

Draft decisions
Transmission: TransGrid
Distribution: EnergyAustralia and
Integral Energy
2009–10 to 2013–14

Mr Steve Edwell
Chairman
9 December 2008

Framework

- The AER's draft transmission determination for TransGrid and the draft distribution determinations for DNSPs are made under the NEL and NER
- Transitional provisions for DNSPs
- Chapter 6A of the NER for transmission

Transitional rules for ACT/NSW

- A number of key features are outlined in the transitional Rules:
 - current classifications of services will continue
 - current forms of regulation will continue
 - current arrangements for capital contributions, ring fencing and cost allocation will continue
 - WACC parameters prescribed in the rules (no AER decision)
 - incentive schemes are discretionary (rather than mandatory)
- AER's focus has been to set efficient expenditure allowances (capital and operating)
- Future reviews will include elements which are 'locked-in' under the transitional rules

AER review process – transmission

- Comprehensive review process
- Pre-lodgement consultation (submission guidelines requirements, demand forecasting methodology)
- Submissions on TransGrid's revenue proposal
- Engineering consultant review – PB
- Secondary engineering consultant – Nuttall Consulting
- AER draft decision

AER review process – distribution

- Comprehensive review process
- Pre-lodgement consultation (RIN, incentive schemes)
- Submissions on regulatory proposals
- Engineering consultant review – Wilson Cook
- Secondary engineering consultant – EMS
- AER draft decisions

Cost of capital

- Majority of WACC parameters set in the NER
- AER's draft decision on WACC
 - TransGrid 9.82 %
 - DNSPs 9.72 %
- AER is currently reviewing WACC parameters
- WACC review is not relevant for the transmission or distribution determinations

Service target performance incentive scheme (STPIS)

- The AER decided not to apply a STPIS in ACT or NSW for 2009–14
- The AER will collect and monitor performance data during the next regulatory control period
- From 1 July 2014 the AER's national distribution STPIS will be applied to the DNSPs with financial incentives

Demand management incentive schemes (DMIS)

- In February 2008, AER published its final decision on DMIS:
 - The D-factor scheme (as applied by IPART) – for NSW DNSPs
 - The demand management innovation allowance (DMIA) – for ACT and NSW DNSPs
- Since February, further consultation and thinking on optimal design of a DMIA
- AER's draft decision is to replace the original DMIA with a 'replacement DMIA'
- No changes to D-factor

Efficiency benefit sharing scheme (EBSS)

- The EBSS released in February for ACT & NSW will apply to the DNSPs
- The EBSS will also apply to TransGrid
- Certain cost categories will be excluded from the EBSS

Negotiating frameworks

- Both DNSPs provided negotiating frameworks
- The AER approved the negotiating frameworks for both EnergyAustralia and Integral Energy
- TransGrid provided a negotiating framework which the AER also approved

Indicative prices – DNSPs

- **Estimated** average customer bill increase in 2009–10:
 - \$2.00 per week for EnergyAustralia customers
 - \$1.70 per week for Integral Energy customers
- AER has determined revenues only at this stage – not price impacts
- Pricing proposals considered in May 2009

Indicative prices – transmission

- AER's draft decision for TransGrid will add approximately \$4.00 to a residential customer's annual bill of \$983
- AER does not set prices for TNSPs but assess price methodology

Process – next steps –transmission

- **16 January 2009** TransGrid to lodge revised proposal
- **16 February 2009** Submissions on draft determination close
- **30 April 2009** AER release final decision on TransGrid's transmission determination
- **1 July 2009** Commencement of the next regulatory control period

Process – next steps – distribution

- **16 January 2009** EnergyAustralia and Integral Energy to lodge revised proposals
- **16 February 2009** Submissions on draft determination close
- **30 April 2009** AER must release final decision on distribution determinations
- **21 May 2009** DNSPs submit pricing proposal
- **1 June 2009** AER approves pricing proposal
- **1 July 2009** Commencement of the next regulatory control period

Questions



AUSTRALIAN
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Draft decision: TransGrid transmission determination 2009–10 to 2013–14

Mr Steve Edwell
Chairman
9 December 2008



AUSTRALIAN ENERGY
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Key drivers of network expenditure

- TransGrid's capex and opex is being driven by:
 - the age profile of its infrastructure
 - planning obligations of NSW DNSPs
 - the rising real price of electricity transmission equipment
 - rising real wages growth and increasing compliance requirements associated with community and environmental obligations

MAR

AER's draft decision on the maximum allowed revenue (\$m, nominal)

	2009–10	2010–11	2011–12	2012–13	2013–14	Total
AER decision on MAR (smoothed)	678.4	726.3	777.5	832.4	891.1	3905.7
TransGrid proposal (smoothed)	670.2	725.6	785.5	850.3	920.5	3952.1
Difference	8.2	0.7	-8.0	-17.9	-29.4	-46.4

Opening RAB

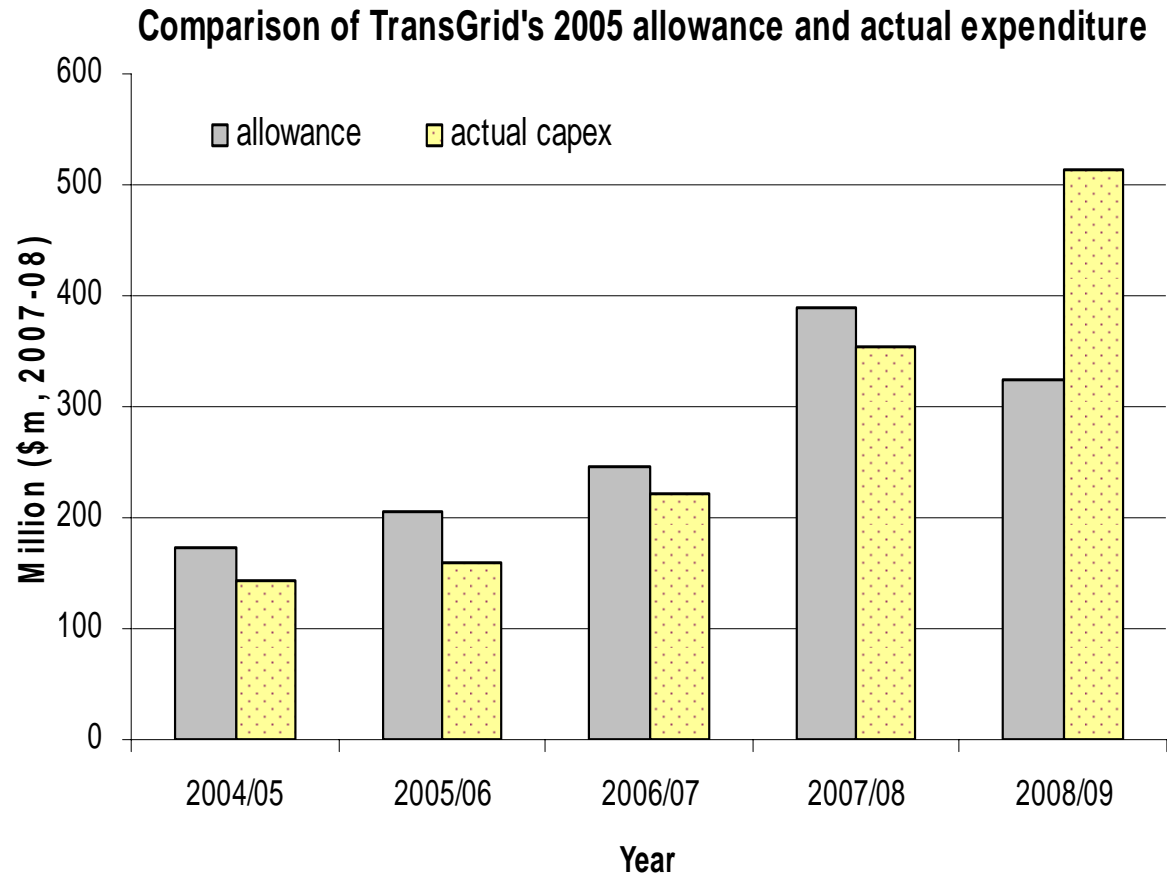
- Proposed an opening RAB of **\$4237m**
- The AER made adjustments due to:
 - identified errors and updated information
 - removal of \$8.1m to account for replacement assets
- The AER determined TransGrid's opening RAB to be **\$4234m**

Demand forecasting

- TransGrid's initial proposal was based on 2007 APR demand forecasts
- MMA found TransGrid's demand forecast methodology was appropriate, well considered and reasonable
- MMA considered the forecasts should be updated to reflect the latest forecasts in the 2008 APR. TransGrid did this and the AER accepted an updated proposal
- The AER's considers the methodologies used by TransGrid provide a realistic expectation of demand for the next regulatory control period

Past capex

- Actual capex around 5% higher than its allowance
- The over spend is in the last year of the current period
- The AER was satisfied that the change was justified



Capex

- Proposed a capex of **\$2550m** (\$2007–08)
- The AER adjustments included those from:
 - detailed project reviews
 - escalations
 - scoping factors
 - agreed adjustments
- The AER approved capex of **\$2376m**

Contingent projects

- Proposed **nineteen** contingent projects with an indicative cost of **\$2.3b**
- The AER approved **nine** contingent projects with a cost of **\$1.2b**
- Projects removed largely reflected concerns with the proposed trigger event

Opex

- Proposed opex of **\$855m** (\$2007–08)
- The AER adjustments included those to:
 - asset growth
 - debt raising costs
 - self insurance
 - agreed adjustments
- The AER approved total opex of **\$765m**

Service target performance incentive scheme

- Two components:
 - Service component
 - Parameters set out in the scheme
 - +/- 1% of MAR
 - AER reviewed TransGrid's proposed performance targets, caps, collars and weightings and made several adjustments
 - Market impact component
 - New component of the scheme
 - 2% MAR
 - AER reviewed TransGrid's proposed performance target and made a minor adjustment

Pricing methodology

- Pricing methodology applies to prescribed transmission services
 - The pricing methodology is a set of principles for TNSPs to follow in determining the structure of prescribed transmission prices
- TransGrid's proposal was submitted in accordance with the chapter 6A and the guidelines
- AER draft decision:
 - proposed pricing methodology was rejected in the draft decision
 - a number of issues need to be addressed by TransGrid

Questions



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Draft decision: EnergyAustralia distribution determination 2009–10 to 2013–14

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AUSTRALIAN ENERGY
REGULATOR

Key drivers of network expenditure

- EnergyAustralia's capex and opex is being driven by:
 - the age profile of its infrastructure
 - increased network security and reliability
 - planning obligations of NSW DNSPs
 - the rising real price of electricity distribution equipment
 - rising real wages growth and increasing compliance requirements associated with community and environmental obligations
 - increased workload largely arising from the larger asset base
 - step changes arising partly from the higher costs of IT from the introduction of new systems and partly from a need to meet statutory and regulatory obligations

Opening RAB (distribution)

- EnergyAustralia proposed an opening RAB of **\$7229m** for its distribution network
- An adjustment was made because EnergyAustralia did not apply IPART's indexation method
- The AER determined EnergyAustralia's opening RAB to be **\$7203m**

Opening RAB (transmission)

- EnergyAustralia proposed an opening RAB of **\$989m** for its transmission network
- As for distribution, an adjustment was made because EnergyAustralia did not apply appropriate indexation method
- The AER determined EnergyAustralia's opening RAB to be **\$985m**

Demand forecasting

- AER engaged MMA to review EnergyAustralia's maximum demand, energy and customer number forecast methodologies and forecasts
- MMA found EA's maximum demand forecast methodology was reasonable, however concluded that the energy and customer number forecasts need to be updated to account for latest energy sales data
- AER's draft decision to accept EA's maximum demand and customer number forecasts
- AER requested revised energy forecast be provided in February 2009

Capex

- Proposed a capex of **\$8659m** (\$2008–09)
- The AER adjustments to the proposed allowance:
 - Cost escalators
 - Errors
 - Substation cost estimates
 - ‘Black spot’ reliability program
 - Replacement of feeders 908 & 909
- The AER approved capex of **\$8435m**

Opex

- Proposed opex of **\$3047m** (\$2008–09)
- The AER made the following adjustments:
 - network operating
 - network maintenance
 - other expenditure
 - labour escalators
 - self insurance
 - debt raising
 - Equity raising
- AER approved total opex of **\$2638m**

Pass throughs

- EnergyAustralia proposed **seven** pass through events
- AER accepts ‘retail project event’ and ‘force majeure’ as nominated pass through events
- Remaining proposed events are likely to be ‘regulatory change events’ and therefore unnecessary

Building block revenues (distribution)

AER's conclusion on EnergyAustralia's revenue requirements and X factors (\$m, nominal)

	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14
Regulatory depreciation		70.8	94.1	114.6	136.3	131.0
Return on capital		699.9	828.6	966.4	1121.5	1263.5
Tax allowance		36.1	64.3	73.8	84.8	89.6
Operating expenditure		478.1	504.5	534.7	567.0	594.0
Annual revenue requirements		1284.8	1491.5	1689.4	1909.5	2078.2
Expected revenues	1023.7	1284.8	1469.5	1670.4	1886.6	2138.0
Forecast CPI (%)		2.55	2.55	2.55	2.55	2.55
X Factors (%)		-24.30	-10.43	-10.43	-10.43	-10.43

Building block revenues (transmission)

AER's conclusion on EnergyAustralia's revenue requirements and X factors (\$m, nominal)

	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14
Regulatory depreciation		4.8	8.1	11.6	14.9	14.0
Return on capital		95.7	122.6	140.6	167.8	203.6
Tax allowance		3.0	6.9	8.0	9.6	10.6
Operating expenditure		32.8	33.3	34.3	35.6	36.3
Annual revenue requirements		136.3	170.9	194.6	227.9	264.5
Expected revenues	129.5	137.1	162.9	193.5	229.9	273.1
Forecast CPI (%)		2.55	2.55	2.55	2.55	2.55
X Factors (%)		-3.26	-15.85	-15.85	-15.85	-15.85

Alternative Control – Public Lighting

- AER statement on control mechanisms for alternative control services proposed:
 - Fixed schedule of prices for the first year
 - Price path for the remaining years
- From its review of proposals and submissions the AER considers a modified approach is appropriate
- The AER decided the control mechanism for public lighting would be two schedules of fixed prices for the first year:
 - assets constructed before 1 July 2009
 - assets constructed after 30 June 2009

Public lighting (cont)

- The AER proposes a building block approach for existing assets and an annuity approach for the capital charge for new assets
- For each remaining year the charges will be permitted to increase in accordance with a price path approved by the AER, such as CPI
- Each NSW DNSP will submit its proposed schedules of fixed prices and price path to the AER by 16 January 2009 for consideration by the AER and for public consultation

Pricing methodology

- This is the first time which EnergyAustralia has been required to lodge a pricing methodology
- The AER has accepted EnergyAustralia's proposed pricing methodology

Questions

Draft distribution determination: Integral Energy 2009–10 to 2013–14

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Chairman
9 December 2008

Key drivers of network expenditure

- Integral Energy's capex and opex is being driven by:
 - the age profile of its infrastructure
 - increased network security and reliability
 - planning obligations of NSW DNSPs
 - the rising real price of electricity distribution equipment
 - rising real wages growth and increasing compliance requirements associated with community and environmental obligations
 - a step change in vegetation management contract costs
 - an increase in the size of the asset base
 - a backlog of defects.

Opening RAB

- Integral Energy proposed an opening RAB of **\$3835m**
- The AER did not accept Integral Energy's proposed increase to the opening RAB to correct erroneous asset lives used in the historical valuation of sub-transmission and zone substations.
- The AER determined Integral Energy's opening RAB to be **\$3678m**

Demand forecasting

- AER engaged MMA to review Integral Energy's maximum demand, energy and customer number forecast methodologies and forecasts
- Some concerns raised with Integral Energy's forecast methodologies
- Integral Energy provided a revised maximum demand forecast during the review
- Integral Energy also provided revised energy and customer number forecasts, however AER considers the energy forecast should be updated again to account for latest energy sales data
- AER requested a second revised energy forecast be provided in February 2009

Capex

- Proposed capex of **\$2953m** (\$2008–09)
- The AER adjustments to proposed allowance:
 - Replacement related capex
 - Adjustment to cost escalators
- The AER approved capex of **\$2914m**

Opex

- Proposed opex of **\$1477m** (\$2008–09)
- Adjustments made to:
 - Labour escalators
 - Self insurance costs
 - Debt & equity raising costs
- AER approved total opex of **\$1460m**

Pass throughs

- Integral Energy proposed **twelve** pass through events
- AER accepts proposed ‘retail project event’ and ‘force majeure’ as nominated pass through events
- Remaining proposed events are likely to be ‘regulatory change events’ and therefore unnecessary

Building block revenues

AER's forecast roll-forward of Integral Energy's regulated asset base (\$m, nominal)

	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14
Regulatory depreciation		137.6	117.0	110.5	102.2	100.4
Return on capital		357.4	402.1	457.2	511.2	564.2
Tax allowance		37.8	39.1	39.3	38.4	41.2
Operating expenditure		292.2	302.6	314.8	327.7	339.5
Annual revenue requirements		825.0	860.8	921.8	979.5	1045.4
Expected revenues	661.5	792.8	856.0	925.0	996.8	1075.4
Forecast CPI (%)		2.55	2.55	2.55	2.55	2.55
X Factors (%)		–15.42	–3.50	–3.50	–3.50	–3.50

Alternative Control – Public Lighting

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- Each NSW DNSP will submit its proposed schedules of fixed prices and price path to the AER by 16 January 2009 for consideration by the AER and for public consultation

Questions

Next steps

- **16 January 2009** Integral Energy may submit revised proposal or submission
- **16 February 2009** Submissions on draft decision and revised proposal close
- **30 April 2009** AER releases final decision on distribution determination
- **1 July 2009** Commencement of the next regulatory control period