Powerlink's proposed annual building block costs (\$million, 2016-17)



Impact of draft decision on customer bills (\$nominal)

| | 2016–17 | 2017–18 | 2018–19 | 2019–20 | 2020–21 | 2021–22 |
|--|-------------------|--------------|----------|----------|-----------|----------|
| AER draft decision | | | | | | |
| Residential annual bill | 1611 ^a | 1562 | 1564 | 1566 | 1569 | 1571 |
| Annual change ^c | | -49 (-3.1%) | 2 (0.1%) | 2 (0.1%) | 3 (0.2%) | 2 (0.1%) |
| Small business with 10 000 kWh consumption annual bill | 3014 ^b | 2921 | 2925 | 2930 | 2935 | 2939 |
| Annual change ^c | | -93 (-3.1%) | 4 (0.1%) | 4 (0.1%) | 6 (0.2%) | 4 (0.1%) |
| Small business with 20 000 kWh consumption annual bill | 5249 ^b | 5088 | 5094 | 5102 | 5112 | 5119 |
| Annual change ^c | | -161 (-3.1%) | 7 (0.1%) | 7 (0.1%) | 10 (0.2%) | 7 (0.1%) |
| Powerlink proposal | | | | | | |
| Residential annual bill | 1611 ^a | 1570 | 1572 | 1574 | 1578 | 1580 |
| Annual change ^c | | -41 (-2.6%) | 2 (0.1%) | 2 (0.2%) | 3 (0.2%) | 2 (0.1%) |
| Small business with 10 000 kWh consumption annual bill | 3014 ^b | 2936 | 2941 | 2945 | 2951 | 2956 |
| Annual change ^c | | -78 (-2.6%) | 4 (0.1%) | 5 (0.2%) | 6 (0.2%) | 4 (0.1%) |
| Small business with 20 000 kWh consumption annual bill | 5249 ^b | 5114 | 5121 | 5129 | 5139 | 5147 |
| Annual change ^c | | -135 (-2.6%) | 7 (0.1%) | 8 (0.2%) | 10 (0.2%) | 8 (0.1%) |

Draft decision on Powerlink's rate of return (% nominal)

| | AER previous decision (2012–17) | Powerlink proposal (2017–18) | AER draft decision (2017–18) | Allowed return over 2017–22 regulatory control period |
|-------------------------------------|---------------------------------|------------------------------|------------------------------|---|
| Return on equity (nominal post-tax) | 9.37 | 7.30 | 6.50 | Constant (6.5%) |
| Return on debt (nominal pre-tax) | 8.10 | 5.20 | 4.79 | Updated annually |
| Gearing | 60 | 60 | 60 | Constant (60%) |
| Nominal vanilla WACC | 8.61 | 6.04 | 5.48 | Updated annually for return on debt |
| Forecast inflation | 2.60 | 2.45 | 2.45 | Constant (2.45%) |

Rate of Return

- In its proposal Powerlink used the AER's approach to determining the rate of return (RoR) as set out in the AER's RoR guideline
- At the time of the decision, there was a difference between our draft decision RoR (5.48%) and Powerlink's proposed RoR (6.04%).
- Difference due purely to changes in financial market conditions since Powerlink submitted its proposal
- We will update the Rate of Return again, for the final decision and by reference to the averaging periods that Powerlink has nominated.

Depreciation

- We do not accept Powerlink's proposed regulatory depreciation allowance of \$623.2 million (\$ nominal) for the 2017–22 regulatory control period.
- Instead, we determine a regulatory depreciation allowance of \$605.8 million (\$ nominal) for Powerlink.
- This represents a decrease of \$17.4 million (or 2.8 per cent) on the proposed amount.

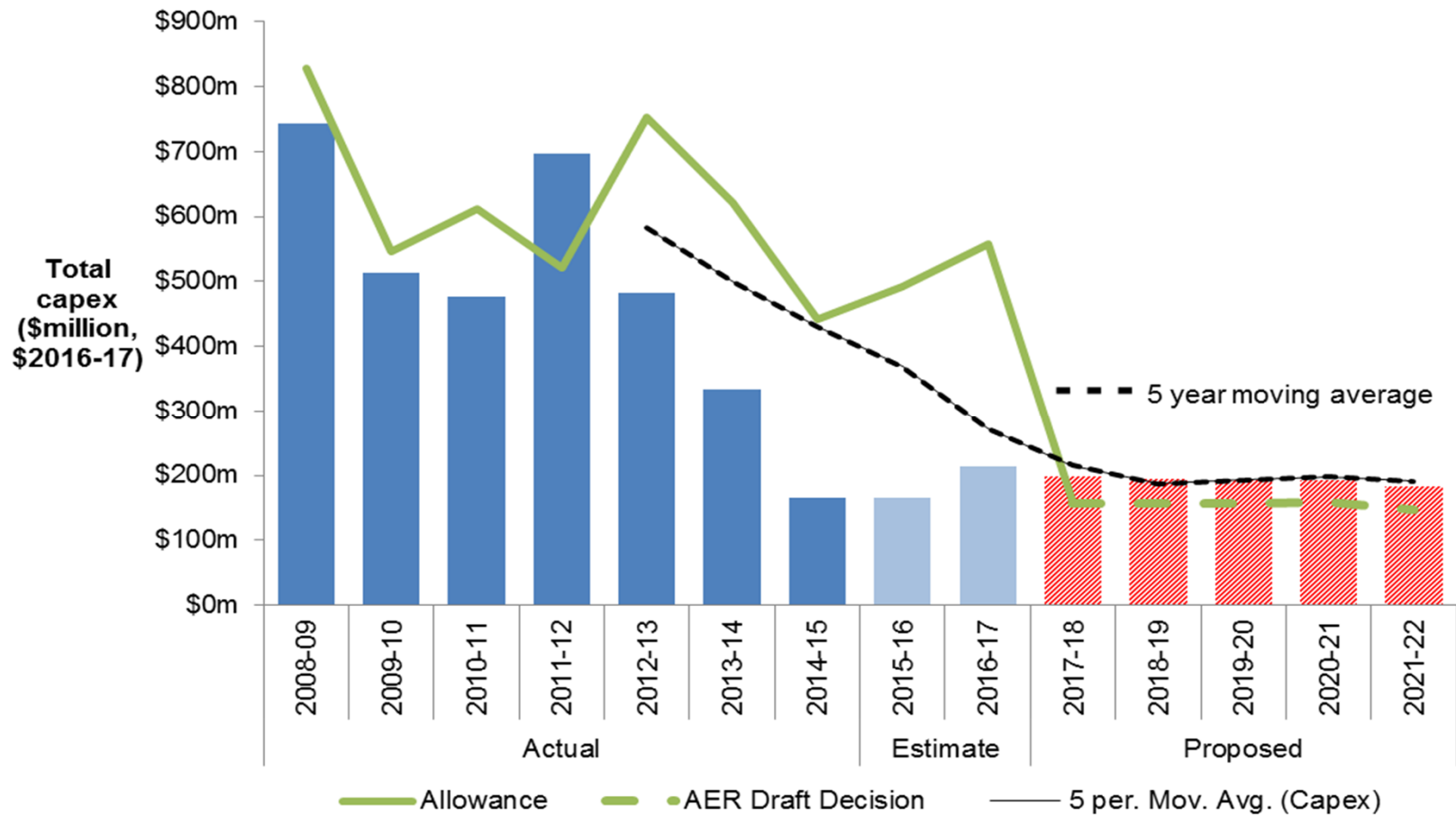
Depreciation (continued)

- We accept Powerlink's proposed straight-line method, and standard asset lives.
- We also accept the proposed weighted average method to calculate the remaining asset lives as at 1 July 2017.
- Difference reflects: the opening RAB as at 1 July 2017, expected inflation rate and forecast capital expenditure.

Capital expenditure

- Our draft decision approves \$775.2 million (\$2016–17) in capex for the 2017–22 regulatory control period. This is or 19 per cent lower than Powerlink’s proposed value of \$959.7 million.
- A key component of our draft decision includes reductions in replacement capital expenditure (repex)
- We were not satisfied that Powerlink’s forecast asset replacement lives used in its repex modelling are realistic, prudent and efficient. We consider that the asset lives proposed by Powerlink were shorter than efficient lives.

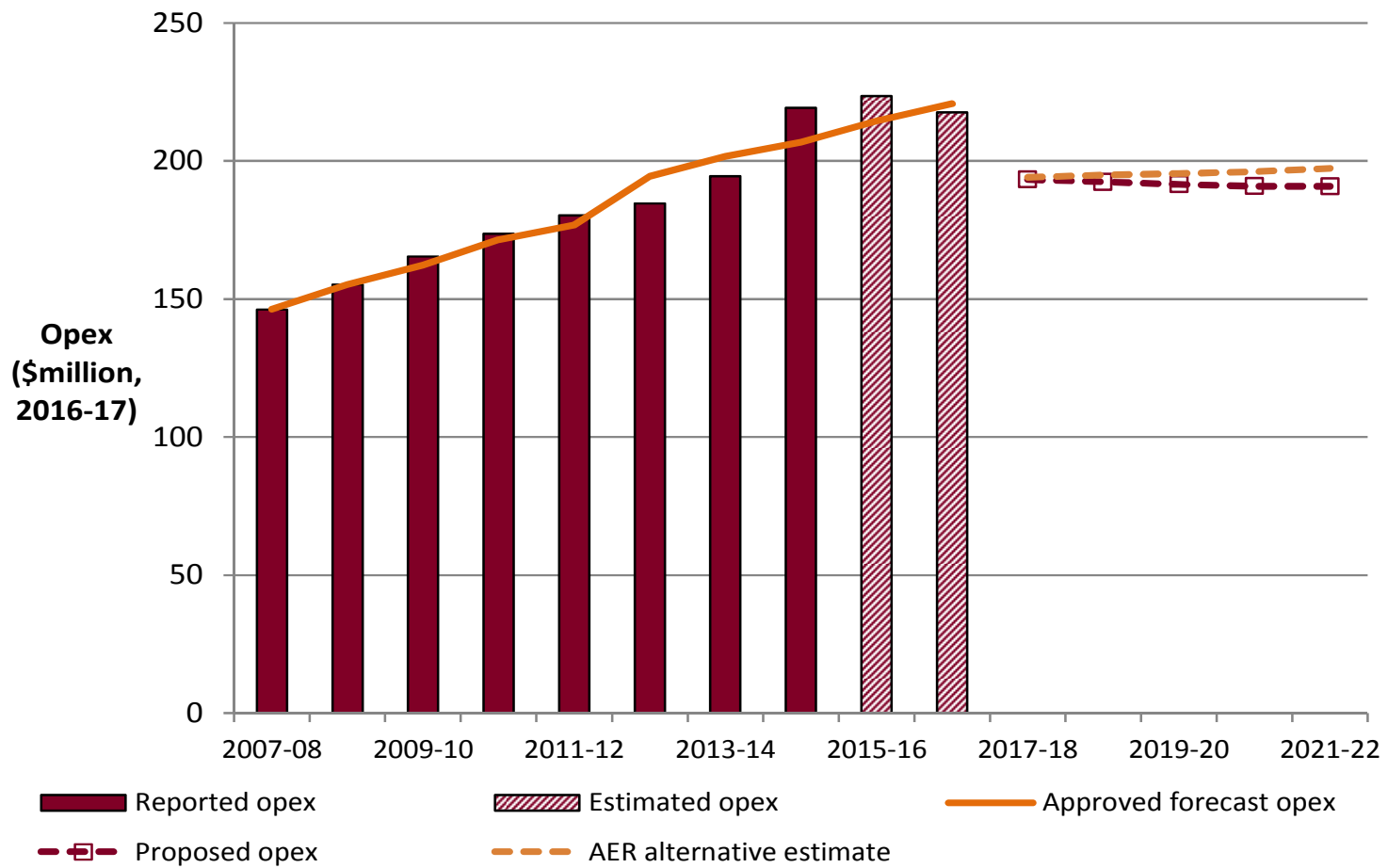
Actual and forecast capex 2014-22 (\$million, 2016-17)



Operating expenditure

- Our draft decision accepts Powerlink's opex forecast of \$976.7 million (\$2016–17) over the 2017–22 regulatory period. Powerlink's proposal is lower (in real terms) than its annual opex spend in the 2012–17 regulatory period.
- We developed an alternative estimate using our standard 'base-step-trend' approach. Our alternative estimate is higher than Powerlink's proposal. So we accepted the Powerlink forecast.

Draft decision on forecast operating expenditure (\$million, 2016-17)



RAB and profitability issues

- The CCP raised concerns about:
 - indexation of the RAB
 - consistency with the WACC and gearing, and
 - analysis of profitability
- In the Draft Decision we explained:
 - Our approach to rate of return is consistent with indexation of the RAB
 - Not persuaded to depart from debt/equity gearing of 60/40
 - Note there is merit in analysis of profitability outcomes. However, we identified specific issues with the CCP members' analysis that would need to be addressed.

**Consumer Challenge Panel
presentation**

Powerlink presentation

Questions?

Next steps

- Submissions due by 1 December 2016
- Revised proposal due by 1 December 2016
- Further submissions (on revised proposal) due by 23 December 2016
- Final decision due by 30 April 2017

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