

May 2022

Statement of reasons: Essential Energy’s Annual Pricing Proposal

The AER approves Essential Energy’s 2022–23 pricing proposal and the tariffs contained within for commencement on 1 July 2022. Essential Energy’s approved tariffs are set out on [our website](#).

Estimated network cost movements

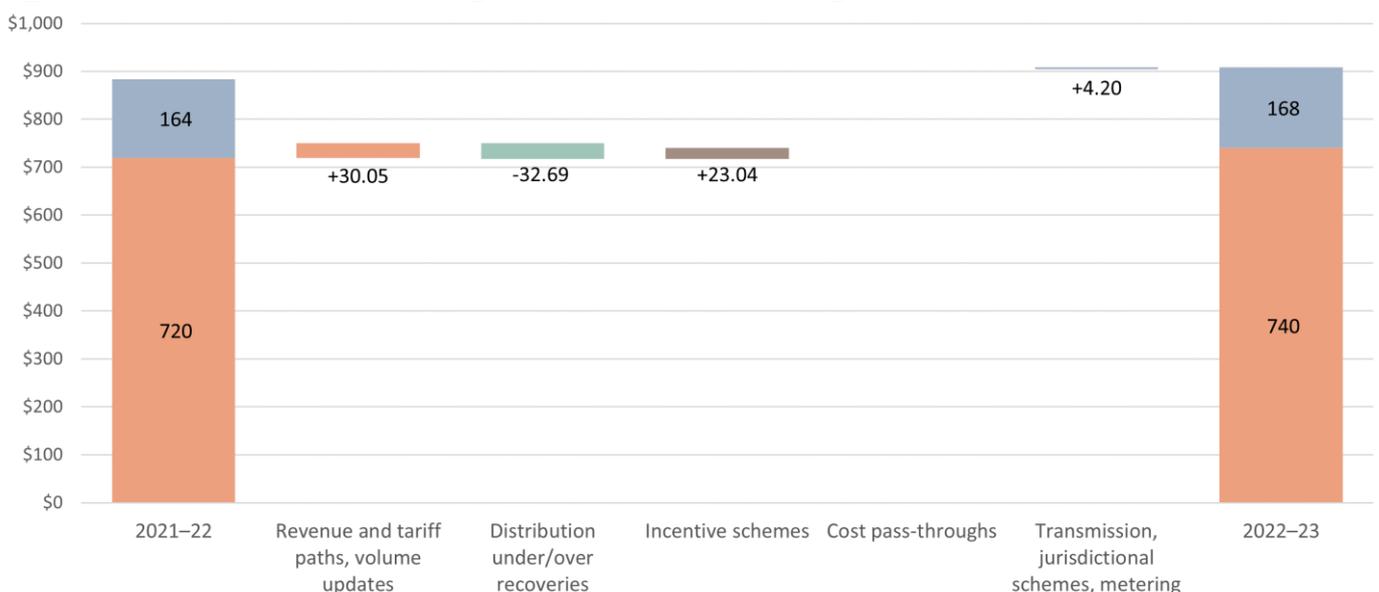
We estimate that, based on our decision, the network component of the typical bill for Essential Energy’s customers to be \$24.61 higher for households and \$43.74 higher for small businesses in 2022–23 compared to 2021–22.

The network cost movements reflect an increase in revenue that Essential Energy is allowed to recover in 2022–23.

The increase in revenue is due to previously approved cost pass-throughs for bushfire natural disasters in recent years, an increase in transmission costs passed through to customers, higher than forecast inflation, higher reward payments under incentive schemes, and adjustments for errors in incentive scheme payments in previous years. This is partly offset by the return of previous over-recovered revenues.

We note electricity retailers ultimately determine how these underlying network tariffs are reflected in the retail prices offered to customers. The network charge component of an energy bill accounts for approximately 43% of the total residential retail bill.

Figure 1 Residential: Average annual network charge



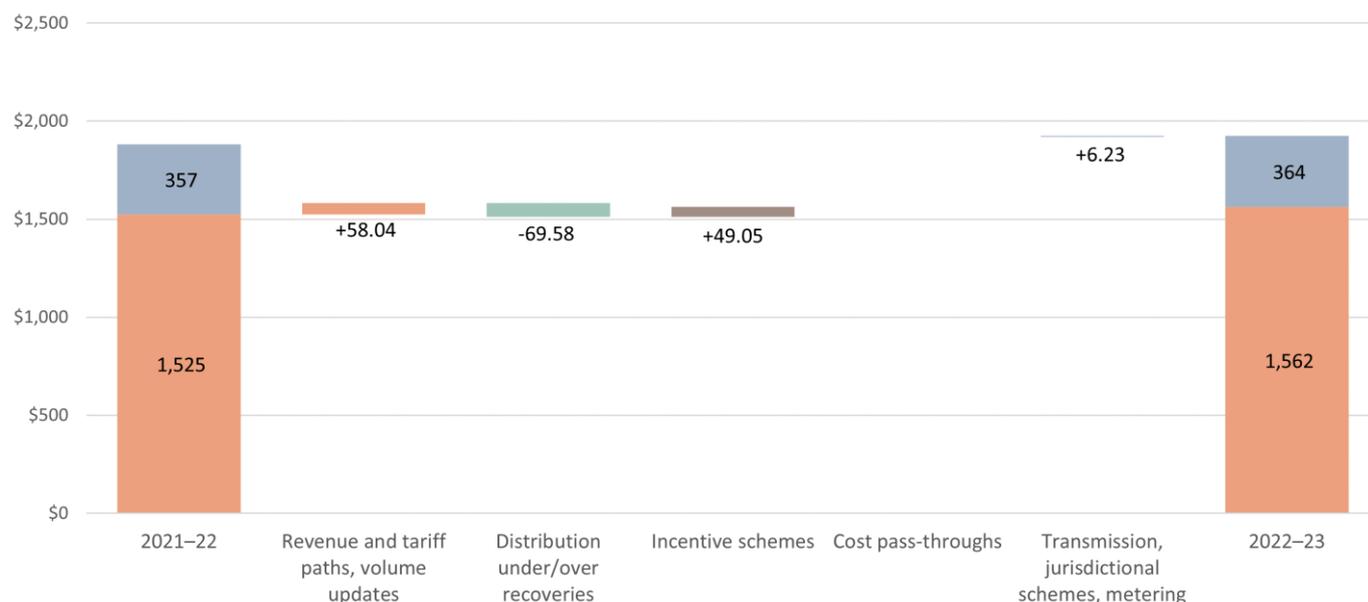
Source: AER Analysis; Essential Energy’s 2022–23 pricing proposal.

Note: Our analysis assumes electricity usage of 4,766kWh for the ‘LV Residential Anytime’ tariff. This is based on actual data for residential electricity usage and customer numbers reported in Essential Energy’s 2022–23 pricing proposal.

‘Revenue and tariff paths, volume updates’ includes all other movements in the distribution network charges not shown above, including cost pass-throughs applied by adjusting the revenue path set in the 2019–24 determination.

‘Transmission, jurisdictional schemes, metering’ includes all movements in the non-distribution network charges.

Figure 2 Small business: Average annual network charge



Source: AER Analysis; Essential Energy's 2022-23 pricing proposal.

Note: Our analysis assumes electricity usage of 9,980kWh for the 'LV Small Business Anytime' tariff. This is based on actual data for small business electricity usage and customer numbers reported in Essential Energy's 2022-23 pricing proposal.

'Revenue and tariff paths, volume updates' includes all other movements in the distribution network charges not shown above, including cost pass-throughs applied by adjusting the revenue path set in the 2019-24 determination.

'Transmission, jurisdictional schemes, metering' includes all movements in the non-distribution network charges.

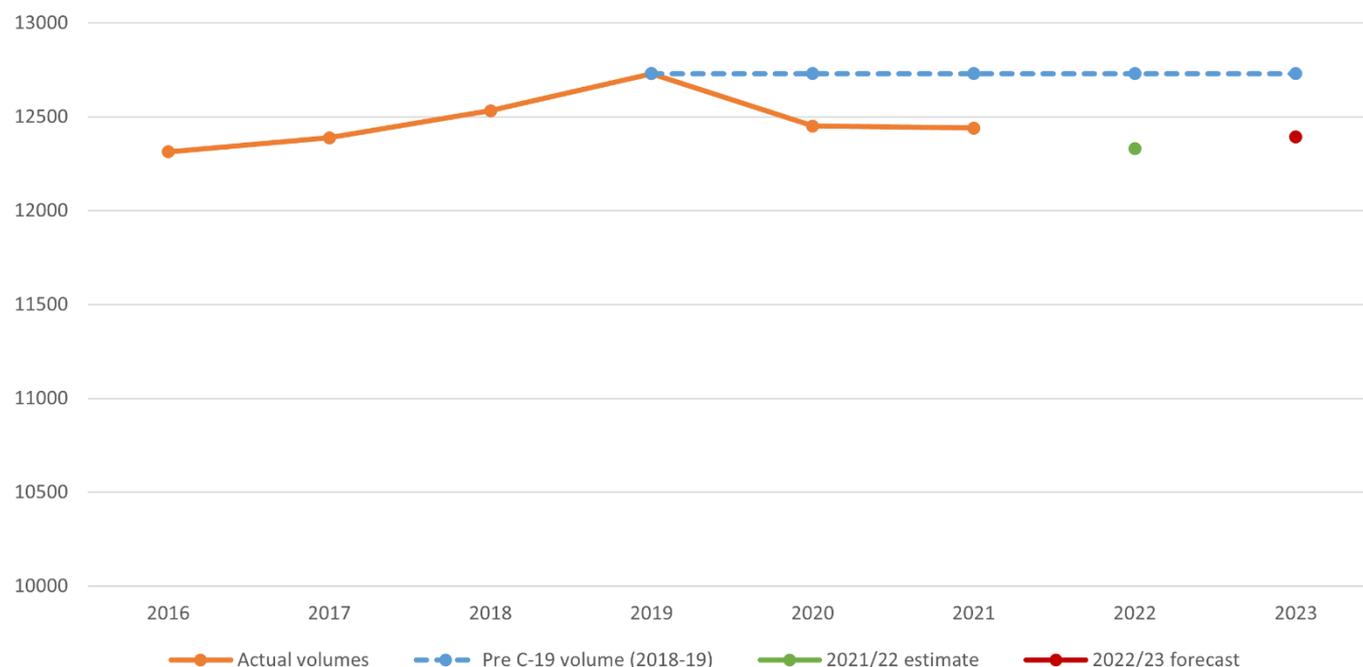
Actual bill impacts for individual customers will vary from our estimates as customers may be on different tariffs or consume different amounts of energy from our assumptions. Our analysis is based on flat rate tariffs, which are the most common tariffs for residential and small business customers. Where overall price movements are small, some tariffs may increase while others decrease.

Consumption forecasts

Electricity distributors operate under a revenue cap which sets the annual allowed revenue they can recover to deliver safe and reliable electricity within their networks. Prices are determined based on forecast consumption for that year, allowing distributors to recover their allowed revenue. If distributors forecast lower consumption, then other things being equal, prices are expected to be higher to allow them to recover the revenue allowed.

Our assessment of the distributors' consumption forecasts includes analysis of historical consumption trends and the reasons put forward for any departure from them. For 2022-23, a key factor of our assessment is the impact that Australia's response to COVID-19 has had and is continuing to have on energy consumption.

Figure 3 Energy volumes (GWh)



Source: AER Analysis; RIN data; Essential Energy’s 2022–23 pricing proposal.

Essential Energy has forecast increased energy consumption for 2022–23. The forecast is based on trends in customer growth and changes in energy consumption between different customer segments.

We consider Essential Energy’s consumption forecasts are reasonable based on our analysis and the supporting information provided by Essential Energy.

Under/over recovered revenues

Although we set the revenues the distributors can recover, the revenue they ultimately receive over an individual year is determined by the amount of actual energy consumed in that year.

- Actual energy consumption can fluctuate from forecast consumption because of a number of factors such as weather, increased uptake of solar PV, or, in recent times, in response to a pandemic. These fluctuations in energy consumption result in distributors recovering more or less than the allowable revenue we set.
- Variations also occur for the transmission costs and jurisdictional scheme amounts a distributor passes through to customers where actual payments differ to what was forecast.

To ‘true-up’ these variations in revenue, adjustments are made to allowable revenues for the upcoming financial year to ensure that over time, a distributor only recovers the revenue it is allowed.