Final Decision

SA Power Networks Distribution Determination 2019 to 2025

(1 July 2019 to 30 June 2025)

Revocation and substitution determination

25 March 2024

AUSTRALIAN ENERGY REGULATOR

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Revocation and substitution determination of SA Power Networks' 2020–25 distribution determination

1 Overview

As part of its regulatory proposal for the 2020–25 regulatory control period, SA Power Networks proposed a step change in its forecast operating expenditure (opex) to reclassify cable and conductor minor repair expenditure as opex rather capital expenditure (capex).

SA Power Networks submitted in its 2020–25 regulatory proposal that this expenditure had historically been categorised as capex in its regulatory accounts. SA Power Networks considered that reclassifying the expenditure as opex better reflected the nature of the expenditure. SA Power Networks submitted that it had removed the expenditure from its capex forecast and included a capex/opex trade-off step change in its opex forecast for the 2020–25 regulatory control period. SA Power Networks stated that this proposed change reduced its forecast capex and increased its forecast opex.

The AER's final determination for 2020–25 reflected this proposed treatment of cable and conductor minor repairs as opex. This resulted in the proposed step change being included in the approved forecast opex and the associated capex was removed from the approved forecast capex.

As part of the early signal pathway process for its 2025–30 regulatory proposal, SA Power Networks informed us that the opex step change for cable and conductor minor repairs was in error. In preparing its regulatory proposal SA Power Networks discovered that cable and conductor minor repairs expenditure had always been treated as opex in its regulatory reporting.

Under rule 6.13(a) of the National Electricity Rules (NER), the AER may revoke a distribution determination during a regulatory control period if it appears that it is affected by a material error or deficiency of one or more of the following kinds:

1. a clerical mistake or an accidental slip or omission
2. a miscalculation or misdescription
3. a defect in form
4. a deficiency resulting from the provision of false or materially misleading information to the AER.

We consider that an error has occurred and that the error is material and within the scope of rule 6.13(a)(4) of the NER. This reflects the magnitude of the impact of the error on forecast opex and capex, and the consequential impacts on revenue and the Demand Management Innovation Allowance Mechanism and the Service Target Performance Incentive Scheme incentive rates. The correction of these errors is set out in the following sections.

The AER, therefore, considers it appropriate to revoke the final distribution determination for the 2020–25 regulatory control period under rule 6.13 of the NER and substitute it with a new determination that will apply for the remainder of the regulatory control period. In sections 2 to 5, we set out the basis for this decision, including what is being revoked, what is being substituted and the reasons why. Further, in making this decision the AER consulted with both SA Power Networks and consumer representatives. The outcomes of this consultation are set out in section 6.

2 Forecast capex and opex

The incorrect information provided, being that cable and conductor minor repairs expenditure had been historically reported as capex, not opex, led us to approve SA Power Networks' forecast opex in its 2020–25 revised regulatory proposal. This included a step change of $49.7 million ($2019–20) for additional cable and conductor minor repair expenditure.[1]

SA Power Networks' forecast opex was derived using a revealed cost, base step trend forecasting approaching. Base opex was derived from SA Power Networks actual opex in a base year. We now know that this included cable and conductor minor repairs expenditure and a step change for this expenditure was thus not required.

Consequently, to correct the error, we have removed $49.7 million ($2019–20) from the approved forecast opex for the 2020–25 regulatory control period, being the amount of the cable and conductor minor repairs step change. We revoke our decision to approve forecast opex of $1,458.3 million ($2019–20)[2] and substitute it with forecast opex of $1,419.8 million ($2019–20), as shown in Table 1.

Table 1 AER's revocation and substitution determination on forecast opex ($ million, 2019–20)

	2020–21	2021–22	2022–23	2023–24	2024–25	Total
Forecast opex	277.9	281.1	284.4	287.0	289.4	1,419.8

Source: AER, *Final decision, SA Power Networks Distribution Determination, 2020 to 2025, Attachment 6*, June 2020, p. 7; AER analysis.

Note: Includes debt raising costs.

Similarly, we have added $69.7 million ($2019–20) to the approved forecast capex for the 2020–25 regulatory control period. This is the amount SA Power Networks removed from its capex forecast as a part of its 2020–25 regulatory proposal.[3] We now know that the SA Power Networks' initial capex forecast did not include any expenditure for cable and conductor minor repairs and none should have been removed. The difference between the amount removed from forecast capex and the amount we added as an opex step change is because we considered the efficient forecast of cable and conductor minor repairs was $49.7 million ($2019–20).[4]

We revoke our decision to approve forecast net capex of $1,595.8 million ($2019–20)[5] and substitute it with forecast net capex of $1,696.0 million ($2019–20), as shown in Table 2. The substituted amounts in Table 2 also includes the additional net capex approved for the April 2022 emergency standards cost pass through event, which we have approved since our June 2020 final decision.[6]

1 AER, *Final decision, SA Power Networks Distribution Determination, 2020 to 2025, Attachment 6*, June 2020, pp. 4, 22.

2 AER, *Final decision, SA Power Networks Distribution Determination, 2020 to 2025, Attachment 6*, June 2020, p. 4.

3 SA Power Networks, *2020–25 Regulatory Proposal, Attachment 5, Capital expenditure*, 31 January 2019, pp. 28, 40.

4 AER, *Draft decision, SA Power Networks Distribution Determination, 2020 to 2025, Attachment 6*, June 2020, pp. 37–41.

5 AER, *Draft decision, SA Power Networks Distribution Determination, 2020 to 2025, Attachment 5*, June 2020, pp. 5–6.

6 AER, *Determination, April 2022 emergency standards cost pass through, SA Power Networks*, September 2022.

Table 2 AER's revocation and substitution determination on total forecast net capex ($ million, 2019–20)

	2020–21	2021–22	2022–23	2023–24	2024–25	Total
Forecast capex	353.4	350.4	339.0	336.0	317.3	1,696.0

Source: AER analysis.
Note: Total forecast net capex also includes the additional net capex approved in our Emergency standard cost pass through decision.

3 Allowed revenue

We have corrected SA Power Networks' allowed revenues to reflect the corrections set out in section 2 that we have made to forecast opex and capex. The correction to opex flows through directly to revenue, while the correction to forecast net capex impacts the return on capital, regulatory depreciation and the net tax allowances we approved for SA Power Networks in the 2020–25 regulatory control period. We have revoked and substituted the post tax revenue model to correct these.

The substituted determination on allowed revenues is outlined in Table 3. This substitutes Table 2 in our final determination overview for SA Power Network' 2020–25 regulatory control period, which we revoke.[7]

Table 3 AER's revocation and substitution determination on SA Power Networks' annual revenue requirement, annual expected revenues, and X factors ($ million, nominal)

	2020–21	2021–22	2022–23	2023–24	2024–25	Total
Return on capital	207.0	205.5	207.9	215.9	198.7	1,035.0
Regulatory depreciation	224.5	238.7	252.2	260.6	257.2	1,233.2
Opex	284.3	294.0	304.3	314.0	323.8	1,520.4
Revenue adjustments	27.7	(3.2)	24.4	18.4	16.5	83.8
Net tax allowance	1.2	1.4	2.5	3.3	3.2	11.5
Annual revenue requirement (unsmoothed)	744.6	736.4	791.3	812.2	799.4	3,883.8
Annual expected revenue (smoothed)	**775.9**	**779.2**	**783.7**	**797.1**	**737.5**	**3,873.3**
X factor	9.40%	1.81%	1.65%	0.56%	9.53%	

Source: AER analysis.
Note: Includes revenues approved in our Emergency standard cost pass through decision and annual updates for return on debt up to and including 2023–24.

7 AER, *Final decision, SA Power Networks Distribution Determination, 2020 to 2025, Overview*, June 2020, p. 21.

The correction to the approved revenue adjustments in Table 3 also reflects the correction we have made to SA Power Networks' allowed revenues for the demand management innovation allowance mechanism (DMIAM).

We calculated the DMIAM allowances for SA Power Networks in our final determination for the 2020–25 regulatory control period based on the approved unsmoothed expected revenue we determined for the period. Because we have revoked and substituted the approved unsmoothed expected revenue (as in Table 3), we have also revoked and substituted the approved DMIAM allowances to reflect the substituted revenue amounts.

Table 4 sets out the substituted DMIAM allowance for SA Power Networks for the 2020–25 regulatory control period. The varied allowance in Table 4 substitutes the allowance in Table 8 of our final determination overview, published on 5 June 2020, which we revoke.[8]

Table 4 AER's revocation and substitution determination on SA Power Networks' demand management innovation allowance ($ million, 2019–20)

	2020–21	2021–22	2022–23	2023–24	2024–25	Total
DMIAM	0.76	0.74	0.77	0.77	0.75	3.78

Source: AER analysis.

4 Service target performance incentive scheme

In the final distribution determination for the 2020–25 regulatory control period we calculated the service target performance incentive scheme (STPIS) incentive rates that apply to SA Power Networks in the period based on the approved smoothed expected revenue. Because we have revoked and substituted the approved smoothed expected revenue (as per Table 3), we have also revoked and substituted the approved STPIS incentive rates to reflect the substituted revenue amounts. The substituted incentive rates in Table 5 substitute the incentive rates in Table 10.1 of our final determination, Attachment 10, published on 5 June 2020, which we revoke.[9]

Table 5 AER's revocation and substitution determination on STPIS incentive rates for the 2020–25 regulatory control period

	CBD	Urban	Short rural	Long rural
SAIDI	0.0033	0.0466	0.0087	0.0087
SAIFI	0.2635	3.0851	0.7382	1.0540

Source: AER analysis.

[8] AER, *Final decision, SA Power Networks Distribution Determination, 2020 to 2025, Overview*, June 2020, p. 36.

[9] AER, *Final decision, SA Power Networks Distribution Determination, 2020 to 2025, Attachment 10*, June 2020, p. 5.

As a consequence of this correction, SA Power Networks has:

- under-recovered STPIS rewards related to performance in the 2020–21 year by $176,579 ($2022–23)
- under-recovered STPIS rewards related to performance in the 2021–22 year by $134,058 ($2023–24).

Additionally, the STPIS rewards related to performance in the 2022–23 year has been under-stated by $74,855 ($2024–25).

5 Control mechanism

To correct SA Power Networks' STPIS rewards, we have revoked and substituted the control mechanism in the final determination for the 2020–25 regulatory control period. We have corrected the discrepancies in payments created by this error through a corrective adjustment in the I factor of the revenue cap formula.

The relevant amounts ($176,579, $134,059, and $74,855) as noted above are in real dollars for the year that they would otherwise have been applied.

Interest charges will apply for the intervening years between the time the STPIS payments were applied (2022–23 and 2023–24) and the regulatory year the payment is passed through to network tariffs (2024–25). An interest charge is not required for the amount determined in 2024–25. These interest charges are to be calculated using the respective approved nominal weighted average cost of capital (WACC) in line with the treatment applied in the unders and overs accounts.

To allow for this, we make the following adjustment to the I factor in both the revenue cap formulae and the side constraint formulae.

> This will also include adjustments in year t=5 (2024–25) to correct for under-recoveries in the year t=3 (2022–23) and t=4 (2023–24) STPIS payments and an understatement in the year t=5 (2024–25) STPIS payment.

6 Consultation

In accordance with rule 6.13(d), the AER consulted with SA Power Networks and considered the feedback provided by it before making the decision to revoke and substitute SA Power Networks' final determination for the regulatory control period 1 July 2020 to 30 June 2025.

Prior to SA Power Networks submitting its 2025–30 regulatory proposal, which proposed to return the over-recovered revenues via lower revenues in the next regulatory control period, the AER had been working with SA Power Networks to understand the error and consider options for returning it to customers.

On 22 February 2024, SA Power Networks' CEO sent a letter to the AER Chair expressing his concerns with the prospect that the AER would revoke and substitute its 2020–25 distribution determination through lower 2024–25 prices. We have considered each of these concerns, and those made via other consultation processes in relation to this matter, in making the substituted determination. Nonetheless, we have determined that we should revoke and substitute the 2020–25 distribution determination. The error was made and identified by SA Power Networks and we consider that the error should be corrected and the revenue returned to customers as soon as possible, within the current regulatory control period. This view around the timing of returning the over-recovered revenue was expressed consistently by customer representatives as a matter of principle.

As part of our consultation with SA Power Networks we:

- Informed SA Power Networks of the consistent feedback we had received from our meetings with the Customer Consultative Group, Energy Consumers Australia and the South Australian Council of Social Service that customers would prefer to receive the over-recovered revenue as soon as possible. When we provided SA Power Networks with this view it questioned whether and how we had informed customer representatives of the revenue and price impacts in the next regulatory control period if the revenues were returned in 2024–25. We confirmed that we informed customer representatives of the revenue and price impacts in the full five years of the 2025–30 regulatory control period, as well as in 2024–25.
- Shared the corrected 2020–25 post tax revenue model and the corrected STPIS modelling with SA Power Networks. SA Power Networks did not identify any issues with the revenue modelling.
- Sought SA Power Networks' views on whether it considered it necessary for the DMIAM allowances and the STPIS incentive rates to be updated to reflect the corrected allowed revenues. SA Power Networks stated that is considered all consequential flow on updates, including to the DMIAM allowances and STPIS incentive rates, should be corrected.
- Discussed the impacts on SA Power Networks' proposal for the 2025–30 regulatory control period.

For the meetings we held with the Customer Consultative Group, Energy Consumers Australia and the South Australian Council of Social Service we presented information that explained the error and showed the different options that were available in terms of returning the over-recovered revenues as a result of the error. This included returning revenues in 2024–25 with two different profiles of revenue in the 2025–30 regulatory control period, as well as returning these revenues in the 2025–30 regulatory control period as proposed by SA Power Networks. As noted above, customer representatives provided clear feedback that customers would prefer to receive the over-recovered revenue returned as soon as possible.

SA Power Networks also requested that we seek the views of its Community Advisory Board (CAB). The AER attended a meeting of the CAB on 13 March 2023. At that meeting the majority view of the CAB was that the revenue should be returned to customers in 2024–25 through lower prices.

Constituent decisions

Our decision to revoke and substitute the SA Power Networks' distribution determination for the 2020–25 regulatory control period involves varying the following constituent decisions in our substituted determination:

Constituent decision
In accordance with clause 6.12.1(2)(i) of the NER, the AER's final decision is not to approve the annual revenue requirement set out in SA Power Networks' building block proposal. Our final decision on SA Power Networks' annual revenue requirement for each year of the 2020–25 regulatory control period is set out in ~~attachment 1 of this final decision~~ this revocation and substitution determination.
In accordance with clause 6.12.1(3)(ii) of the NER and acting in accordance with clause 6.5.7(d), the AER's final decision is not to accept SA Power Networks' proposed total forecast net capital expenditure of $1693.4 million ($2019–20). Our final decision therefore includes a substitute estimate of SA Power Networks' total forecast net capex for the 2020–25 regulatory control period of ~~$1595.8 million ($2019–20)~~ $1,696.0 million ($2019–20). The reasons for our final decision are set out in attachment 5 of our final determination published 5 June 2020 and this revocation and substitution determination.
In accordance with clause 6.12.1(4)(ii) of the NER and acting in accordance with clause 6.5.6(d), the AER's final decision is not to accept SA Power Networks' proposed total forecast operating expenditure, inclusive of debt raising costs and exclusive of DMIA of $1469.5 million ($2019–20). Our final decision therefore includes a substitute estimate of SA Power Networks total forecast opex for the 2020–25 regulatory control period of $1,419.8 million ($2019–20). The reasons for our final decision are set out in attachment 6 of our final determination published 5 June 2020 and this revocation and substitution determination.
In accordance with clause 6.12.1(7) of the NER, the AER's final decision on the estimate of SA Power Networks' corporate income tax is $~~22.7 million ($ nominal)~~ $11.5 million ($ nominal). This is discussed in attachment 7 of ~~this~~ our final decision published 5 June 2020 and this revocation and substitution determination.
In accordance with clause 6.12.1(8) of the NER, the AER's final decision is to not approve the depreciation schedules submitted by SA Power Networks. Our final decision substitutes alternative depreciation schedules that accord with clause 6.5.5(b) and is discussed in attachment 4 of ~~this~~ our final decision published 5 June 2020 and this revocation and substitution determination.
In accordance with clause 6.12.1(9) of the NER, the AER makes the following final decisions on how any applicable efficiency benefit sharing scheme (EBSS), capital expenditure sharing scheme (CESS), service target performance incentive scheme (STPIS), demand management incentive scheme (DMIS), demand management innovation allowance mechanism (DMIAM) or small-scale incentive scheme is to apply: • We will apply version 2 of the EBSS to SA Power Networks in the 2020–25 regulatory control period. This is discussed in attachment 8 of ~~this~~ our final decision published 5 June 2020. • We will apply the CESS as set out in the Capital Expenditure Incentives Guideline to SA Power Networks in the 2020–25 regulatory control period. This is discussed in attachment 9 of ~~this~~ our final decision published 5 June 2020. • We will apply our STPIS to SA Power Networks for the 2020–25 regulatory control period. This is discussed in attachment 10 of ~~this~~ our final decision published 5 June 2020 and this revocation and substitution determination.

- We will apply the DMIS and DMIAM to SA Power Networks in the 2020–25 regulatory control period. This is discussed in section 2.7 of ~~this~~ the final decision overview published 5 June 2020 and this revocation and substitution determination.