FINAL DECISION
Murraylink transmission determination
2018 to 2023

Attachment 5 – Regulatory depreciation

April 2018

AUSTRALIAN
ENERGY
REGULATOR

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Note

This attachment forms part of the AER's final decision on Murraylink's transmission determination for 2018–23. It should be read with all other parts of the final decision.

The final decision includes the following documents:

Overview

Murraylink transmission determination 2018–23

Attachment 1 – Maximum allowed revenue

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 5 – Regulatory depreciation

Attachment 6 – Capital expenditure

Attachment 8 – Corporate income tax

Attachment A – Negotiating framework

Attachment B – Pricing methodology

Contents

Shortened forms

Shortened form	Extended form
AARR	aggregate annual revenue requirement
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
ASRR	annual service revenue requirement
augex	augmentation expenditure
capex	capital expenditure
CCP	Consumer Challenge Panel
CESS	capital expenditure sharing scheme
CPI	consumer price index
DMIA	demand management innovation allowance
DRP	debt risk premium
EBSS	efficiency benefit sharing scheme
ERP	equity risk premium
MAR	maximum allowed revenue
MRP	market risk premium
NEL	national electricity law
NEM	national electricity market
NEO	national electricity objective
NER	national electricity rules
NSP	network service provider
NTSC	negotiated transmission service criteria
opex	operating expenditure
PPI	partial performance indicators
PTRM	post-tax revenue model
RAB	regulatory asset base
RBA	Reserve Bank of Australia
repex	replacement expenditure
RFM	roll forward model
RIN	regulatory information notice

Shortened form	Extended form
RPP	revenue and pricing principles
SLCAPM	Sharpe-Lintner capital asset pricing model
STPIS	service target performance incentive scheme
TNSP	transmission network service provider
TUoS	transmission use of system
WACC	weighted average cost of capital

5 Regulatory depreciation

Depreciation is the allowance provided so capital investors recover their investment over the economic life of the asset (return of capital). In deciding whether to approve the depreciation schedules submitted by Murraylink, we make determinations on the indexation of the RAB and depreciation building blocks for Murraylink's 2018–23 regulatory control period.[1] The regulatory depreciation allowance is the net total of the straight-line depreciation less the inflation indexation adjustment of the RAB.

5.1 Final decision

Our final decision is to determine a regulatory depreciation allowance of $20.2 million ($nominal) for Murraylink over the 2018–23 regulatory control period. This amount represents a reduction of $0.2 million (or 0.8 per cent) on the $20.4 million ($nominal) in Murraylink's revised proposal.[2] It represents a decrease of $2.9 million (or 12.6 per cent) from the $23.2 million ($nominal) in our draft decision. In coming to this decision:

- We accept Murraylink's revised proposed straight-line method to calculate the regulatory depreciation allowance.
- We largely accept Murraylink's revised proposed asset classes and standard asset lives. However, we do not accept the name change for the asset class 'Ancillary 7 - pressure vessel testing and inspection' to 'Inspection and test equipment'.
- We accept Murraylink's revised proposal to apply the weighted average method to calculate the remaining asset lives as at 1 July 2018. In accepting the weighted average method, we have updated Murraylink's remaining asset lives as at 1 July 2018 to reflect the actual capex input corrections and 2017–18 CPI input update we made in the RFM (attachment 2).
- We made determinations on other components of Murraylink's revised proposal, which affect the RAB and in turn impacts the forecast regulatory depreciation allowance. The decrease to the regulatory depreciation allowance from the revised proposal reflects our adjustments to the opening RAB as at 1 July 2018 (attachment 2) and expected inflation rate (section 2.3 of the Overview).

Table 5.1 sets out our final decision on the forecast regulatory depreciation allowance for Murraylink over the 2018–23 regulatory control period.

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1 NER, cll. 6A 5.4(a)(1) and (3).

2 Murraylink, *Revised Revenue proposal 2018–23, attachment 8.1 - Murraylink - PTRM - 20171201 - Public,* December 2017.

Table 5.1 AER's final decision on Murraylink's forecast regulatory depreciation for the 2018–23 regulatory control period ($million, nominal)

	2018–19	2019–20	2020–21	2021–22	2022–23	Total
Straight-line depreciation	6.2	6.4	6.6	6.9	9.0	35.1
Less: inflation indexation on opening RAB	2.8	2.8	3.0	3.2	3.2	14.9
Regulatory depreciation	**3.4**	**3.6**	**3.6**	**3.7**	**5.8**	**20.2**

Source: AER analysis.

Standard and remaining asset lives as at 1 July 2018

For this final decision, we accept the majority of Murraylink's revised proposed standard asset lives for its asset classes in respect of forecast capex to be commissioned in the 2018–23 regulatory control period. However, we do not accept Murraylink's revised proposal to change the name of the asset class 'Ancillary 7 - pressure vessel testing and inspection' to 'Inspection and test equipment'.

In the draft decision, we accepted Murraylink's proposed standard asset lives for its existing asset classes. This is because they are consistent with those approved at the 2013–18 transmission determination and comparable to the standard asset lives used for other TNSPs in respect of similar asset classes. However, we did not retain the proposed standard asset life of 10 years for the 'Test equipment' asset class in the PTRM. This is because we did not approve the proposed forecast capex allocated to this asset class and therefore no standard asset life was required.

Murraylink's revised proposal adopted all aspects of our draft decision in terms of the standard asset lives. It has also removed the 'Test equipment' asset class from its revised PTRM.[3] However, Murraylink has changed the name of the asset class 'Ancillary 7 - pressure vessel testing and inspection' to 'Inspection and test equipment'.[4]

We do not accept this proposed name change. We consider by adding the label 'Test equipment' to the 'Ancillary 7 - pressure vessel testing and inspection' asset class, Murraylink has in effect applied a standard asset life of 7 years for test equipment assets. However, we note that there is no forecast capex for test equipment for the 2018–23 regulatory control period. Our draft decision did not approve any forecast capex for test equipment, and Murraylink's revised proposal has adopted this aspect of the draft decision. Therefore, we are not required to approve a standard asset life of 7 years for test equipment for the 2018–23 regulatory control period. For this reason, we do not accept Murraylink's proposed name change to the asset class 'Ancillary 7 -

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[3] Murraylink, *Revised Revenue proposal 2018–23, attachment 8.1 - Murraylink - PTRM - 20171201 - Public*, December 2017.

[4] Murraylink, *Revised Revenue proposal 2018–23,* December 2017, p. 49.

pressure vessel testing and inspection' in the PTRM. Further, we note that Murraylink has made the same name change in its revised proposed RFM for RAB roll forward purposes. As discussed in attachment 2, we also do not accept this change for the RFM.

In addition, we note that the standard asset lives for the 'Other operating assets' and 'Office machines' asset classes are incorrectly recorded in Murraylink's revised proposal PTRM. We have corrected these inputs to be consistent with the values as shown in our draft decision PTRM and the revised proposal.[5]

Our final decision is to accept Murraylink's revised proposal to use the weighted average method in the RFM to calculate the remaining asset lives as at 1 July 2018 for its existing asset classes. This is consistent with Murraylink's initial proposal and our draft decision. In accepting this method, we have updated the remaining asset lives to reflect the actual inflation value for 2017–18 that we made in the RFM, which became available after Murraylink submitted its revised proposal. We have also corrected some input errors relating to the actual capex for 2012–13 and 2013–14 in the revised proposed RFM (attachment 2). These inputs affect the remaining asset lives calculation.

Table 5.2 sets out our final decision on the standard and remaining asset lives as at 1 July 2018 for Murraylink over the 2018–23 regulatory control period. We are satisfied the approved standard asset lives would lead to a depreciation schedule that reflects the nature of the assets over the economic lives of the asset classes. Further, the sum of the real value of the depreciation attributable to the assets would be equivalent to the value at which the assets were first included in the RAB for Murraylink.[6]

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5 Murraylink, *Revised Revenue proposal 2018–23,* December 2017, p. 14. Murraylink has made similar errors with the tax standard asset lives in the revised proposed RFM. We have also corrected these errors in the final decision RFM (attachment 8).

6 NER, cll. 6A.6.3(b)(1)–(2).

Table 5.2 AER's final decision on Murraylink's standard and remaining asset lives as at 1 July 2018 (years)

	Standard asset life	Remaining asset life as at 1 July 2018
Switchyard	40.0	26.0
Transmission line	40.0	25.3
Easements	n/a	n/a
Ancillary 15 - control systems	15.0	12.3
Ancillary 30	30.0	29.1
Ancillary 7 - pressure vessel testing and inspection	7.0	4.2
Other operating assets	5.0	5.0
Office machines	3.0	1.8

Source: AER analysis.

n/a: not applicable. We have not assigned a standard asset life to some asset classes because the assets allocated to those asset classes are not subject to depreciation.

5.2 Assessment approach

We did not change our assessment approach for the regulatory depreciation from our draft decision. Attachment 5 section 5.3 of our draft decision details that approach.