Determination

Increase to minimum wood pole interventions cost pass through

Powercor

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AUSTRALIAN ENERGY REGULATOR

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Overview

On 27 September 2021, Energy Safe Victoria (ESV) issued a notification under section 109 of the *Electricity Safety Act 1998 (Vic)* (Electricity Safety Act) requiring Powercor to update its bushfire mitigation plan (BMP) to specify a minimum volume of wood pole interventions. ESV provisionally accepted Powercor's revised BMP on 23 December 2021.

On 1 March 2022, Powercor submitted a cost pass through application (Powercor's application) seeking to recover costs it is likely to incur as a result of the required changes to its BMP (the Regulatory Obligation). Powercor is seeking to recover $112.8 million ($2020–21) in incremental costs, resulting in $14.0 million ($ nominal) in incremental revenue over the 2021–26 regulatory period.[1]

Under the National Electricity Rules (NER), Powercor can seek the approval of the Australian Energy Regulator (AER) to pass through to network users a positive pass through amount in respect of certain events (referred to in the NER as positive change events).[2] A cost pass through application must address specified matters.[3]

If the AER determines that a positive change event has occurred in respect of a cost pass through application, the AER is required to determine (within a specified timeframe):

- the approved pass through amount, and
- how much of that amount should be passed through to distribution network users in the regulatory year, and each subsequent regulatory year, in which the positive change event occurred,

taking into account the matters referred to in clause 6.6.1(j) of the NER.[4]

On 11 March 2022, we published Powercor's application on our website and invited stakeholder submissions. We received two submissions. Both parties made a confidential submission and requested that it not be made public; however, we have had regard to these submissions in forming our decision.

This determination sets out our assessment of Powercor's application and addresses the requirements of clause 6.6.1 of the NER.

We are satisfied that the Regulatory Obligation meets the definition of a regulatory change event. Based on our consideration of the matters set out in clause 6.6.1(j) of the NER, we determine to allow the pass through of the costs proposed in Powercor's application.

1 All amounts in this determination are in real $2020–21 unless otherwise specified.

2 NER, cl. 6.6.1(a1) outlines the events which may be a *pass through event*. NER, Chapter 10 (Glossary) defines a *positive change event*.

3 NER, cl. 6.6.1(c).

4 NER, cl. 6.6.1(d).

1 Introduction

This section sets out the AER's role in assessing cost pass through applications from electricity distribution network service providers (DNSPs) and provides information on Powercor's application.

1.1 Who we are and our role in this process

The AER works to ensure all Australian energy consumers are better off now and in the future. Consumers are at the heart of our work, and we focus on ensuring a secure, reliable and affordable energy future for Australia. We are the economic regulator for electricity distribution and transmission services in the National Electricity Market (NEM). Our electricity-related powers and functions are set out in the National Electricity Law (NEL) and NER.[5]

The AER regulates Powercor's revenues through five-year distribution revenue determinations. Powercor's current revenue determination for the 2021–26 regulatory period runs from 1 July 2021 to 30 June 2026.

We are responsible for assessing cost pass through applications.[6] Under the NER, a DNSP may apply to us seeking the recovery of additional costs incurred, or are expected to be incurred, during a regulatory period if predefined events occur as specified in either the NER or in the revenue determination.[7]

1.2 Powercor's application

On 27 September 2021, ESV issued a request pursuant to section 109 of the Electricity Safety Act to Powercor to submit a revised BMP. Relevantly, ESV requested Powercor to state in its BMP that it would:

- intervene on a minimum of 34,650 wood poles, including:[8]
    - a minimum of 25,241 wood pole interventions in high bushfire risk areas and/or electric line construction areas[9], with a minimum of 13,614 of these interventions to be replacements
    - replace no less than 3,519 reinforced wood poles
- complete the minimum interventions between 1 January 2022 and 31 December 2026.

5 In addition to regulating transmission and distribution in the NEM and the Northern Territory, we also monitor the wholesale electricity market to ensure suppliers comply with the legislation and rules, taking enforcement action where necessary, and regulate retail energy markets in Queensland, New South Wales, South Australia, Tasmania (electricity only) and the ACT.

6 NER, cl. 6.6.1(d).

7 NER, cl. 6.6.1(a1).

8 Intervene means to replace or reinforce (i.e. stake) a wood pole.

9 Electric line construction areas are hazardous bushfire areas designated by the Victorian Government and have special safety standards under the Electricity Safety (Bushfire Mitigation) Regulations 2013.

The purpose of this requirement is to "address concerns held by ESV that [Powercor's] current wood pole management practices…will not achieve sustainable and safe outcomes for the Victorian community, particularly in HBRA."[10] A HBRA is a Hazardous Bushfire Risk Area.

ESV provisionally accepted Powercor's revised BMP on 23 December 2021.

On 1 March 2022, Powercor submitted a cost pass through application (Powercor's application) proposing a positive pass through amount of $112.8 million in incremental costs that it forecasts it will incur as a result of the Regulatory Obligation, as shown in Table 1.

Powercor submits that the incremental costs are required to intervene on 11,060 wood poles. This volume is the difference between the wood pole interventions that we allowed for in our 2021–26 regulatory determination and the volume of wood pole interventions required by the Regulatory Obligation within the 2021–26 regulatory period.[11]

Table 1 Powercor – Proposed positive pass through amount ($million, $2020–21)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
Capital expenditure (capex)	11.9	23.8	24.0	24.1	24.3	108.0
Operating expenditure (opex)	0.5	1.1	1.1	1.1	1.1	4.8
Total	12.4	24.9	25.0	25.2	25.4	112.8

Source: Powercor.

Note: some cells may not add up due to rounding.

The revenue impact of the proposed pass through amount is $14.0 million ($ nominal) over the last three years of the 2021–26 regulatory period.

1.3 Structure of determination

This document sets out our assessment and determination, amongst other things, on whether a cost pass through event has occurred, the pass through amount, the time period for the recovery of the pass through amount, and our reasons for the determination.

The decision is structured as follows:

- Section 2 sets out our determination on Powercor's cost pass through application
- Section 3 outlines the relevant regulatory requirements that we have had regard to, and our assessment approach
- Section 4 sets out our reasons for the determination
- Section 5 sets out our assessment of Powercor's cost pass through application against the NER requirements.

[10] ESV, *Request pursuant to section 109(1) of the Electricity Safety Act 1998*.

[11] Powercor, *Increase to minimum wood pole interventions – pass-through application,* March 2022.

2 Determination

Based on our consideration of all the matters set out in this decision, we determine that Powercor's application, submitted on 1 March 2022, establishes that a pass through event has occurred in respect of the Regulatory Obligation, being a regulatory change event as specified in NER cl. 6.6.1(a1). Our assessment against the requirements of a positive change event is summarised in section 5.

We are satisfied that the Regulatory Obligation constitutes a positive change event as defined under the NER. In particular, we are satisfied that Powercor will incur a material increase in the costs of providing direct control services in the 2021–26 regulatory period as a result of the Regulatory Obligation.

Our determination is to approve a positive pass through amount of $112.8 million. This results in incremental revenue of $14,006,628 ($ nominal), to be recovered over the three remaining regulatory years of Powercor's 2021–26 regulatory period through the X-factors set in the post-tax revenue model (PTRM), as follows:

- $2,271,360 ($ nominal) to be recovered in 2023–24.
- $4,636,519 ($ nominal) to be recovered in 2024–25.
- $7,098,389 ($ nominal) to be recovered in 2025–26.

Sections 4 and 5 set out our assessment of Powercor's cost pass through application and the positive pass through amount.

We estimate that the approved cost pass through amount will add approximately $3 per year ($ nominal) to the average residential customer's bills from 1 July 2023 to 30 June 2026.[12]

[12] Our expected bill impact approach shows the incremental dollar impact due to the incremental revenue from the pass through application, while holding all other component costs that make up the electricity bill constant. Powercor's 2022–23 pricing proposal is used as the source for the base bill as at 30 June 2023. Any difference in expected bill impact figures with Powercor's proposal is due to our different bill impact approach.

3 Relevant regulatory requirements and assessment approach

The pass through mechanism recognises that an efficient revenue allowance cannot account for certain matters that are uncertain and outside the control of the business and which cannot be prevented or mitigated by prudent operational risk management. A cost pass through enables a network service provider to recover the costs of defined unpredictable, high-cost events not factored into our five-year revenue determination for the business.

Clause 6.6.1(a1) of the NER defines a pass through event as one of the following prescribed pass through events for all DNSPs:

1) a regulatory change event
2) a service standard event
3) a tax change event
4) a retailer insolvency event, and
5) any other event specified in a distribution determination as a pass through event for the determination (nominated pass through event).

The first step in our assessment is to determine whether a pass through event has occurred and examine timing matters, e.g. whether an application is submitted within the timeframe set out in the NER. Once we have determined that a pass through event has occurred, we are to determine whether it is a positive (or negative) change event.

The NER defines a positive change event for a DNSP as:

> "a pass through event…which entails the DNSP incurring materially higher costs in providing direct control services than it would have incurred but for that event…"[13]

We undertake this assessment with reference to the NER and the revenue determination applicable to Powercor when the Regulatory Obligation took effect, which is Powercor's distribution determination for the 2021–26 regulatory period.[14]

As part of this process, we examine whether Powercor's application has addressed matters specified in clause 6.6.1(c) of the NER (see section 5 below (Table 4 and Table 5)). We also assess the materiality of the proposed pass through amount.

Clause 6.6.1(d) of the NER provides that if the AER determines that a positive change event has occurred, the AER must determine:

- the approved pass through amount, and
- the amount that should be passed through to distribution network users in the regulatory year, and each regulatory year after that, in which the positive change event occurred,

taking into account the matters referred to in clause 6.6.1(j) of the NER.

[13] NER, Chapter 10 (Glossary).

[14] See https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/powercor-determination-2021-26/final-decision.

3.1 Timing matters

To seek the approval of the AER to pass through a positive pass through amount, clause 6.6.1(c) of the NER requires a DNSP to submit to the AER a written statement specifying a range of details relating to the event within 90 business days of the relevant positive change event occurring.

The NER requires us to make a determination within the timeframe specified in clause 6.6.1(e). That is, within 40 business days from the later of the date the AER received Powercor's cost pass through application and the date it received any additional information required by it through a notice issued under clause 6.6.1(e1) of the NER.

Clause 6.6.1(k1) additionally provides that if the AER is satisfied that the making of a determination in relation to a pass through application involves issues of such complexity or difficulty that the time limit should be extended, the AER may extend the time limit by a further period of up to 60 business days, provided that it gives written notice to the DNSP of that extension at least 10 business days before the expiry of the time limit.

4 Reasons for determination

The sections below set out the reasons for our determination.

4.1 Positive change event

We must determine whether the pass through event qualifies as a "positive change event". That is, whether Powercor incurred, or is likely to incur, materially higher costs in providing direct control services than it would have incurred but for the pass through event.

Relevantly, the NER defines "materially" as:[15]

> "For the purposes of the application of clause 6.6.1, an event results in a DNSP incurring materially higher or materially lower costs if the change in costs (as opposed to the revenue impact) that the DNSP has incurred and is likely to incur in any regulatory year of a regulatory period, as a result of that event, exceeds 1% of the annual revenue requirement for the DNSP for that regulatory year."

Table 2 shows that the costs that Powercor is likely to incur in providing direct control services as a result of the Regulatory Obligation meet the materiality threshold for the 2021–26 regulatory period. Please note that Table 2 is in nominal terms.

Table 2 AER – Materiality assessment of the Regulatory Obligation ($million, nominal)

	2021-22	2022-23	2023-24	2024-25	2025-26	Total
Cost pass through opex	0.5	1.1	1.1	1.2	1.2	5.1
Cost pass through capex	12.1	24.8	25.4	26.1	26.8	115.2
Total incremental capex and opex	**12.6**	**25.9**	**26.5**	**27.2**	**28.0**	**120.3**
AER approved unsmoothed revenues as per latest approved PTRM	646.1	671.4	691.8	712.3	738.1	3459.7
Materiality	**2.0%**	**3.9%**	**3.8%**	**3.8%**	**3.8%**	**3.5%**

Source: AER analysis.

Note: Opex amounts exclude adjustment to debt raising costs.

4.2 Regulatory change event

The NER define a regulatory change event as follows:[16]

> **Regulatory change event**
>
> A change in a regulatory obligation or requirement that:
>
> (a) falls within no other category of pass through event; and
>
> (b) occurs during the course of a regulatory control period; and

[15] NER, Chapter 10 (Glossary).

[16] NER, Chapter 10 (Glossary).

(c) substantially affects the manner in which the Transmission Network Service Provider provides prescribed transmission services or the Distribution Network Service Provider provides direct control services (as the case requires); and

(d) materially increases or materially decreases the costs of providing those services.

Relevantly, the NEL defines a **regulatory obligation or requirement** as follows:[17]

> A regulatory obligation or requirement is an obligation or requirement under an Act of a participating jurisdiction, or any instrument made or issued under or for the purposes of that Act…that materially affects the provision, by a regulated network service provider, of electricity network services that are the subject of a distribution determination or transmission determination.

We consider that the Regulatory Obligation satisfies the definition of a regulatory change event.

4.3 Timing of Powercor's application

Clause 6.6.1(c) of the NER requires a DNSP to submit a pass through application to us within 90 business days of the positive change event occurring.

We consider the Regulatory Obligation to have occurred when Powercor's BMP was provisionally approved by ESV on 23 December 2021. We received Powercor's pass through application on 1 March 2022, which was less than 90 business days after the positive change event occurred.

Following our initial assessment of Powercor's application, we issued an information notice to Powercor (on 28 March 2022) under clause 6.6.1(e1) of the NER, requesting further information on the scope of works and associated costs.

Subsequently, on 10 May 2022 we issued a notice to Powercor extending the time limit for making this determination in accordance with clause 6.6.1(k1) of the NER. Accordingly, we are required to make this determination by 2 September 2022.

4.4 Assessment of the pass through amount

In assessing a pass through application, the NER requires us to take into account a range of relevant matters,[18] including the need to ensure that Powercor only recovers any actual or likely increment in costs, to the extent that such an increment is solely as a consequence of the pass through event,[19] and that Powercor does not recover costs that have or will be factored into Powercor's annual revenue requirement.[20]

[17] NEL, sec. 2D(1)(b)(v).

[18] NER, cl. 6.6.1(j).

[19] NER, cl. 6.6.1(j)(5).

[20] NER, cl. 6.6.1(j)(7).

We approach this assessment by ensuring, amongst other things, that:

- the pass through amount reflects only those costs likely to be incurred as a result of the Regulatory Obligation, and not costs incurred as a result of other positive change events, business-as-usual costs, or costs of increasing the scope of network services provided by Powercor
- the costs incurred are prudent and efficient costs required to fulfil the Regulatory Obligation;
- the pass through amount reflects only the incremental costs of the Regulatory Obligation, taking into account deductions for actual and expected cost savings that will occur as a result of works undertaken to fulfil the Regulatory Obligation. For example, the replacement of pole top structures together with wood poles may result in lower future replacement of pole top structures, which should be deducted from the costs to be passed through.

We are satisfied that Powercor's estimates of the increase in capex and opex costs due to the Regulatory Obligation, accounting for the identified avoided costs, are prudent and efficient. Our reasons for this are discussed below. As such, our determination on the approved incremental capex and opex costs for the Regulatory Obligation is the proposed $112.8 million set out in Table 1 earlier in this determination.

4.4.1 Costs reflect adjustments for savings to business-as-usual costs resulting from the Regulatory Obligation

We are satisfied that Powercor's pass through amount reflects deductions for savings to business-as-usual costs resulting from the Regulatory Obligation. Powercor proposes an expenditure decrement of $0.53 million in the 2021–26 regulatory period to account for pole-top structures. These will be replaced in conjunction with the incremental wood pole replacements and therefore no longer require the funding approved in our 2021–2026 distribution determination.[21] We asked Powercor to provide its modelling for the cost savings, and find that its calculations are reasonable.

4.4.2 Powercor's proposed positive pass through amount is prudent and efficient

We have assessed Powercor's proposed positive pass through amount of $112.8 million, and are satisfied that it reasonably reflect prudent and efficient costs. In its application, Powercor provided its forecast pole condition data and cost breakdowns. In response to our information request that we sent on 25 March 2022, Powercor provided further details of its forecasting approach and reasons for its assumptions. Our key areas of focus are discussed below.

Wood pole replacement unit rates

We examined Powercor's proposed replacement unit rates ($13,365 per pole) as they are 28 per cent higher than the unit rates that we used in our final determination allowance

[21] Powercor, *Increase to minimum wood pole interventions – pass-through application,* March 2022, p 17.

($10,437).[22] However, they are only 2 per cent higher than recent actual rates (2017–2020, volume weighted).

Powercor explained that the higher unit rates are due to the need to outsource the labour for the higher volumes. The unit rates were calculated from the outcomes of a market tender process that commenced in November 2021. In response to our information request, Powercor provided evidence of its market tender process and explained the basis of its assumptions for estimating the replacement unit rate.

The higher unit rates also reflect a higher proportion of wood poles to be replaced by concrete poles compared with previous years. Powercor demonstrated that it forecasts a relatively higher rate of replacement in the north of its network in the 2021–26. Powercor's practice is to replace all wood poles with concrete poles in the northern region because of a higher incidence of termite infestation.

We met with Powercor on 10 June 2022, and presented our analysis of Powercor's proposed replacement unit rates. We suggested that Powercor may, on average, incur lower replacement unit rates than it had proposed. We explained that, in our view, Powercor would seek efficiencies by using the lowest-cost contractor to the greatest extent possible and for those pole types where savings could be maximised. Powercor responded that, in principle, it accepts the AER's premise. However, there are other deliverability and practical issues that should be considered.

Following our meeting, Powercor provided the following new information:

- completed or issued replacement volumes by pole type and installer (including contractors and Powercor), monthly
- short-term availability of contractors
- how Powercor allocates work to its contractors in practice.

The information provided by Powercor is confidential. However, we consider that the available evidence supports Powercor's proposed replacement unit rates. As such, we consider that the forecast unit rates reasonably reflect efficient costs.

Staking rate

Powercor's proposed replacement and reinforcement volumes imply a staking rate – that is the proportion of pole reinforcements to total interventions – of around 40 per cent. This is comparable to our final decision rate of 41 per cent. However, we would expect the forecast staking rate to be higher. This is because our final decision volumes were sufficient to intervene on Powercor's highest risk poles, which are less likely to be suitable for staking. The pole interventions incremental to our final decision will be on poles that are in relatively better condition or are a lower risk; therefore, we consider that they are more likely to be suitable for staking.

Powercor forecast its reinforcement and replacement volumes by using actual current staking rates (for unserviceable and added-control serviceable poles) or an estimate (for

[22] In our final determination, we accepted Powercor's proposed unit rates as they were lower than actual unit rates in the 2016–2020 regulatory control period.

serviceable poles – as Powercor has historically not intervened on these). It provided its forecast data and the model it used to determine its forecast replacement and reinforcement volumes. Powercor set out its proposed reinforcement and replacement volumes in its BMP.[23]

In our meeting with Powercor, we queried whether the relatively low staking rate implied by Powercor's proposed reinforcement and replacement volumes reflects efficient costs. We also asked for further detail regarding the reinforcement and replacement volumes set out in Powercor's BMP.

Powercor provided a written response on 17 June 2022 addressing our issues. It stated that it understands its BMP imposes an unqualified obligation on it to achieve the total replacement and reinforcement volumes set out in the BMP. It also stated that, in its view, ESV's section 109 request and subsequent section 109 decision together operate to require that the BMP obliges Powercor to achieve the staking rate implied by those figures. Powercor referred to ESV's section 109 decision:[24]

> "We agree that the approach you have proposed is consistent with our request with one exception. We are concerned with the references you have made to 'target' intervention volumes. We require you to deliver to the intervention commitments that you have made, both on a year on year and overall basis."

We also met with ESV on 22 June 2022 to discuss the Regulatory Obligation, and in particular Powercor's proposed replacement and reinforcement volumes in its BMP. ESV confirmed that it intends to hold Powercor to account to deliver the replacement and reinforcement volumes set out in the BMP and that it regards these volumes as a regulatory obligation.

We are satisfied that compliance with the BMP implies that a certain staking rate must be met; and that Powercor has no discretion to modify it except by intervening on higher than the minimum prescribed volumes (i.e. at additional cost to Powercor).

Customer Service Incentive Scheme (CSIS)

Powercor proposes to adjust the CSIS planned outage targets to account for the impact of the higher pole volumes, as shown in Table 3. It submits that it will likely incur the maximum penalty (capped at $1 million) for the remainder of the 2021–26 regulatory period for failing to achieve its CSIS targets for planned interruptions. This is because the Regulatory Obligation will materially increase the number of planned outages that Powercor will incur.

Powercor assessed a number of options to address this issue. Its proposed approach means that the pass through is not expected to change Powercor's incentive to reduce the duration and frequency of planned outages.

[23] Powercor, *Bushfire Mitigation Plan*, revision 9.3, 19 April 2022, table 9.

[24] Energy Safe Victoria, *Decision on Powercor's response in relation to ESV's request pursuant to section 109(1) of the Electricity Safety Act 1998*, 18 February 2022, p. 1.

Table 3 Powercor's proposed amendments to CSIS targets

Planned outages	AER final determination	Proposed targets
SAIDI	65.98	66.25
SAIFI	0.32	0.37

Source: Powercor, Pass through application, Table 4.8.

We have looked at Powercor's planned approach and requested further information to better understand how it calculated its proposed targets. We are satisfied that Powercor's adjustment is appropriate.

We also looked at how the Regulatory Obligation might impact other incentive schemes such as the Service Target Performance Incentive Scheme (STPIS) and F-factor scheme in the 2021–26 regulatory period because of potential improvements to network reliability and bushfire safety. Overall, we consider that the impact on these schemes does not warrant an adjustment to targets. We consider that the Regulatory Obligation will not materially reduce fire-starts or the number of unplanned interruptions, and hence expected incentive payments under the STPIS and the F-factor scheme, in this regulatory period.

Other considerations

We asked Powercor to provide further details to support the following costs and assumptions used in its forecast:

- basis of assumptions to estimate the design time per pole and earthing unit rates
- further explanation of Powercor's requirements for additional resourcing, ensuring only costs required to fulfil the Regulatory Obligation are included and that these costs are not included in forecast capitalised overheads.
- evidence of historical wood to concrete replacements, and an explanation of why the proposed wood to concrete ratio is efficient.

We have examined Powercor's responses to our queries, and are satisfied that these elements of Powercor's application reasonably reflect efficient costs.

Submissions from stakeholders

We received two submissions from stakeholders. Both parties made a confidential submission and requested that it not be made public. We have had regard to these submissions in arriving at our decision.

4.4.3 The proposed positive pass through amount includes only the incremental increase in costs

The Regulatory Obligation requires Powercor to intervene on 34,650 poles between 1 January 2021 to 31 December 2026. However, Powercor's application seeks to only recover costs to intervene on 11,060 wood poles. This volume is the difference between the wood pole interventions that we allowed for in our 2021–26 regulatory determination and the volume of wood pole interventions required by the Regulatory Obligation within the 2021–26 regulatory period. As such, we are satisfied that Powercor's pass through amount includes

only costs that it is likely to incur in the 2021–26 regulatory period, and that are over and above what was provided for in our 2021–26 regulatory determination.

4.4.4 Incremental revenue

Table 4 details our determination on incremental revenue. Please note that Table 4 is in nominal terms.

Table 4 Approved incremental revenue for the Regulatory Obligation ($million, nominal)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
Return on capital	-	0.57	1.63	2.63	3,56	8.38
Return of capital (regulatory depreciation)	-	0.00	0.01	0.02	0.05	0.07
Operating expenditure	0.54	1.11	1.15	1.19	1.24	5.23
Net tax allowance	-	-	-	-	-	-
Incremental annual revenue requirement (unsmoothed)	0.54	1.68	2.78	3.84	4.84	13.68
Incremental annual expected revenue (smoothed)	**-**	**-**	**2.27**	**4.64**	**7.10**	**14.01**

Source: AER analysis

Notes: '0.00' represents a small nonzero number and '–' represents zero. The smoothed and unsmoothed revenues are equal in net present value terms. The difference between the nominal smoothed and unsmoothed total revenues is explained by the time value of money.

Incremental operating expenditure amounts include $0.09 million for debt raising costs.

4.5 Timing of cost pass through recovery

Powercor has proposed to recover the incremental revenue arising from its cost pass through application over the remaining three years of its 2021–26 regulatory period.

We are satisfied that this approach will minimise volatility in Powercor's revenue requirements while still allowing it to recover its efficient costs in a timely manner.

5 NER requirements

For a cost pass through to be determined, there must be a positive change event that results in an eligible pass through amount. Powercor can then submit a pass through application that must address certain matters specified in the NER.[25] We make a determination on Powercor's cost pass through application, and determine the approved pass through amount and the regulatory years in which that pass through amount is to be recovered.[26]

For the reasons set out in Table 5, we are satisfied that a positive change event has occurred, and that Powercor's application relating to the Regulatory Obligation specifies the necessary matters required by the NER. Additionally, after consideration of the matters set out in Table 6, we are satisfied the appropriate positive pass through amount is $112.8 million. This results in incremental revenue of $14.0 million ($ nominal) to be recovered over the three remaining regulatory years of Powercor's 2021–26 regulatory period.

Table 5 Requirements for determining whether a positive change event has occurred

Requirement of the NER	Our consideration
Is the pass through event a regulatory change event, service standard event, tax change event, or retailer insolvency event?[27]	Yes. We consider that the positive pass through event satisfies the criteria of a regulatory change event.
Is the pass though event a contingent project or a trigger event associated with a contingent project?[28]	No.
Does the pass through relate to any other event specified in Powercor's 2021–26 distribution determination as a pass through event for that determination?[29]	No.
Will the regulatory change pass through event result in Powercor incurring materially higher costs in providing direct control services than it would have incurred but for the event?[30]	Yes. As discussed in section 4.1, the additional costs incurred by Powercor in providing direct control services as a result of the Regulatory Obligation meet the materiality threshold.
What is the date on which the positive change event occurred?	For the purpose of complying with 6.6.1(c), we consider that the positive change event occurred on 23 December 2021. This was when ESV provisionally accepted, and Powercor was obligated to comply with, the revised BMP.
Did Powercor submit a written statement of its pass through application within 90 business days of the positive change event occurring?[31]	Yes. Powercor submitted its written statement on 1 March 2022.

25 NER, cl. 6.6.1(c).

26 NER, cl. 6.6.1 (d).

27 NER, cll. 6.6.1(a1)(1) through 6.6.1(a1)(4); and Chapter 10 (Glossary).

28 See the definition of "positive change event" in Chapter 10 (Glossary) of the NER.

29 NER,cl. 6.6.1(a1)(5).

30 That is, does it meet the definition of a "positive change event" as defined in Chapter 10 (Glossary) of the Rules.

31 NER, cl. 6.6.1(c).

Requirement of the NER	Our consideration
Did Powercor specify details of the positive change event, including the date on which the event occurred, in its written statement?[32]	Yes. Powercor's application is available on our website.[33]
Did Powercor specify in its written statement the eligible pass through amount, the proposed positive pass through amount and the amounts proposed to be recovered from customers in each regulatory year?[34]	Yes. Powercor's application is available on our website.
Did Powercor specify in its written statement evidence of the actual and likely increase in costs that occurred solely as a consequence of the positive change event?[35]	Yes. Powercor's application set out the costs it will incur as a direct result of the Regulatory Obligation, and how it calculated its proposed pass through amount.
Was there a regulatory information instrument applicable to the pass through application?[36]	Powercor provided its revised post tax revenue model.
Is the pass through amount, in whole or in part, in respect of expenditure for a restricted asset?[37]	No.

Table 6 Matters that the AER is to consider under the NER when determining a positive pass through amount

Relevant matters under cl. 6.6.1(j)	AER consideration
In making the pass through determination we must take into account the matters and proposals set out in Powercor's written statement.[38]	This decision sets out how we have taken into account the matters and proposals set out in Powercor's application.
We must take into account the increase in costs in providing direct control services resulting from the pass through event.[39]	In section 4.4 we have set out our assessment of the costs that Powercor is likely to incur as a consequence of the Regulatory Obligation.
We must take into account the efficiency of Powercor's decisions and actions in relation to the risk of the event.[40]	As part of our assessment of the costs that Powercor is likely to incur, we have examined Powercor's estimated capital and operational expenditure. We requested further information from Powercor on 25 March 2022 on the scope of works and associated costs. Based on the evidence before us, we consider that Powercor's proposed pass through amount reasonably reflects efficient costs.
We must take into account the time cost of money.[41]	We have used the nominal rate of return, as determined in Powercor's 2021–26 distribution determination, and a forecast inflation of 2.0 per cent to calculate the approved pass through amount in nominal terms.

32 NER, cll. 6.6.1(c)(1) and 6.6.1(c)(2).

33 See https://www.aer.gov.au/networks-pipelines/powercor-cost-pass-through-increase-to-minimum-wood-pole-interventions.

34 NER, cll. 6.6.1(c)(3), 6.6.1(c)(4), and 6.6.1(c)(5).

35 NER, cl. 6.6.1(c)(6).

36 NER, 6.6.1(c)(7).

37 NER, cl. 6.6.1(c1) and (d2).

38 NER, cl. 6.6.1(j)(1).

39 NER, cl. 6.6.1(j)(2).

40 NER, cl. 6.6.1(j)(3).

41 NER, cl. 6.6.1(j)(4).

Relevant matters under cl. 6.6.1(j)	AER consideration
We must take into account the need to ensure that the pass through amount reflects only actual or likely increment costs solely as a consequence of the pass through event.[42]	We have investigated the costs proposed in Powercor's application and subsequent information request. We are satisfied that the proposed pass through amount includes only incremental costs that Powercor is likely to incur as a consequence of the Regulatory Obligation.
We must take into account whether the costs of the pass through event have already been factored into the calculation of the DNSP's annual revenue requirement for the regulatory period in which the pass through event occurred or will be factored into the calculation of the DNSP's annual revenue requirement for a subsequent regulatory period.[43]	We are satisfied that the proposed pass through amount includes only costs that are incremental to costs that we have factored into the 2021–26 regulatory determination. We are also satisfied that Powercor has not included in its proposed pass through amount any costs that it is likely to incur in any subsequent regulatory period.
We must take into account the extent to which Powercor's costs have already been funded by previous pass through determinations.[44]	There is no evidence to suggest that costs included in Powercor's application have already been funded by previous pass through determinations.
We must take into account any other factors that we consider relevant.[45]	The other factors we took into account in our assessment of Powercor's application include: — the details included in ESV's request under section 109 of the Electricity Safety Act — information from ESV including its reasons for the Regulatory Obligation and how it intends to enforce Powercor's compliance with aspects of its BMP — factors that may impact contractor rates for wood pole replacements.

[42] NER, cl. 6.6.1 (j)(5).

[43] NER, cl. 6.6.1(j)(7).

[44] NER, cl. 6.6.1(j)(7A).

[45] NER, cl. 6.6.1(j)(8).

Glossary

Term	Definition
AER	Australian Energy Regulator
BMP	Bushfire Mitigation Plan
Capex	Capital Expenditure
CSIS	Customer Service Incentive Scheme
DNSP	Distribution Network Service Providers
ESV	Energy Safe Victoira
HBRA	Hazardous Bushfire Risk Area
NEL	National Electricity Law
NEM	National Electricity Market
NER	National Electricity Rules
Opex	Operating Expenditure
PTRM	Post-Tax Revenue Model