Determination Network support pass through for 2020–21 regulatory year

Powerlink

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AUSTRALIAN ENERGY REGULATOR

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Overview

On 20 September 2021, Powerlink applied to the Australian Energy Regulator (AER) to pass through costs relating to network support for the 2020–21 regulatory year.

Powerlink is the provider of electricity transmission network services in Queensland.

Network support refers to non-network solutions used by transmission network service providers (TNSPs) as a cost effective substitute for network augmentation. Potential non-network solutions include local generation, co-generation, demand side response and services from a Market Network Service Provider. Generally, network support is seen as desirable where it can cost effectively substitute for network build and is promoted by allowing TNSPs to pass through network support payments which are different to those forecast and are beyond the TNSPs' control[1]. In addition, unlike other pass throughs, network support pass through events are not subject to any materiality test under the regulatory regime, which is intended to further promote such measures.

We have assessed Powerlink's pass through application in accordance with the National Electricity Rules (NER) and our procedural guideline for preparing a transmission network support pass through application.[2]

We determine that a positive network support event has occurred, and the appropriate positive network support pass through amount is $2,512,590 ($nominal, 2022–23). This amount will be added to allowed revenues for the next regulatory year (2022–23) and result in slightly higher transmission charges (other things constant).

[1] See, National Electricity Rules (NER), Chapter 10 (definition of 'network support payment').

[2] AER, Procedural guideline for preparing a transmission network support pass through application, June 2011.

1 Determination

We consider that a positive network support event has occurred[3] and approve a positive network support pass through amount of $2,512,590 ($nominal, 2022–23). This is due to network support costs being higher in 2020–21 than the allowance forecast for such costs in Powerlink's revenue determination. The approved network support pass through amount will be adjusted in Powerlink's maximum allowed revenue in the 2022–23 regulatory year in accordance with the procedures set out in Powerlink's 2017–22 revenue determination.

The NER require us to determine the amount that should be passed through to customers.[4] We base our decision on an assessment of the factors set out in clause 6A.7.2(i) of the NER. Powerlink proposed a positive network support pass through amount of $2,536,987 ($nominal, 2022–23) to recover from its transmission network users, submitted on 20 September 2021.

We have adjusted Powerlink's proposed network support pass through amount by applying the 2020–21 percentage change in the December quarter CPI figures in the escalations of the actual and forecast network support costs. In addition, we applied the 2021–22 weighted average cost of capital (WACC) from Powerlink's current 2017–22 determination when escalating the figure to the end of the 2021–22 regulatory year and the 2022–23 WACC from Powerlink's 2022–27 draft decision when escalating the figure to the middle of the 2022–23 regulatory year. This approach ensured we used the most up to date data in our calculation.

[3] A positive change event is defined in the NER as a pass through event which entails the transmission network service provider incurring materially higher costs in providing prescribed transmission services than it would have incurred but for that event. See NER, chapter 10 Glossary.

[4] NER, cl. 6A.7.2(d).

2 Powerlink's application

Powerlink submitted its network support pass through application on 20 September 2021. The application is available on our website.[5]

2.1 Background

Revenue determinations for TNSPs include forecast allowances for network support payments.

A network support event occurs when the actual amount of network support payments differs from the forecast amount allowed in the determination. Differences generally arise because the amount of network support required by a TNSP in a regulatory year is dependent on factors that are outside the control of the TNSP, such as weather conditions, demand levels and electricity usage patterns. The difference between the forecast cost of network support and the actual cost of network support is passed through to users in higher (or lower) charges for the use of the TNSP's transmission services.

2.2 Regulatory requirements

Clause 6A.7.2 of the NER provides that a TNSP may apply to the AER for a determination on a positive or negative network support event following a regulatory year.

A positive or negative network support event entails a TNSP making higher or lower network support payments in the preceding regulatory year than the amount of network support payments (if any) that is provided for in the annual building block revenue requirements for the TNSP for that regulatory year.

Where a positive or negative network support event occurs, the AER must determine a network support pass through amount.[6]

Clause 6A.7.2(i) of the NER lists the relevant factors that the AER must consider when making a determination on a positive or negative network support event:

> (1) the matters and proposals set out in any statement given to the AER by the Transmission Network Service Provider under paragraph (c);
>
> (2) in the case of a positive network support event, the increase in costs in the provision of prescribed transmission services that the provider has incurred in the preceding regulatory year as a result of the positive network support event;
>
> (3) in the case of a positive network support event, the efficiency of the provider's decisions and actions in relation to the risk of the event, including whether the provider has failed to take any action that could reasonably be taken to reduce the magnitude of the positive network support event and whether the provider has taken or omitted to take any action where such action or omission has increased the magnitude of the amount in respect of that event;
>
> (4) the time cost of money based on the allowed rate of return for the provider for the relevant regulatory control period;

[5] https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/cost-pass-throughs

[6] NER, cl. 6A.7.2(d) and 6A.7.2(f).

(5) the need to ensure that the provider only recovers any actual increment in costs under this paragraph (i) to the extent that such increment is solely as a consequence of a network support event; and

(6) any other factors the AER considers relevant.

The NER does not require that any materiality threshold be applied to network support pass throughs as opposed to other or most pass through events. The reason for this is to encourage the use of non-network solutions.

2.3 Guidelines for transmission network support pass through applications

We released a guideline detailing our approach to assessing network support cost pass throughs in June 2011 (guideline).[7] The guideline was prepared in order to assist TNSPs in preparing their network support pass through applications. The guideline increases the transparency of the process applying to network support pass through arrangements.

The guideline provides information regarding what steps we will take in assessing an application for a network support cost pass through, and what information is required from TNSPs for the process. The basic steps to assessing an application are:

- Assessing whether a network support event has occurred
- Verifying the network support payments
- Checking the calculations for the pass through amount, including steps taken to compensate the TNSP or its users for the time cost of money
- Assessing the efficiency of a network support provider's decisions and actions in relation to the risk of an event.

For further detail, the guideline can be found at http://www.aer.gov.au/node/972

We have considered Powerlink's application for a network support pass through in accordance with the NER and the guideline, and our reasoning is set out below.

2.4 Powerlink's proposed pass through amount

On 20 September 2021, Powerlink applied to the AER for a positive network support pass through of $2,536,987 ($nominal, 2022–23). This reflects Powerlink's calculation of the difference between the allowance Powerlink received for network support payments as part of its revenue determination and what Powerlink actually spent on network support in the relevant period. Powerlink's revenue determination for the 2017–22 regulatory control period included an allowance for $0 ($2020–21) for the 2020–21 regulatory year.[8] Thus, this network support pass through application relates to network support payments which Powerlink have incurred as a result of a network support contract it entered into after its revenue determination for the 2017–22 regulatory control period.

The pass through relates to network support services incurred in response to the Australian Energy Market Operator's (AEMO's) report "Notice of Queensland System Strength

[7] AER, *Procedural guideline for preparing a transmission network support pass through application*, June 2011.

[8] AER, *Powerlink 2017–22 – Post tax revenue model - 2021–22 return on debt update*, January 2021; AER analysis.

Requirements and Ross Fault Level Shortfall". This report required adequate system strength services in place to meet this shortfall by 31 August 2021.

In response to this, Powerlink entered into a short-term agreement with CleanCo Queensland to provide system strength services between 1 July 2020 and 31 December 2020 through utilising its existing assets in Far North Queensland. This was done to quickly address the fault level shortfall identified by AEMO. Powerlink also undertook retuning of invertors at the Daydream, Hamilton, Hayman and Whitsunday solar farms in North Queensland as part of the longer-term solution to address the system strength requirements at the Ross 275kV node.[9]

Powerlink submitted that the variation in expenditure compared with the allowance only reflects the costs it accrued during the 2020–21 regulatory year, in relation to the aforementioned actions. Powerlink noted that it has yet to be invoiced for the costs of retuning the North Queensland solar farms which it estimated to be approximately $400,000. Because of this, Powerlink indicated it may submit a further network support pass through application for the 2021–22 regulatory year seeking to recover those costs.[10]

[9] Powerlink, Network Support Pass Through Application for 2020–21, September 2021, p.3.

[10] Powerlink, Network Support Pass Through Application for 2020–21, September 2021, p.1.

3 AER assessment

3.1 Positive network support event

The NER defines network support event as follows[11]:

> **Network support event**
>
> If, at the end of a regulatory year of a regulatory control period, the amount of network support payments made by a Transmission Network Service Provider for that previous regulatory year is higher or lower than the amount of network support payments (if any) that is provided for in the annual building block revenue requirement for the Transmission Network Service Provider for that regulatory year, this constitutes a network support event.

We determine that a positive network support event has occurred because the network support payments made by Powerlink in 2020–21 ($2,324,295, $2020–21) were higher than the amount of network support payments provided for in Powerlink's 2017–22 determination ($0, $2020–21).

3.2 Relevant factors

As aforementioned, clause 6A.7.2(i) of the NER sets out a number of factors that we must take into account when determining the approved pass through amount following a network support event.

We have given regard to the appropriate factors:

- We have considered the matters and proposals set out by Powerlink
- We have calculated the increase in costs Powerlink has occurred as a result of the positive network support event
- We are satisfied that Powerlink's decisions and actions in relation to the risk of the event were efficient
- We have taken into account the time cost of money to calculate the appropriate pass through amount
- We are satisfied that the costs Powerlink will recover under this determination are solely a consequence of the aforementioned network support event
- We do not consider any other factors to be relevant.

3.3 Calculation of pass through event

In its application submitted to the AER on 20 September 2021, we consider that Powerlink has incorrectly calculated the positive network support pass through amount.

[11] NER, chapter 10 Glossary.

To calculate the positive network support pass through amount, we have used the network support cost amount of $2,314,358 ($nominal, 2020–21) reported in Powerlink's 2020–21 Category Analysis data, provided as part of its response to our Regulatory Information Notice. This amount matches the network support cost amount in its application.[12] Actual network support payments are assumed to be valued at middle of the year terms.[13] Therefore, we escalated this amount by applying the 2020–21 CPI figure (0.86 per cent) over a time period of half a year, and determined the value of the network support cost amount at June 2021 as $2,324,295 ($2020–21). This amount is slightly lower than the network support cost amount in Powerlink's application due to Powerlink's use of the 2019–20 CPI figure (1.84 per cent) during the escalation process.

We are satisfied that Powerlink has reasonably incurred actual network support costs of $2,324,295 ($2020–21) compared to the applicable regulatory allowance of $0 ($2020–21). The variation in the expenditure meets the definition of a network support event in the NER. The contract for these network services was awarded on the basis of a competitive expression of interest (EOI) process[14] and we consider this an appropriate method for maintaining costs at an efficient level.[15]

To account for the time cost of money, WACC escalations are applied for a period of one and a half year time when determining the network support pass through amount. Therefore, in our calculation we applied:

- 2021–22 nominal WACC of 5.67 per cent over one year, which represents the year in which the network support pass through application is submitted and assessed by the AER.[16]
- a further 2022–23 nominal WACC of 4.65 per cent for half a year, which represents the period where the network support pass through amount is passed through to customers. As this time period falls outside Powerlink's current 2017–22 determination, we have relied on the nominal WACC figure in Powerlink's 2022–27 draft decision.[17]

This method produced an amount slightly lower than what was proposed in Powerlink's application, due to Powerlink's use of the 2021–22 nominal WACC of 5.67 per cent throughout the entire July 2021 to December 2022 escalation period.

Consequently, we determine that a positive network support event has occurred and the appropriate positive network support pass through amount is $2,512,590 ($nominal, 2022–23). This amount will be recovered from allowed revenues for the next regulatory year (2022–23) and result in higher transmission charges (other things constant).

[12] Powerlink, *Network Support Pass Through Application for 2020–21*, September 2021, p.3

[13] AER, *Procedural guideline for preparing a transmission network support pass through application*, June 2011, p. 13.

[14] Powerlink, *Network Support Pass Through Application for 2020–21*, September 2021, p.4.

[15] NER, cl. 6A.7.2(i)(3).

[16] AER, *Powerlink 2017–22 – Post tax revenue model - 2021–22 return on debt update*, January 2021.

[17] AER, *Draft decision – Powerlink transmission determination – Post-tax revenue model*, September 2021

3.4 Timing matters

The NER provide that an application for network support pass through must be made within 60 business days of the end of the relevant regulatory year.[18] We must then make a determination within 60 business days of the business' application to us.[19]

The relevant regulatory year ended on 30 June 2021 and Powerlink made its network support pass through application on 20 September 2021, 58 business days later.

[18] NER, cl. 6A7.2(c).

[19] NER, cl. 6A7.2(e).

Glossary

Term	Definition
AER	Australian Energy Regulator
AEMO	Australian Energy Market Operator
CPI	Consumer price index
EOI	Expression of Interest
Guideline	Procedural guideline for preparing a transmission network support pass through application
NER	National Electricity Rules
TNSP	Tansmission network service providers
WACC	Weighted average cost of capital