Final Decision

Essential Energy Electricity Distribution Determination 2024 to 2029

(1 July 2024 to 30 June 2029)

Overview

April 2024

AUSTRALIAN ENERGY REGULATOR

Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601
Tel: 1300 585 165

AER reference: AER212495

Amendment record

Version	Date	Pages
1	30 April 2024	49

List of attachments

This Overview forms part of the AER's final decision on the distribution determination that will apply to Essential Energy for the 2024–29 period. It should be read with all other parts of the final decision.

As a number of issues were settled at the draft decision stage or required only minor updates, we have not prepared all attachments. In these circumstances, our draft decision reasons form part of this final decision. The final decision attachments have been numbered consistently with the equivalent attachments to our draft decision.

The final decision includes the following documents:

Overview

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 4 – Regulatory depreciation

Attachment 7 – Corporate income tax

Attachment 13 – Classification of services

Attachment 14 – Control mechanisms

Attachment 16 – Alternative control services

Attachment 18 – Connection policy

Attachment 19 – Tariff structure statement

Attachment 20 – Metering services

Attachment A – Contingent projects

Executive Summary

The Australian Energy Regulator (AER) exists to ensure 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 as it transitions to net zero emissions. The regulatory framework governing electricity transmission and distribution networks is the National Electricity Law and Rules (NEL and NER). Our work is guided by the National Electricity Objective (NEO).

A regulated network business must periodically apply to us to determine the maximum allowed revenue it can recover from consumers for using its network. On 31 January 2023 we received a revenue proposal from New South Wales (NSW) electricity distribution network service provider Essential Energy, for the period 1 July 2024 to 30 June 2029 (2024–29 period).

This final decision is the conclusion of over two and half year's work to determine what Essential Energy can recover from its customers in the 2024–29 period.

On 20 October 2021, Essential Energy formally requested we revise its Framework and approach (F&A) paper. The F&A is responsible for determining which services we will regulate, and why, and the broad nature of the regulatory arrangement. Our final decision on Essential Energy's F&A was published in July 2022.

In March 2022, we accepted Essential Energy as one of the first two businesses on the Better Resets Handbook's (the Handbook) early signal pathway. As part of this process, we had the opportunity to engage extensively and receive early access to data and information relevant to the expectations set out in the Handbook.

Essential Energy submitted its initial proposal on 31 January 2023, which we acknowledged was a high-quality proposal, and developed through an extensive, genuine engagement process.

In March 2023, our Issues paper outlined that we, based on our assessment as part of the early signal pathway process, would undertake a targeted review of Essential Energy's proposal including: about 50% of the total capital expenditure (capex) forecast, its forecasting approach relating to aspects of its base operating expenditure (opex), and the Future Networks step change, the depreciation approach for the proposed new asset class for Distributed Energy Resources, and a proposed new two-way pricing tariff.[1] We also highlighted that additional factors impacting the Australian economy may affect Essential Energy's total revenue for 2024–29 period. In particular, that there has been increases in interest rates and inflation over the 2019–24 period.

We held a public forum in April 2023 to assist stakeholders in their consideration of Essential Energy's proposal and received a number of submissions prior to publishing our draft decision on 28 September 2023. Our draft decision accepted much of Essential Energy's proposal, including its total capex and opex forecasts.

---

1 AER, *Issues Paper - Essential Energy – 2024–29 Distribution revenue proposal*, March 2023, p. 2.

Essential Energy responded to our draft decision in its revised proposal, submitted 30 November 2023. Interested stakeholders were invited to provide submissions on our draft decision and Essential Energy's revised proposal.

Our assessment has been balanced so that consumers only pay for what is necessary and in their long term interests. When we undertake our expenditure assessments, we consider whether or not we are satisfied that proposed expenditure reasonably reflects prudent and efficient costs and a realistic expectation of future demand and cost inputs (the capex and opex criteria).[2] We must make our decision in a manner that will, or is likely to, deliver efficient outcomes in terms of the price, quality, safety, reliability and security of supply, and to achieve targets for reducing Australia's greenhouse gas emissions that benefit consumers in the long term (as required under the NEO).[3]

In practice, this has involved us applying our various analytical tools, such as the replacement capital expenditure (repex) model and economic benchmarking for opex, scrutinising the business cases and supporting information provided by the businesses, and having regard to the advice provided by our expert consultants. In addition, our findings have been informed by the various stakeholder submissions we received, and the information on consumer preferences and priorities elicited through the consumer engagement processes of the businesses and from our Consumer Challenge Panel.

We have assessed that the majority of expenditure Essential Energy has proposed is likely to deliver these efficient outcomes and is therefore in the long term interests of consumers.

Our final decision on Essential Energy’s revised proposal

Our final decision is that Essential Energy can recover $6,309.9 million ($nominal, smoothed) from consumers over the 2024–29 period. This is $116.8 million (1.9%) more than Essential Energy’s revised proposal, and $118.8 million (1.9%) more than our draft decision.

Essential Energy’s revised proposal accepted most components of our draft decision, including capex and opex and its tariff structure statement. The increase in overall revenue in this final decision, compared to Essential Energy’s revised proposal, is mainly driven by updates in data related to external economic factors, such as a lower expected inflation rate (which increases the regulatory depreciation building block) and a higher forecast rate of return.

For illustrative purposes, we estimate that the total revenue from this final decision would result in an average increase of $39 per annum to the typical electricity bill for Essential Energy’s residential customers over the 2024–29 period. For small business customers, the impact would be an increase on average of $83 per annum.

In our draft decision we accepted much of Essential Energy’s proposal, including its total capex and opex as we were satisfied that this reasonably reflects prudent and efficient costs to maintain the safety, reliability and security of the network. We acknowledged that

2 National Electricity Rules (NER), cl.6.5.6(c) and cl. 6.5.7(c).

3 National Electricity Law (NEL), ss. 7, 16(1)(a).

Essential Energy's consumer engagement was a material factor in accepting most of its proposal.[4]

Our final decision accepts Essential Energy's revised total capex forecast of $2,655.4 million ($2023–24) for the 2024–29 period and its revised total opex forecast of $2,323.0 million ($2023–24), including debt raising costs, for the 2024–29 period. Consistent with the findings in our draft decision, we are satisfied that Essential Energy's expenditure reflects its prudent and efficient costs.

Our draft decision on Essential Energy's total capex forecast was provisional on Essential Energy providing sufficient justification to support the efficient cost of its stand-alone power system (SAPS) proposal. We are satisfied that Essential Energy's revised proposal has provided sufficient information to justify its SAPS proposal.

To manage uncertain costs, Essential Energy's revised proposal included a new nominated cost pass through event to recover potential costs associated with the reclassification of bushfire risk across its network in the 2019–24 period. We do not consider this risk is best managed through a new nominated pass through event, but rather we consider the costs appropriate for consideration as contingent capex. Our final decision therefore includes a contingent project to provide Essential Energy the flexibility and time needed to appropriately consider the impact of changing bushfire risk management requirements, conduct necessary engagement with affected communities, and develop a proposal for cost recovery once the need for and quantum of costs has been established.

Essential Energy accepted our draft decision approach to calculating its Efficiency Benefit Sharing Scheme (EBSS) penalty, however its revised proposal also requested we reconsider the application of the EBSS based on an amended (higher) opex forecast for the 2019–24 period. It suggested that the EBSS penalties were excessive, and its alternative approach better aligns with regulatory precedent and the intent of the incentive regime.

We have reviewed the approach proposed by Essential Energy and recognise the penalties for overspends in the 2019–24 period as calculated under the EBSS are material. We have reflected the higher level of opex incurred by Essential this period (relative to its forecast) in the higher opex forecast for the 2024–29 period. We therefore consider that the EBSS carryover amounts determined in this final decision are consistent with the intended operation of the scheme. The EBSS outcomes should not be considered in isolation, but rather taken together with our forecasting approach for total opex, which works together with the EBSS to appropriately share efficiency rewards and penalties.

Our draft decision largely accepted Essential Energy's tariff structure statement, but requested Essential Energy to make or consider minor improvements for its revised tariff structure, including further information on its high voltage battery/storage tariff and simplifying its two-way tariffs. Our final decision approves Essential Energy's revised tariff structure statement with a minor amendment to its storage tariff.

Our final decision accepts Essential Energy's revised proposal to reclassify metering services as a standard control service. Following the metering review final decision by the

---

4 AER, *Draft Decision - Overview - Essential Energy – 2024–29 Distribution revenue proposal, September 2023*, p. x.

Australian Energy Market Commission (AEMC), our draft decision asked businesses to consider reclassifying legacy metering services to standard control services.[5] We outlined this approach would result in the benefit of socialising Essential Energy's legacy metering services costs across a wider customer group and mitigate inequitable price impacts during the smart meter transition.

Ensuring consumers pay no more than necessary while supporting the future energy network transition

Our draft decision reflected that the 2024–29 revenue determinations had been developed during a challenging time for energy consumers and the sector more broadly. Economy wide factors have resulted in higher inflation and interest rates, and cost-of-living pressures and affordability concerns continue to be important to consumers.

Energy Consumers Australia's recent sentiment survey observed that 54% of households believe having affordable energy prices is the most important issue for the future energy system (up 5%).[6] While consumers note current cost-of-living pressures and the challenges ahead for the energy system in terms of the importance of affordable energy prices for all Australians, they are also considering the importance of the energy transition and the pace at which this should be occurring.[7]

Our final decisions for the 2024–29 businesses continue to seek the balance of affordability, with necessary expenditure required to support the energy transformation, and to address important emerging issues such as network cybersecurity, climate resilience, integration of consumer energy resources (CER), and digitalisation.

Our draft decision noted the role distributors could play in the energy transition. We also note that the Australian Energy Market Operator's (AEMO's) recent Draft Integrated System Plan states that the lowest cost way to supply electricity throughout Australia's transition to a net zero economy is with new transmission and modernised distribution networks. These will connect a diverse mix of utility-scale renewables, rooftop solar and distributed solar, and firming technologies such as energy storage to consumers.[8]

AEMO's Optimal Development Path (Step Change) includes a forecast of a four-fold increase in rooftop solar capacity by 2050, representing almost a third of the total generation capacity. It also includes facilitating consumer-owned batteries and coordinated CER via Virtual Power Plants to deliver flexible demand response to the National Electricity Market, representing almost half of the total dispatchable capacity. AEMO's draft 2024 Forecasting Assumptions update also outlines that electric vehicle (EV) uptake is forecast to increase from the 2023 yearly projections under all scenarios.[9]

---

5 AEMC, *Final Report: Review of the regulatory framework for metering services*, August 2023.

6 Energy Consumers Australia, *Sentiment Survey,* December 2023. See https://ecss.energyconsumersaustralia.com.au/sentiment-survey-dec-2023/.

7 Energy Consumers Australia, *Challenges ahead for the energy system' and 'Speed of transition,* December 2023. See https://ecss.energyconsumersaustralia.com.au/sentiment-survey-dec-2023/featured-content-household-sentiment-dec-2023/.

8 AEMO, *Draft 2024 Integrated System Plan (ISP),* 17 January 2024, pp. 9-11.

9 AEMO, *Draft 2024 Forecasting Assumptions Update*, December 2023, p. 24

Given these ongoing developments, we maintain that flexibility in response to a rapidly changing energy industry is important. We consider the national regulatory framework can adapt to changes in technology, emerging business models and evolving customer preferences.

Alongside the transitioning energy market, the current environment has several uncertainties that network businesses are required to consider, including evolving threats around cybersecurity and climate risk. These issues have been central considerations for all businesses in developing their 2024–29 proposals. All businesses have proposed, to varying extents, investments in new and emerging areas of CER integration, climate resilience, and cybersecurity.

We recognise the continuing need for investments in these important areas. We have provided efficient levels of funding to enable the businesses to continue to respond prudently to the cyber security risks and climate change-related risks that their networks face.

In addition, our decisions provide both necessary funding for export service levels so customers with rooftop solar may export their excess electricity to the grid, and appropriate price signals to optimise network capacity. Where network tariff price signals are passed through in a retail offer, and customers are well placed to respond, appropriately structured network tariffs can enable growth in the value and number of people with CER, particularly rooftop solar. Energy storage operating in line with the right price signals will direct more renewables to peak evening periods when fossil fuel generation still dominates supply.

Similarly for the forecast increase in electricity demand from a continued uptake of EVs, the right mix of investment and price will facilitate new, clean, forms of transport at least cost to electricity customers.

Innovation will assist customers who are able to respond with greater opportunities to reduce their bills. The accelerated roll-out of smart meters to customers, flagged by the AEMC's metering review, is a critical enabler for the energy transition, including the integration of CER work programs. Our decisions facilitate cost recovery of old legacy network-delivered meters in the quickest, least cost way to all customers.

Some of our 2024–29 final decisions provide for dedicated innovation expenditure – this will enable the businesses to test new and unproven technologies and ways of managing their networks, to benefit consumers. We also outline guidance on what factors we will consider in assessing future innovation expenditure proposals.

The amended National Electricity Objective and the current regulatory determination resets

The NEL requires us to make our decision in a manner that contributes, or is likely to contribute, to achieving the NEO. The focus of the NEO is on promoting efficient investment in, and operation and use of, electricity services (rather than assets) in the long term interests of consumers. This is not delivered by any one of the NEO's factors in isolation, but rather by balancing them in reaching a regulatory decision.

Prior to the emissions objective rule change, the 2024–29 businesses' proposals were already considering the challenges faced by the energy transition, including the steps needed to deliver net zero.

Many of the businesses have been proactive in considering the impact of emissions reduction as part of their regulatory proposals. In considering customer and stakeholder engagement provided as part of the regulatory resets, many of these network service providers noted that stakeholders were advising that climate change mitigation was a priority to them and should be incorporated or prioritised accordingly in regulatory proposals.

We have had regard to the recently published interim value of emissions reduction in these final decisions where relevant. In the 2024–29 regulatory determinations, only a limited number of businesses used a quantitative value in their initial and revised regulatory proposals, and it was related to a relatively small component of the proposed overall expenditure, such as in the case of certain innovation and CER-related expenditure. In those cases, we have considered the interim value of emissions reduction in assessing whether to accept or reject specific programs as part of our final decisions.

Consumers at the centre of proposals

As outlined in our draft decision, consumer engagement is an important facet of our assessment; together with ensuring we are satisfied that the proposed forecast reasonably reflects prudent and efficient costs and a realistic expectation of future demand and cost inputs. Genuine engagement with consumers is likely resulting in better quality proposals and we are looking to see how consumer values and preferences are shaping engagement.

Since the release of the Handbook we have seen a strong commitment from all 2024–29 businesses to engage with customers and have their preferences considered and reflected in their revenue proposals.[10] As one of the first businesses on the early signal pathway, we consider Essential Energy demonstrated a genuine commitment to consumer engagement.

Essential Energy noted that as the cost of living has increased for its customers, it wanted to re-test support for its planned investments in resilience and network of the future. Essential Energy's revised proposal maintains support from consumers and stakeholders, and it indicates that customers' reasons for support varied, but most commonly they stated that the investment 'is needed, seems to be fair/well-reasoned/balanced, and that the costs are reasonable/acceptable.'[11]

The Consumer Challenge Panel, sub-panel 26 (CCP26) has highlighted that ongoing engagement is likely to deliver considerable benefits. Consumer engagement is likely to reduce the volume of bespoke reset-related engagement activities that are needed to adequately inform regulatory proposals, through businesses having a better understanding of the long term insights from their consumers.[12]

Following this decision, we encourage Essential Energy to build on the work undertaken during this process to ensure consumer engagement becomes a sustainable and continuous business-as-usual process.

---

10 AER, *Better Resets Handbook – Towards consumer centric network proposals,* December 2021, p. 13.

11 Essential Energy, *2.01 Summary of engagement outcomes*, November 2023, p. 3.

12 Consumer Challenge Panel 26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy* January 2024, p. 14.

The 2024–29 final decisions mark the completion of the first businesses whose proposals have been developed using the expectations and guidance in the Handbook. We have heard from consumer stakeholders, that while the guidance of the Handbook has been valuable, there should be consideration of the application of the Handbook and early signal pathway.

The Handbook not only sets important expectations on how network businesses engage with consumers, but outlines our expectations for capex, opex, regulatory depreciation and tariff structure statements. These aspects are important to ensure we continue to encourage networks to develop high quality proposals through genuine engagement with consumers and that meet our expectations to constrain cost increases.

We acknowledge the importance of seeking insights and learning from this process for future regulatory determinations. We are not undertaking a formal review of the Handbook at this stage, however, we will be seeking to capture and refine the feedback already provided. We will continue to develop the successful application of the Handbook as we work with the businesses on current and upcoming determinations.

Contents

1 Our final decision

Our final decision allows Essential Energy to recover a total revenue of $6,309.9 million ($ nominal, smoothed) from its consumers from 1 July 2024 to 30 June 2029.

In the sections below we briefly outline what is driving Essential Energy's revenue, and the key differences between our final decision revenue compared to the $6,191.1 million in our draft decision, and the $6,193.1 million in its revised proposal.

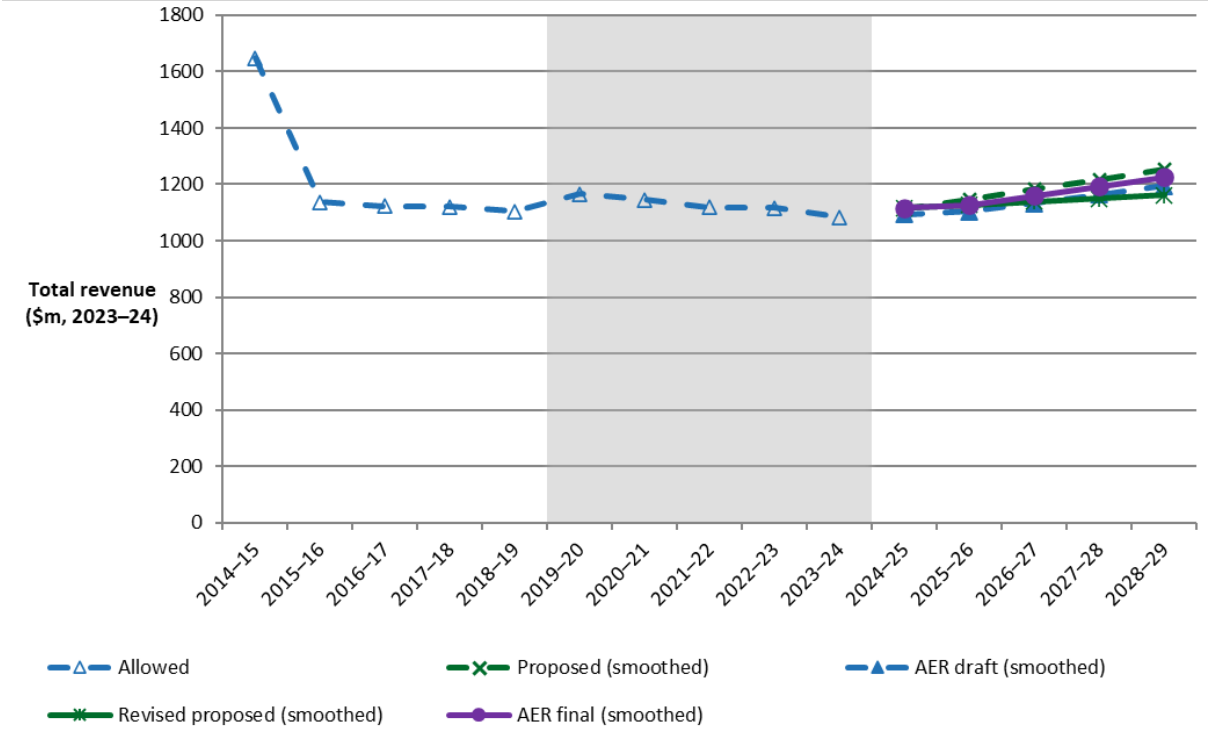
1.1 What is driving revenue?

Revenue is driven by changes in real costs and inflation. We assess costs (such as capex and opex) in real terms.

Over time, inflation impacts the spending power of money. To compare revenue from one period to the next on a like-for-like basis, in this section we use 'real' values based on a common year (2023–24) that have been adjusted for the impact of inflation instead of the nominal values above.

In real terms, this final decision would allow Essential Energy to recover $5,820.5 million ($2023– 24, smoothed) from consumers over the 2024–29 period. This is 3.4% higher than our decision for the current (2019–24) period. Changes in Essential Energy's revenue over time are shown in Figure 1.

Figure 1 Changes in regulated revenue over time ($ million, 2023–24)



Source: AER analysis.

In real terms, this final decision would allow Essential Energy to recover a total building block revenue of $5,822.4 million ($2023–24, unsmoothed) over the 2024–29 period. Figure 2

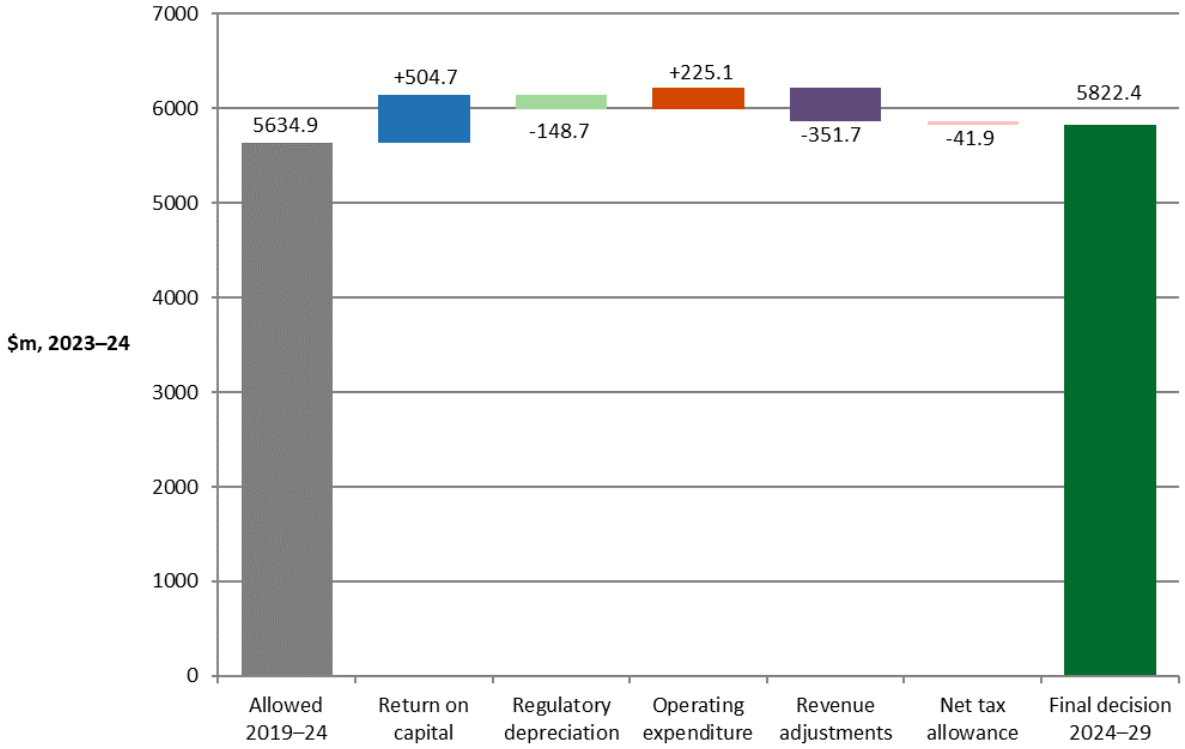
highlights the key drivers of the change between the revenue approved for Essential Energy for the 2019–24 period and in this final decision for the 2024–29 period. Similar to our observations in the draft decision, it shows that our final decision provides for reductions in the building blocks for:

- return of capital (regulatory depreciation), which is $148.7 million (19.3%) lower than the 2019–24 period, driven primarily by a higher indexation of the regulatory asset base (RAB) for the 2024–29 period
- revenue adjustments, which are $351.7 million lower than the 2019–24 period, mainly due to the large negative efficiency benefit sharing scheme (EBSS) outcome applied in this final decision
- net tax allowance, which is $41.9 million (47.7%) lower than the 2019–24 period, primarily due to the exclusion of gifted assets from the calculation of the estimated cost of corporate income tax in the 2024–29 period. It is also due to a lower regulatory depreciation (which lowers income) and a higher tax depreciation (which increases tax deductions) determined in this final decision compared to the 2019–24 period.

Figure 2 also shows that our final decision provides for increases in the building blocks for:

- return on capital, which is based on the opening RAB, capex and rate of return. This is $504.7 million (19.2%) higher than the 2019–24 period, driven by an increase in the RAB due in part to higher actual inflation in that period, and a higher rate of return being applied in the 2024–29 period, in accordance with the 2022 Rate of Return Instrument.
- opex, which is $225.1 million (10.7%) higher than the opex forecast we approved in the 2019–24 period, driven primarily by higher actual opex in the base year, step changes and output growth.

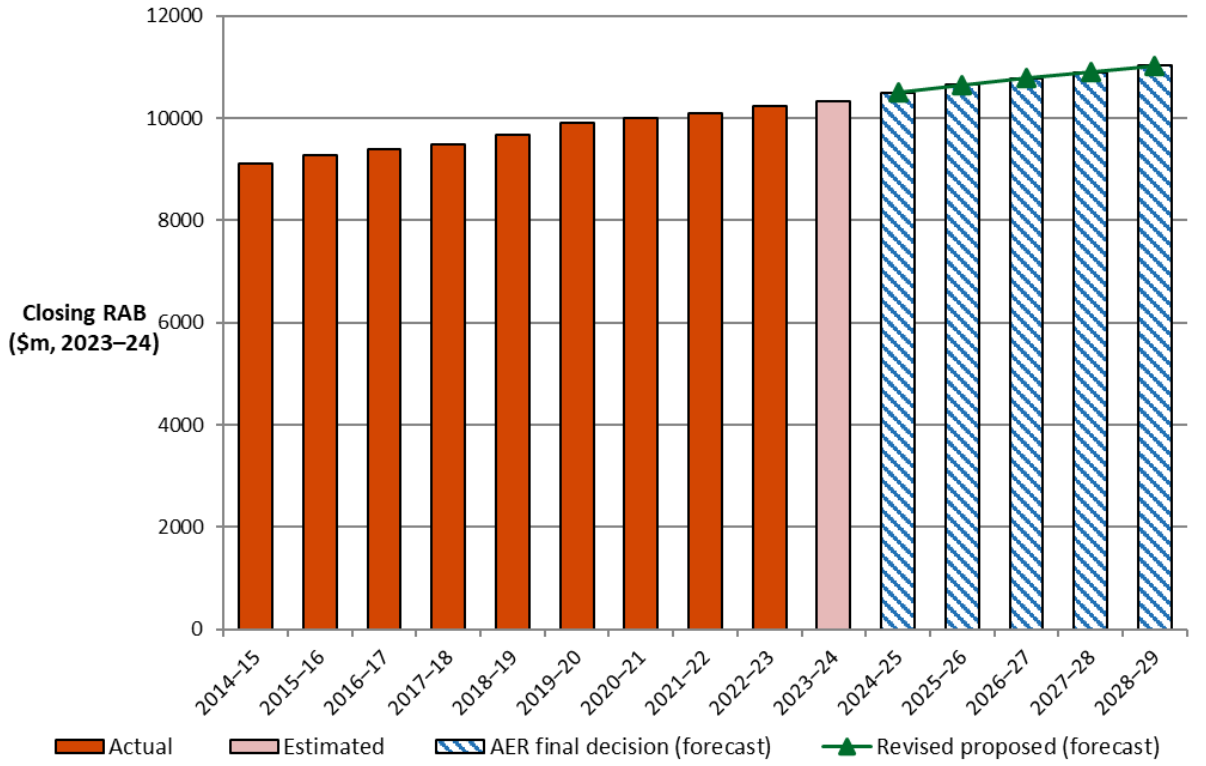
Figure 2 Changes in total revenue 2019–24 to 2024–29 ($ million, 2023–24 unsmoothed)



Source: AER analysis
Note: This comparison is based on converting 2019–24 forecast opex for inflation to 2023–24 dollar terms using lagged consumer price index (CPI).

Figure 3 shows the value of Essential Energy's combined RAB over time. The RAB grew by 6.9% in real terms over the 2019–24 period. Our final decision results in a further forecast increase of the RAB by $699.3 million (6.8%) over the 2024–29 period. The growth in RAB over 2024–29 is primarily driven by higher forecast capex than the 2019–24 period.

Figure 3 Essential Energy RAB value over time ($ million, 2023–24)



Source: AER analysis.

1.2 Key differences between our final decision and Essential Energy's revised proposal

Essential Energy's revised proposal accepted our draft decision with minor updates to reflect the latest available inputs and made mechanistic updates to revenue requirements.

Our final decision determines a total unsmoothed revenue that is $121.9 million (2.1%) ($2023–24) higher than Essential Energy's revised proposal. Movements in market variables such as expected inflation and rate of return have led to revenue outcomes that are higher in our final decision than in Essential Energy's revised proposal. These include:

- higher return on capital, driven primarily by a higher average rate of return over the 2024–29 period
- higher regulatory depreciation amount, driven primarily by the lower expected inflation rate in our final decision than at the time of Essential Energy's revised proposal
- higher estimated cost of corporate income tax amount, driven primarily by our final decision on a higher regulatory depreciation amount and higher return on equity amount.

The higher regulatory depreciation and return on equity amounts increase the cost of corporate income tax as they are both components of revenue for tax purposes.

Essential Energy's revised proposal responded to our draft decision guidance in relation to managing legacy metering services following the final decision of the Metering review by the AEMC. As a result, Essential Energy proposed legacy metering costs to move to standard control services.

Essential Energy's revised proposal also included a new nominated pass-through event for bushfire risk reclassification. The purpose of this event was to address any material cost impacts of implementing new bushfire risk classification and management systems that may be identified following a current coronial inquiry. Our final decision recognises this need, but instead of a new nominated pass through event, we consider these potential costs appropriate for consideration as contingent capex.

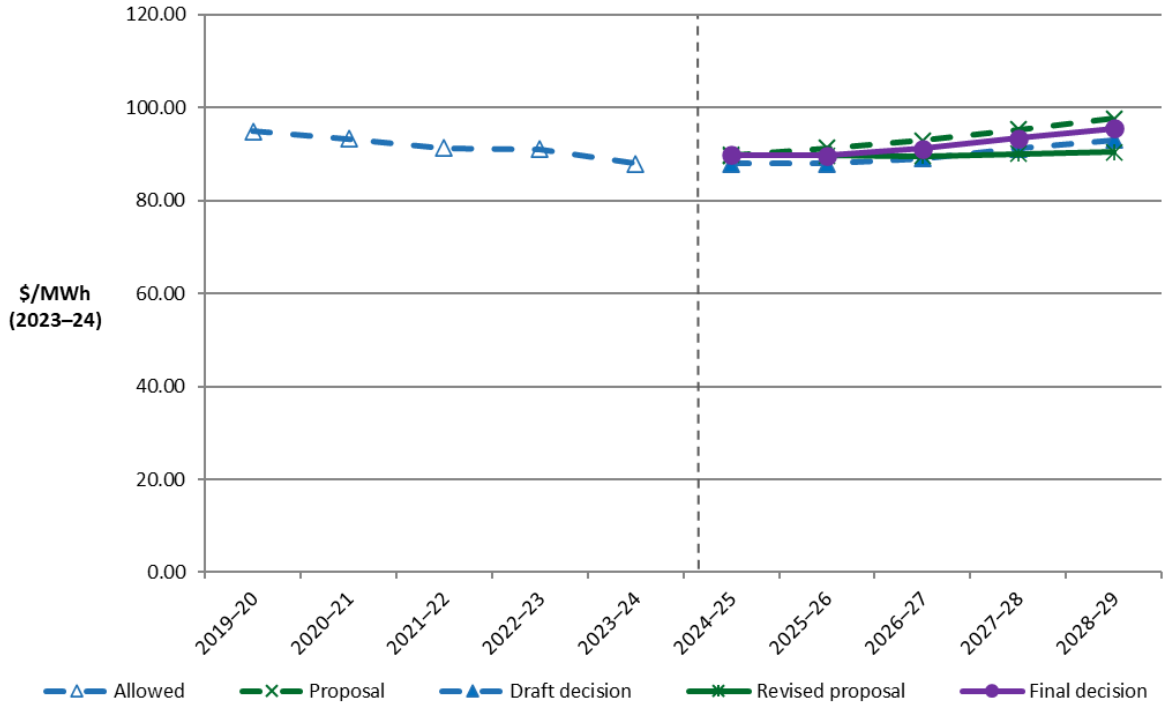
1.3 Expected impact of our final decision on electricity bills

Essential Energy recovers its regulated revenue through distribution charges, set annually by reference to the tariff structure statement and pricing formulae approved by us as part of this decision.

For illustrative purposes only, we estimate the impact of this final decision would be a total increase to Essential Energy's distribution charges of around 6.9% in real terms by 2028–29 compared to 2023–24 levels, or an average increase of 1.3% per annum.[13] This estimate will be subject to ongoing revenue adjustments and changes in consumer energy consumption. Figure 4 compares this indicative price path for the 2024–29 period to the 2019–24 period.

[13] The average increase to indicative distribution charges of 1.3% ($2023–24) per annum reflects two components: 1) The final decision smoothed revenue average increase of 2.1% per annum ($2023–24); and 2) The forecast energy delivered in Essential Energy's distribution network area which is expected to increase on average by 0.8% per annum.

Figure 4 Change in indicative charges for 2019–24 to 2024–29 ($2023–24, $/MWh)



Source: AER analysis.

1.3.1 Potential bill impact

Essential Energy's distribution charges make up around 35% of its residential customers' electricity bills and 33% of its small business customers' electricity bills. Other components of the electricity supply chain—the cost of purchasing energy from the wholesale market, transmission network charges, environmental schemes and the costs and margins applied by electricity retailers in determining the prices they will charge consumers for supply—also contribute to the prices ultimately paid by consumers.[14] These sit outside the decision we are making here and will also continue to change throughout the period.

In nominal terms, which include the impact of expected inflation, the impact of this final decision would be an increase to Essential Energy's network component of customers' energy bills. For illustrative purposes only, we estimate the impact of our final decision on the average annual electricity bill for a customer in Essential Energy's network area, as it is today, would be:

- an increase of $194 (7.7%) by 2028–29, or an average of $39 per annum for a residential customer

[14] AEMC, *Data Portal, Trends in NSW supply chain components 2023/24*.

- an increase of $417 (7.2%) by 2028–29, or an average of $83 per annum for a small business customer.[15]

Our decision on Essential Energy's revised proposal will set the revenue allowance that forms the major component of its network charges for the next 5 years. It provides a baseline or starting point for that period.

Over the 2024–29 period there are several additional mechanisms under the NER that may operate to increase or decrease those charges. These include cost pass through events or contingent projects[16] proposed by Essential Energy and approved in this final decision. The triggers we have set out for these events or the contingent project in this decision will, if met, allow Essential Energy to apply for additional revenue throughout the period, at which point proposed costs will be subject to further consultation and assessment.

1.4 Consumer Engagement

Essential Energy undertook comprehensive and significant engagement approach with its customers throughout the development of its 2024–29 determination. This included its participation in the early signal pathway process.

Essential Energy continued its engagement program following the submission of its initial proposal with an additional 5th phase to inform its revised proposal. Phase 5 comprised a similar structure to Phases 1–4, but with the addition of a new People's Panel and customer webinar.[17]

Essential Energy noted that as the cost of living has increased for its customers, it wanted to re-test support for its planned investments in resilience and network of the future. It invited its customers who had participated in Phase 1–4 to a webinar, where they were updated on changes to its proposal and any resulting bill impacts.

Following this session, customers were asked to complete a short survey to indicate whether they still provided their support. A total of 252 customers completed the survey, with 96% indicating their support for these investments.[18] The CCP26 observed that while Essential Energy confirmed its customers still supported the proposal, it did not engage explicitly with customers on their affordability concerns in the same way as the other businesses.[19]

CCP26 observed that Essential Energy's 5th engagement phase was targeted to manage a smaller number of issues. They observed engagement on Essential Energy's reclassification

---

15 Our estimated bill impact is based on the typical annual electricity usage of 4,613 kWh and 10,027 kWh for residential and small business customers in Essential Energy's network area, respectively. This is based on the 2023–24 final decision default market offer.

16 A contingent project has been approved for Essential Energy for the reclassification of bushfire risk, see Attachment A.

17 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p. 11.

18 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p. 11.

19 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.10.

of bushfire risks, approaches for allocation of costs for legacy meters, and changes to the tariff structure statement.[20]

CCP26 observed that Essential Energy's post-lodgement engagement has continued to deliver a well planned and executed engagement program, with Essential Energy genuinely willing to listen to customers and take their ideas on board. CCP26 state that the People's Panel was a very effective engagement channel and will be a valuable asset as part of their ongoing activities. CCP26 consider that, overall, the post-lodgement engagement has met the expectations of the Handbook.[21]

In relation to the reclassification of bushfire risk, CCP26 note that Essential Energy had engaged with its Stakeholder Collaborative Collective (SCC) and People's Panel to inform them of the likely changes to vegetation management practices following any potential findings of the NSW Coronial Inquest. CCP26 observed that the issues were clearly explained and understood by participants.[22]

CCP26 noted that Essential Energy indicated it did not support the EBSS carryover calculation and that leading up to the submission of its revised proposal, Essential Energy informed its SCC of its intention to provide further information on an alternative approach. However, the CCP26 noted it was surprised that given such a significant change in revenue that Essential Energy was seeking ($68 million more in revenue) that it did not appear to be the subject of engagement with its customers and stakeholders.[23]

The Public Interest Advocacy Centre (PIAC) observed that Essential Energy has the most mature and consistent engagement history of the NSW businesses and has done well to build on its learnings from previous engagement. PIAC observed that Essential Energy's People's Panel has done well to build on learnings from previous engagement, however improvements could be made to the structure of the program, suggesting it move away from elements such as snap-polling and undirected table conversations in order to strengthen the deliberative quality of the engagement.[24]

CCP26, also observed that consistent with its earlier advice, attendance at its SCC remained problematic. CCP26 note that the SCC continued to effectively provide feedback but consider that the group's capacity to provide the breadth and depth and ongoing advice and support Essential Energy is seeking may have been impacted.[25]

---

20 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.4.

21 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.4.

22 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, pp. 9-10.

23 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.14.

24 PIAC, *Submission on the NSW revised proposals and draft decisions 2024–29*, February 2024, p.28.

25 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.9.

We received a number of submissions on the tariffs of the NSW distributors.[26] For Essential Energy, this included, ACEnergy raising concerns with Essential Energy's High Voltage Distribution Battery and Hybrid tariff[27] and Origin Energy which supported the decision to modify its proposed tariffs in response to our draft decision and stakeholder feedback.[28] A submission from Southern Lights outlined it still had concerns with Essential Energy's proposed approach to public lighting. However, Southern Lights did acknowledge the increasingly open dialogue that it has had with Essential Energy.[29]

Essential Energy has indicated it will continue its engagement with stakeholders and customers as it implements its 2024–29 plans. This will include meeting regularly with its People's Panel to report on how it is tracking. Essential Energy considers this will set up its development for the next period and beyond. It believes that an ongoing business-as-usual approach to customers and stakeholder engagement is becoming increasingly important and necessary to build customer trust in a dynamic environment.[30]

CCP26 acknowledge that Essential Energy has made good progress towards establishing its ongoing business-as-usual engagement and suggest that in designing its fit-for-purpose engagement strategy, to consider whether there are ongoing roles for its stakeholder groups such as the SCC, Pricing Collaboration Collective and the New Technology Providers Forum.[31]

---

26 See the list of submissions received for Essential Energy at section 7.

27 ACEnergy, *Submission on Essential Energy's revised proposal and draft decision 2024–29*, January 2024.

28 Origin Energy, *Submission on the NSW and ACT revised proposals and draft decisions 2024–29*, January 2024, p.1

29 Southern Lights, *Submission on Essential Energy's revised proposal and draft decision 2024–29*, January 2024.

30 Essential Energy, *2.01 Summary of engagement outcomes*, November 2023, p. 12.

31 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.10.

2 Key components of our final decision on revenue

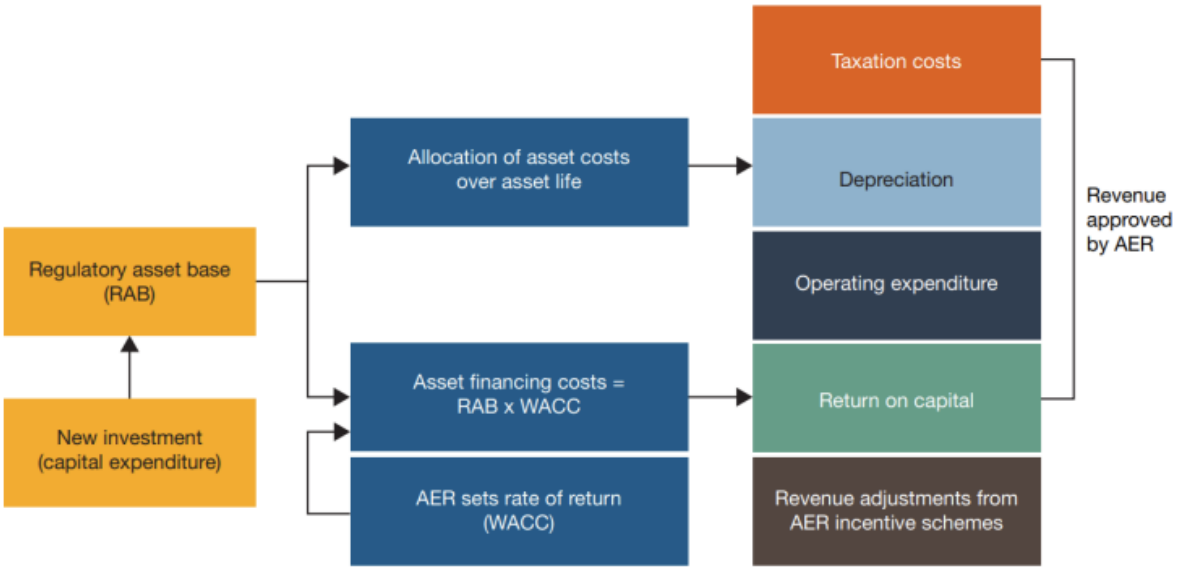
Building block approach

The foundation of our regulatory approach is a benchmark incentive framework to setting maximum revenues: once regulated revenues are set for a 5-year period, a network that keeps its actual costs below the regulatory forecast of costs retains part of the benefit. This provides an incentive for service providers to become more efficient over time. It delivers benefits to consumers as efficient costs are revealed and drive lower cost benchmarks in subsequent regulatory periods. By only allowing efficient costs in our approved revenues, we promote delivery of the NEO and ensure consumers pay no more than necessary for the safe and reliable delivery of electricity.

Essential Energy's proposed revenue reflects its forecast of the efficient cost of providing distribution network services over the 2024–29 period. Its proposal, and our assessment of it under the NEL and NER, are based on a 'building block' approach which looks at five cost components (see Figure 5):

- return on the RAB – or return on capital, to compensate investors for the opportunity cost of funds invested in this business
- depreciation of the RAB – or return of capital, to return the initial investment cost to investors over time
- forecast opex – the operating, maintenance and other non-capital expenses, incurred in the provision of network services
- revenue increments/decrements – resulting from the application of incentive schemes, such as the EBSS and capital expenditure sharing scheme (CESS)
- estimated cost of corporate income tax.

Figure 5 The building block model to forecast network revenue



Source: AER.

Following the AEMC's metering review, Essential Energy's revised proposal took up our draft decision recommendation to recover metering charges as standard control services and proposed to recover through a flat per customer charge. This issue is discussed further at section 5.1.

As a result of this change in classification, all building block components for Essential Energy have been affected by the moving of legacy metering services from alternative control services to standard control services.

The revenue smoothing profile determined for Essential Energy's final decision is based on standard control services, without the inclusion of metering.

For the purpose of our decision, the associated impacts of the metering revenue have been triaged out for consistency and are discussed in attachment 20.

Revenue smoothing

Our final decision incudes a determination of Essential Energy's annual revenue requirement (ARR) (unsmoothed revenue) and annual expected revenue (smoothed revenue) across the 2024–29 period. The expected revenues we set in this final decision are the amounts that Essential Energy will target for its annual pricing purposes and recover from its customers for the provision of standard control services for each year of the 2024–29 period.[32]

The ARR is the sum of the various building block costs for each year of the regulatory control period, which can be lumpy over the period. To minimise price shocks, revenues are smoothed within a regulatory control period while maintaining the principle of cost recovery under the building block approach. As such, revenue smoothing requires diverting some of the cost recovery to adjacent years within the regulatory control period. Revenue smoothing also helps to minimise any potential large revenue variance (and thus price shocks) at the commencement of the 2029–34 period.

For this final decision, we approved higher revenues than those in our draft decision and Essential Energy's revised proposal. This is mainly driven by external economic factors, which involves updating data to reflect lower expected inflation rate, which increases the regulatory depreciation building block and higher interest rates, which increases the return on capital. We have smoothed the increase in expected revenues over the 2024–29 period for Essential Energy.

Our final decision results in initial increases of 3.7% (nominal) per annum in 2024–25 and 2025–26, followed by average annual increases of 5.6% during the remaining 3 years of the 2024–29 period (2026–27 to 2028–29).

---

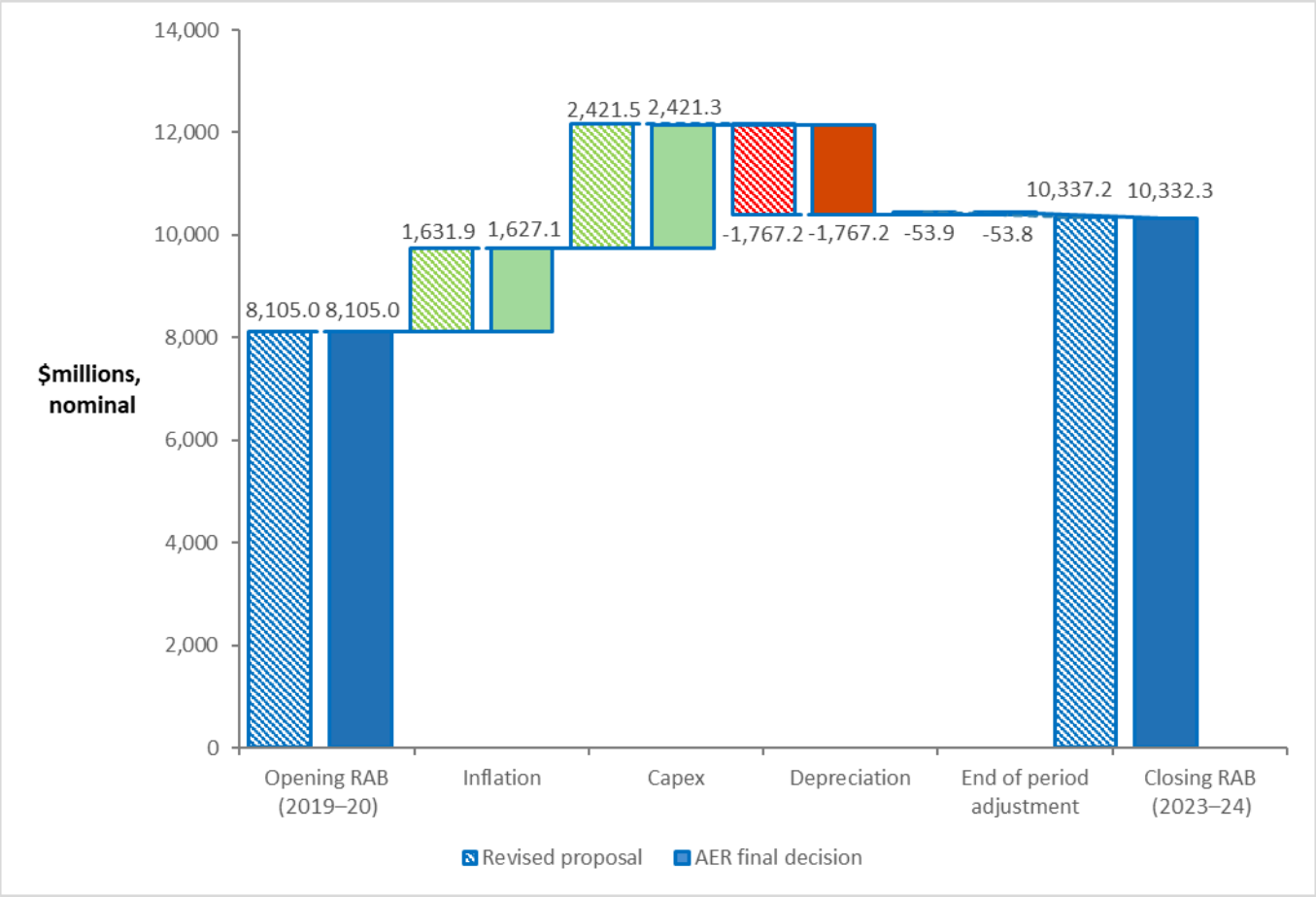
[32] Our final decision expected revenues have not factored in any changes arising from incentive scheme amounts, cost pass throughs or unders/overs reconciliation that usually occur in the annual pricing process to come up with the total allowed revenue.

2.1 Regulatory asset base

The RAB accounts for the value of regulated assets over time. To set the value of the RAB for a new regulatory period, we take the opening value of the RAB from the end of the last period and roll it forward each year by indexing it for inflation, adding new capex and subtracting depreciation and other possible factors (such as disposals). This gives us a closing value for the RAB at the end of each year of the regulatory period. The value of the RAB is used to determine the return on capital and regulatory depreciation building blocks. It substantially impacts Essential Energy's revenue, and the price consumers ultimately pay. Other things being equal, a higher RAB would increase both the return on capital and regulatory depreciation components of the revenue determination.

For this final decision, we have determined an opening RAB value of $10,332.3 million ($ nominal) as at 1 July 2024. This value is $4.9 million (less than 0.1%) lower than Essential Energy's revised proposal opening RAB value of $10,337.2 million. This reduction is largely due to the update we made to the consumer price index (CPI) input for 2023–24 to reflect the actual outcome in the roll forward model (RFM). Figure 6 shows the key drivers of change in Essential Energy's RAB over the 2019–24 period compared to its revised proposal.

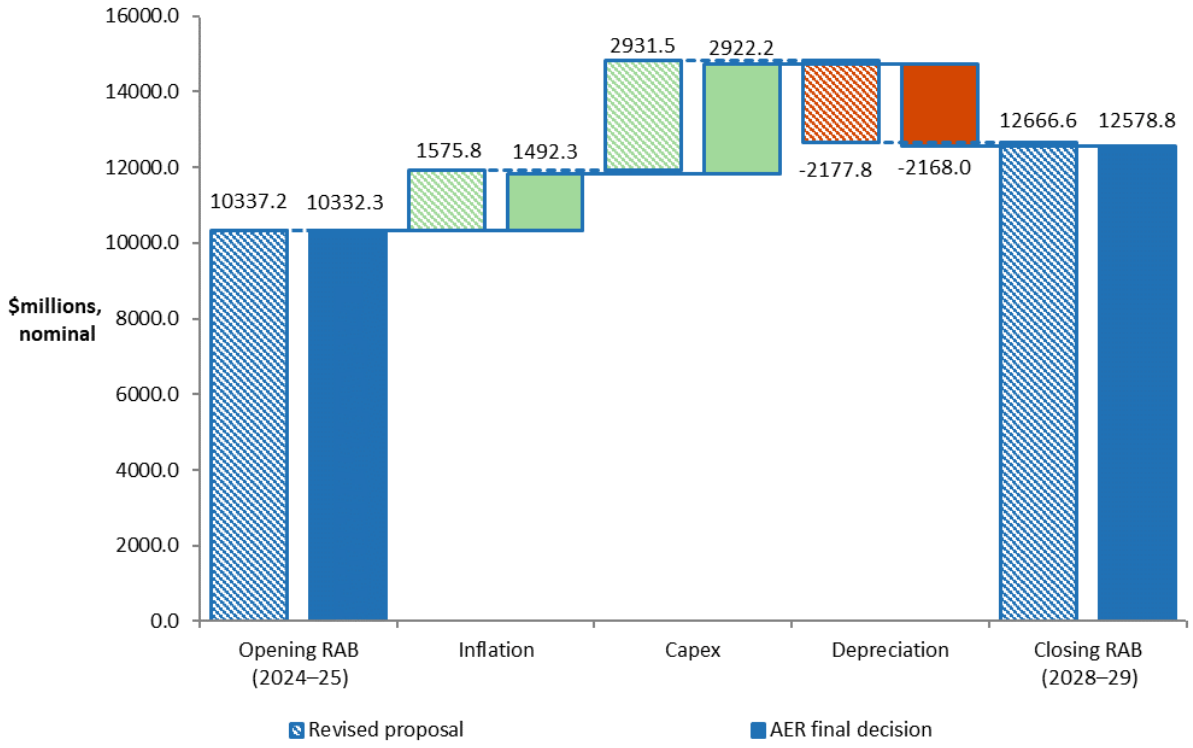
Figure 6 Key drivers of change in the RAB over the 2019–24 period – revised proposal compared with our final decision ($ million, nominal)



Source: AER analysis.
Note: Capex is net of disposals and capital contributions. It is inclusive of the half-year WACC to account for the timing assumptions in the RFM.

Figure 7 likewise shows the key drivers of change in Essential Energy's combined RAB over the 2024–29 period compared to its revised proposal. Our final decision projects an increase of $2,246.5 million (21.7%) to the RAB by the end of the 2024–29 period compared to the $2,329.4 million (22.5%) increase in Essential Energy's revised proposal. We have determined a projected closing RAB of $12,578.8 million ($ nominal) as at 30 June 2029, which is $87.8 million (0.7%) lower than Essential Energy's revised proposal of $12,666.6 million. This lower value is mainly due to our final decision on the expected inflation rate. It also reflects our final decision on a lower opening RAB as at 1 July 2024, forecast capex and forecast depreciation (discussed in the sections below).

Figure 7 Key drivers of change in the RAB over the 2024–29 period – revised proposal compared with our final decision ($ million, nominal)



Source: AER analysis.
Note: Capex is net of disposals and capital contributions. It is inclusive of the half-year WACC to account for the timing assumptions in the PTRM.

2.2 Rate of return and value of imputation credits

The return each business is to receive on its RAB (the 'return on capital') is a key driver of proposed revenues. We calculate the regulated return on capital by applying a rate of return to the value of the RAB.

We estimate the rate of return by combining the returns of two sources of funds for investment – equity and debt. The allowed rate of return provides the business with a return on capital to service the interest rate on its loans and give a return on equity to investors.

The estimate of the rate of return is important for promoting efficient prices in the long term interests of consumers. If the rate of return is set too low, the network business may not be able to attract sufficient funds to be able to make the required investments in the network and

reliability may decline. Conversely, if the rate of return is set too high, the network business may seek to spend too much, and consumers will pay inefficiently high tariffs.

The NEL requires us to apply the 2022 Rate of Return Instrument (Instrument)[33] to estimate the rate of return for Essential Energy.[34]

Essential Energy's revised proposal adopted the 2022 Instrument.[35] The 5.92% (nominal vanilla) rate of return in this final decision is higher than the 5.83% placeholder in the revised proposal, principally due to an increase in interest rates.

Our calculated rate of return in Table 1 would apply to the first year of the 2024–29 regulatory control period. A different rate of return may apply for the remaining years of the 2024–29 period. This is because we will update the return on debt component of the rate of return each year, in accordance with the 2022 Instrument, to use a 10-year trailing average portfolio return on debt that is rolled-forward each year. Hence, only 10% of the return on debt is calculated from the most recent averaging period, with 90% from prior periods.

Our final decision accepts Essential Energy's proposed risk-free rate[36] and debt averaging periods[37] because they were consistent with the 2022 Instrument.[38] For this final decision, we adopt the confidential appendix setting out the averaging periods issued with our draft decision.

Table 1 Final decision on Essential Energy's rate of return (nominal)

	AER's draft decision (2024–29)	Essential Energy's revised proposal (2024–29)	AER's final decision (2024–29)	Allowed return over the regulatory control period
Nominal risk-free rate	3.95%	3.95%	4.20% [a]	
Market risk premium	6.20%	6.20%	6.20%	
Equity beta	0.6	0.6	0.6	
Return on equity (nominal post-tax)	7.67%	7.67%	7.92%	Constant (%)
Return on debt (nominal pre-tax)	4.60%	4.60%	4.59%[b]	Updated annually

33 AER, *Rate of return Instrument (version 1.2)*, February 2023. See https://www.aer.gov.au/publications/guidelines-schemes-models/rate-of-return-instrument-2022/final-decision.

34 NEL, ss 18V and 18H.

35 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal,* 30 November 2023. p. 19.

36 AER, *Draft Decision Appendix A - CONFIDENTIAL Appendix to Attachment 3 - Rate of return – Essential Energy Distribution revenue proposal,* September 2023, p. 1.

37 AER, *Draft Decision Appendix A - CONFIDENTIAL Appendix to Attachment 3 - Rate of return – Essential Energy Distribution revenue proposal,* September 2023, p. 2.

38 AER, *Rate of return Instrument (version 1.2)*, February 2023, cll 7–8, 23–25.

	AER's draft decision (2024–29)	Essential Energy's revised proposal (2024–29)	AER's final decision (2024–29)	Allowed return over the regulatory control period
Gearing	60%	60%	60%	Constant (60%)
Nominal vanilla WACC	5.83%	5.83%	5.92%[c]	Updated annually for return on debt
Expected inflation	2.80%	2.80%	2.66%	Constant (%)

Source: AER analysis; AER, *Draft Decision Attachment 3 - Rate of return - Essential Energy – 2024–29 Distribution revenue proposal,* September 2023, p. 2; Essential Energy, *Revised Proposal - 3.04 Post Tax Revenue Model,* 30 November 2023.

(a) Calculated using Essential Energy's actual nominated risk-free rate averaging period from 4 December 2023 to 29 February 2024.
(b) Calculated using Essential Energy's actual nominated return on debt averaging period.
(c) Applied to the first year of the 2024–29 regulatory control period.

Debt and equity raising costs

In addition to providing for the required rate of return on debt and equity, we provide an allowance for the transaction costs associated with raising debt and equity. We include debt raising costs in the opex forecast because these are regular and ongoing costs, and equity raising costs in the capex forecast because these costs are incurred once and would be associated with funding particular capital investments. Our approach to forecasting capital raising costs is set out in more detail in our draft decision.[39]

Essential Energy has proposed to use our approach to estimate equity raising costs.[40] We have updated our estimate for the 2024–29 period based on the benchmark approach using updated inputs. This results in zero equity raising costs.

Our final decision accepts Essential Energy's revised opex proposal therefore we do not provide substitute estimates of its debt raising cost using our benchmark approach.[41]

Imputation credits

Our final decision applies a value of imputation credits (gamma) of 0.57 as set out in the 2022 Instrument.[42] Essential Energy's revised proposal has also adopted the value of gamma set out in the 2022 Instrument.[43]

---

39 AER, *Draft Decision - Attachment 3 - Rate of return – Essential Energy – 2024–29 Distribution revenue proposal,* September 2023, pp. 4-6.

40 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023. p. 19.

41 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023. p. 19.

42 AER, *Rate of return Instrument (version 1.2)*, February 2023, cll. 27.

43 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023. p. 19.

Expected inflation

As set out in Table 2 our estimate of expected inflation is 2.66%. It is an estimate of the average annual rate of inflation expected over a five-year period based on the outcome of our 2020 inflation review.[44]

Essential Energy's revised proposal adopted our current approach for estimating expected inflation.[45]

Table 2 Final decision on Essential Energy's forecast inflation (%)

	Year 1	Year 2	Year 3	Year 4	Year 5	Geometric average
Expected inflation	3.10%	2.60%	2.57%	2.53%	2.50%	2.66%

Source: AER Analysis; RBA, *Statement on Monetary Policy*, February 2024, Table 3.1: Detailed Forecast Table. See https://www.rba.gov.au/publications/smp/2024/feb/outlook.html#table31

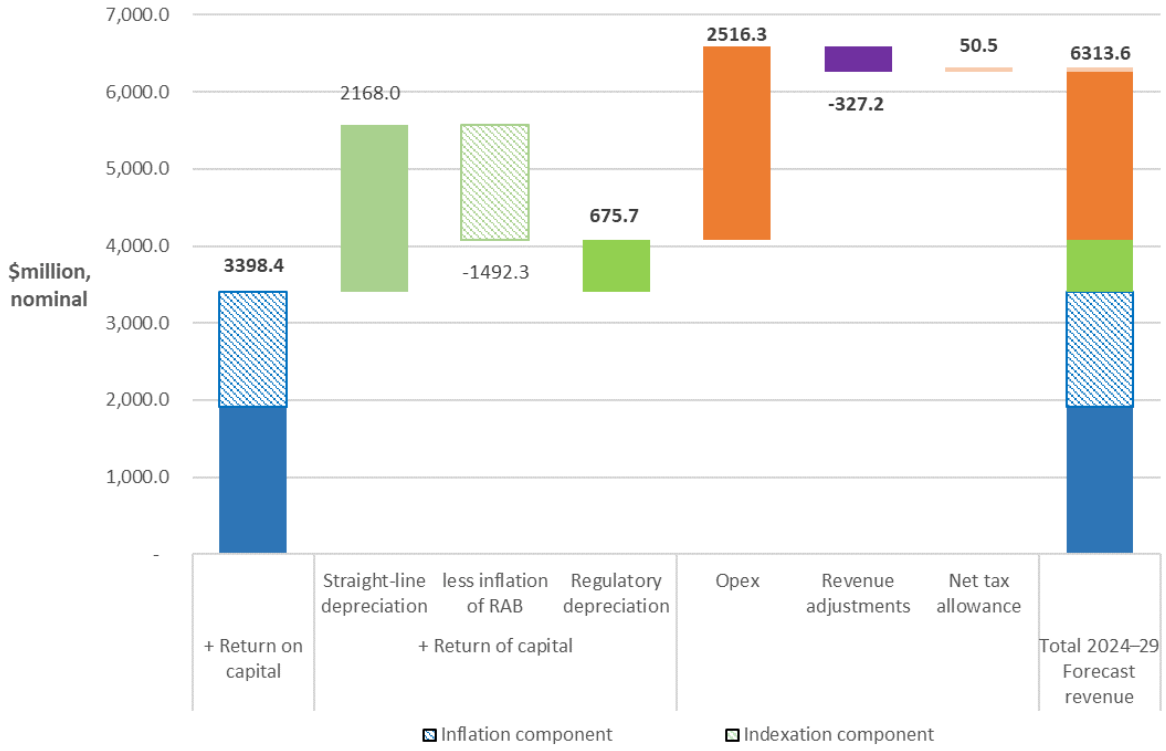
Our final decision uses the Reserve Bank of Australia's (RBA) February 2024 Statement of Monetary Policy (SMP) which contains a CPI forecast for the year-ending June 2024 and June 2025. This means the first two years of the 2024–29 period are based on RBA forecasts and, thereafter, a linear glide-path from year three to the mid-point of the RBA's inflation target band of 2.5% in year five.

Figure 8 isolates the impact of expected inflation from other parts of our final decision to illustrate its effect on the return on capital and regulatory depreciation building blocks, and the total revenue allowance. Other elements held constant, lower inflation reduces the return on capital, but increases regulatory depreciation.

44 AER, *Final position, Regulatory treatment of inflation*, December 2020.

45 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, 30 November 2023. p. 19.

Figure 8 Inflation components in final decision revenue building blocks – distribution and transmission ($ million, nominal)



Source: AER analysis.

2.3 Regulatory depreciation (return of capital)

Depreciation is a method used in our decision to allocate the cost of an asset over its useful life. It is the amount provided so capital investors recover their investment over the economic life of the asset (otherwise referred to as 'return of capital'). When determining total revenue, we include an amount for the depreciation of the projected RAB. The regulatory depreciation amount is the net total of the straight-line depreciation less the indexation of the RAB.

Our final decision determines a regulatory depreciation amount of $675.7 million ($ nominal) for the 2024–29 period. This is an increase of $73.7 million (12.2%) from Essential Energy's revised proposal of $602.1 million.

This increase is primarily due to our final decision on the expected inflation rate for the 2024–29 period, which affects the projected RAB over this period. The lower expected inflation rate applied in this final decision reduces the indexation of the RAB that is offset against straight-line depreciation in determining regulatory depreciation. The reasons for our decision are discussed in attachment 4.

2.4 Capital expenditure

Our final decision approves total forecast capex of $2,655.4 million ($2023–24) for the 2024–29 period. This is equivalent to Essential Energy's revised proposal taking into consideration updated inflation and real wage escalation. As in our draft decision, we accept Essential Energy's proposal for capex and remain satisfied that it reasonably reflects the capex criteria.

We also find Essential Energy's response to our draft decision request to demonstrate the efficient cost of its SAPS proposal to be satisfactory. In our draft decision, we noted that our acceptance of Essential Energy's total capex forecast was provisional on Essential Energy providing sufficient justification to support the efficient cost of its SAPS proposal of $52 million.[46] Essential Energy submitted:[47]

- Results from its recent market testing (August 2023), where 5 external SAPS suppliers responded to a competitive tender by providing quotes in relation to sites similar to the one that was included in the regulatory proposal. The average cost of these 5 quotes is higher than the SAPS unit costs included in Essential Energy's proposal.
- A summary of its independent consultant's review of the technical specifications of its SAPS solution to demonstrate that Essential Energy's SAPS proposal is not over-specified. Its consultant did not find any aspect of Essential Energy's SAPS technical specifications that sought to exceed performance requirements.

Our final decision also accepts Essential Energy's Bushfire Risk Reclassification contingent project. Essential Energy originally submitted a new cost pass through event to address expected costs from reclassification of large areas of the Essential Energy network into a higher bushfire risk category. We engaged with Essential Energy and found the costs were better treated as capex, with a contingent project the more appropriate mechanism for Essential Energy to recover its costs. Our decision is discussed at Attachment A – Contingent projects.

We received a submission from the CCP26 who noted that Essential Energy did not engage on the price impacts of this matter, acknowledging that this may have been because of the uncertainty of the potential costs.[48] CCP26 did consider, that where the regulatory requirements were met, it was their view a cost pass through would be a preferrable approach. CCP26 submitted that this would allow Essential Energy to analyse changes in requirements, conduct the necessary community engagement, properly scope the works, and put forward a realistic proposal for recovery of prudent and efficient costs.[49]

Table 3 provides a summary of our final decision by capex category.

---

46 AER, *Draft Decision Attachment 05 - Capital expenditure - Essential Energy- 2024–29 Distribution revenue proposal*, September 2023, p. 3.

47 Essential Energy, *Attachment 4.01: Stand-alone Power Systems – Supporting information*, November 2023.

48 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.11.

49 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, p.11.

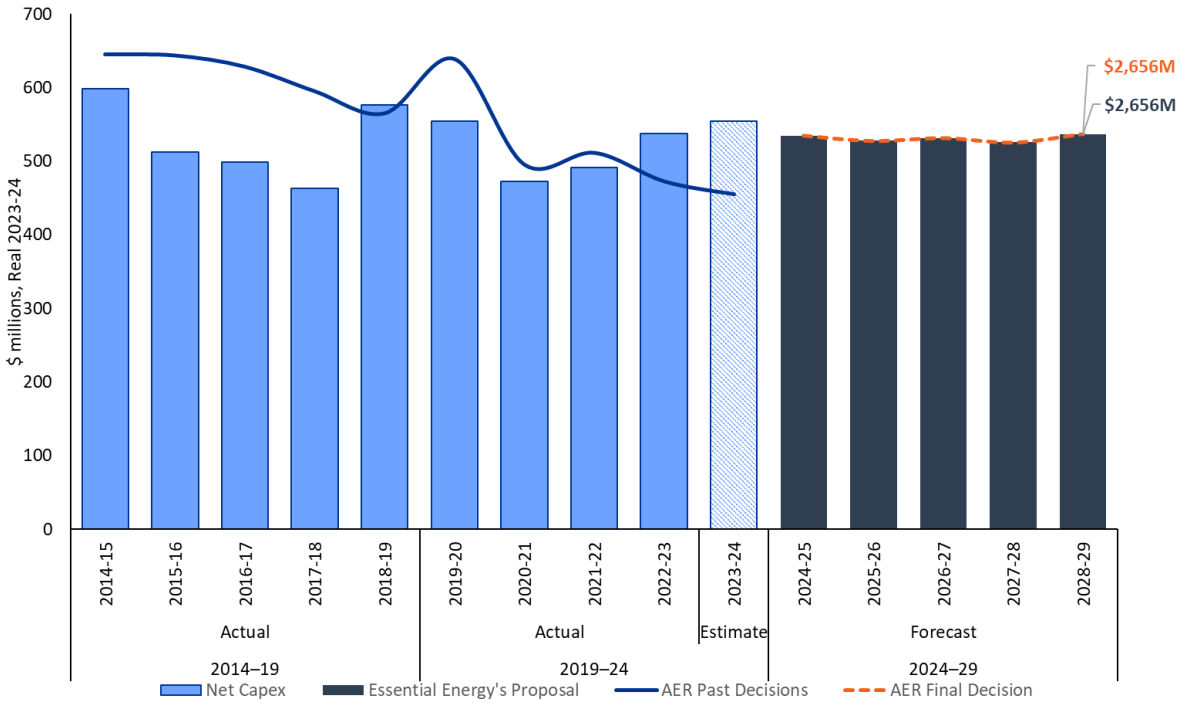
Table 3 AER's final decision by capex category ($million, $2023–24)

Category	Essential's proposal and AER final decision
Replacement	972.8
Augmentation	109.9
Connections	66.9
Capitalised overheads	830.1
CER integration[(a)]	86.6
Resilience[(b)]	204.8
ICT	106.8
Fleet	183.6
Capitalised leases	15.3
Property	73.0
Other non-network	14.5
Total capex (excluding capital contributions)	**2664.3**
Disposals	8.9
Net capex	**2655.4**

Source: Essential capex model and AER analysis.
(a) includes CER-related ICT
(b) includes repex-related resilience, augex-related resilience and property-related resilience.

Figure 9 shows Essential Energy's historical capex trend, its revised proposed forecast for the 2024–29 period, and our draft and final decision.

Figure 9 Essential Energy's historical and forecast capex ($2023–24, million)



Source: AER analysis. Capex is net of asset disposals and capital contributions.

Note: Numbers may not add up to totals due to rounding.

Essential Energy is one of the businesses selected to be on the early signal pathway. We found that Essential Energy had partially satisfied the capex expectations at the Issues paper stage. While we were satisfied with most of the top-down testing of its proposal, we did not have sufficient information leading up to the Issues paper to assess the prudency and efficiency of its key programs. Our targeted review involved assessing connections capex, augex and new and emerging capex common to several current regulatory proposals, these being in CER integration, resilience-related capex and cyber security ICT.

As outlined in our draft decision, for some expenditure such as CER, non-recurrent ICT, cyber security ICT and climate resilience, we assessed the forecasted investment to not be consistent with prudent and efficient decision-making. However, when we considered the total of these category level alternative estimates at the total capex level we found that our alternative forecast was not materially different from Essential Energy's total forecast.

2.5 Operating expenditure

Our final decision is to accept Essential Energy's revised total opex forecast of $2,323.0 million ($2023–24)[50], including debt raising costs, for the 2024–29 period.[51] Our alternative estimate of $2,287.3 million, including debt raising costs, is $35.7 million or 1.5% lower than Essential Energy's revised proposal of total forecast opex. We consider this is not materially different to Essential Energy's revised proposal. Consequently, we consider that Essential Energy's total opex forecast reasonably reflects the opex criteria.[52]

Essential Energy accepted our draft decision approach for opex, only applying mechanical updates to total forecast opex to:

- reflect actual, audited opex for the base year 2022–23[53]
- correctly reflect a change in the International Financial Reporting Interpretations Committee accounting guidance on Software as a Service (SaaS) costs, which will be implemented at the commencement of the 2024–29 period.[54] We noted in our draft decision that Essential Energy may have incorrectly reflected this change in its initial proposal.[55]
- reflect minor cost allocation method (CAM) updates that arose as a result of the mechanistic changes to the main standard control services opex and capex forecasts

50 All dollars, unless otherwise indicated are in $2023–24.

51 Essential Energy, *7.01 Standard Control Opex Model*, November 2023.

52 The opex criteria are set out in cl. 6.5.6(c) of the NER.

53 Essential Energy, *2024–29 Revised Regulatory Proposal*, November 2023, p. 38.

54 Essential Energy, *2024–29 Revised Regulatory Proposal*, November 2023, pp. 38-39.

55 AER, *Draft Decision – Essential Energy distribution determination 2024–29 – Attachment 6 – Operating expenditure*, September 2023, p. 26.

and updates to the legacy metering standard control services and alternative control service forecasts.[56]

- reflect more recent data on output measures (for customer numbers, circuit length and ratcheted maximum demand) and Wage Price Index (WPI) forecasts.[57]

The difference between our alternative total opex forecast and Essential Energy's revised proposal is due to us applying a non-recurrent efficiency adjustment,[58] the most up-to-date forecast inflation,[59] and updated forecast WPI from our consultant (KPMG).[60]

Table 4 shows Essential Energy's forecast opex over the 2024–29 period.

Table 4 Essential Energy's opex for the period 2024–29 ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Total Opex, excluding debt raising costs	449.9	455.0	458.9	464.2	467.3	2,295.2
Debt raising costs	5.4	5.5	5.6	5.6	5.7	27.7
Total Opex, including debt raising costs	**455.3**	**460.5**	**464.4**	**469.8**	**473.0**	**2,323.0**

Source: Essential Energy, *7.01 Standard Control Opex Model*, November 2023.
Note: Numbers may not add up to totals due to rounding.

Figure 10 compares our final decision total opex forecast for the 2024–29 period, which is the same as Essential Energy's revised proposal (the orange dashed line), to its actual and estimated opex in the previous and current regulatory control period (the blue bars). We have also included the forecasts we approved in past decisions (the orange solid line), Essential Energy's initial proposal for the 2024–29 period, which is the same as our draft decision (the blue dashed line with marker), and our alternative estimate for the final decision (the blue dashed line).

Figure 10 shows that our final decision opex forecast (Essential Energy's revised forecast of $2,323.0 million) is:

56 Essential Energy, *2024–29 Revised Regulatory Proposal*, November 2023, p. 40.

57 Essential Energy, *2024–29 Revised Regulatory Proposal*, November 2023, p. 39.

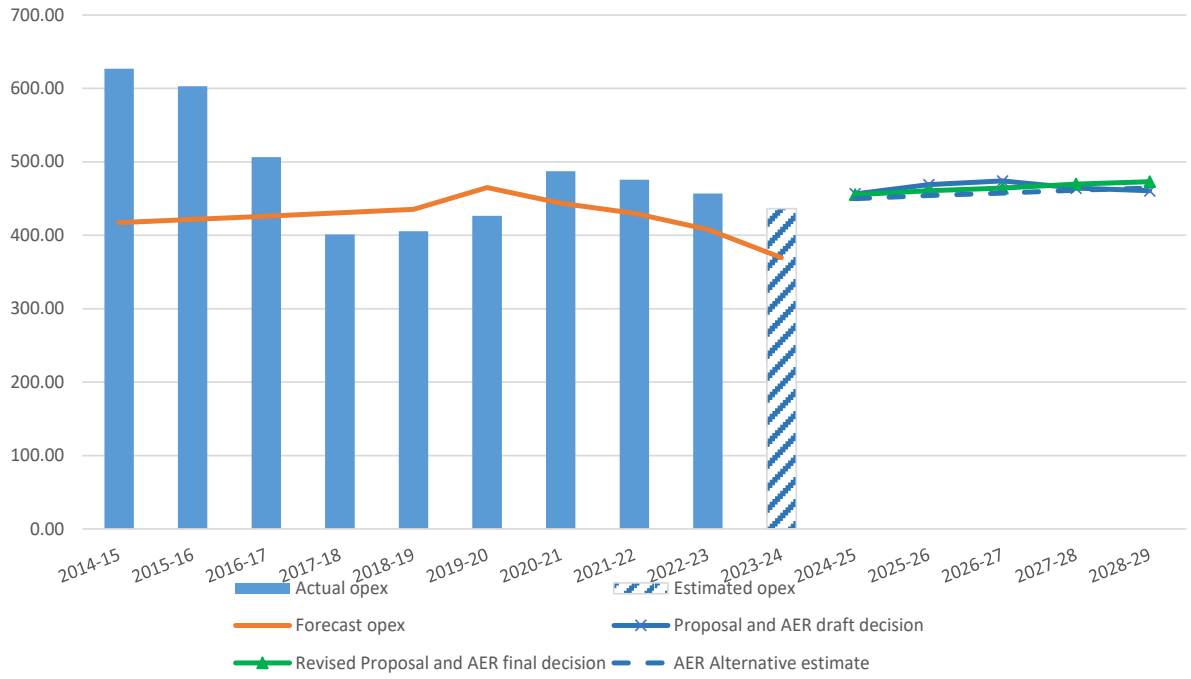
58 This is consistent with our draft decision where we also applied a non-current efficiency adjustment to align with our standard approach to forecast opex. In its initial proposal Essential Energy did not apply our standard final year equation to estimate opex in the final year of the current period. For more details, see: AER, *Draft Decision – Essential Energy distribution determination 2024–29 – Attachment 6 – Operating expenditure*, September 2023, pp. 17-18.

59 Our alternative estimate reflects forecast inflation as published in the 6 February 2024 *Statement on Monetary Policy* by the Reserve Bank of Australia.

60 KPMG, *Wage Price Index Forecasts Report 4*, 8 April 2024, p. 10.

- $207.1 million, or 9.8% higher than the opex forecast we approved in our final decision for the 2019–24 regulatory control period[61]
- $40.5 million, or 1.8% higher than Essential Energy's actual (and estimated) opex in the 2019–24 regulatory control period
- $0.9 million, or 0.04% lower than Essential Energy's initial proposal (our draft decision).

Figure 10 Essential Energy's historical and forecast opex ($million, 2023–24)



Source: Essential Energy, *Regulatory accounts 2014–15 to 2021–22*; Essential Energy, *9.03.07 Standard Control Operating Expenditure Model*, January 2023; Essential Energy, *7.01 Standard Control Opex Model*, November 2023; AER, Essential Energy *revenue determination, PTRM (multiple periods 2014–19, 2019–24, 2024–29)*; AER analysis.
Note: Includes debt raising costs and movements in provisions.

2.6 Corporate income tax

Our determination of the total revenue requirement includes the estimated cost of corporate income tax for 2024–29 period. Under the post-tax framework, this amount is calculated as part of the building blocks assessment using our post-tax revenue model (PTRM).

Our final decision determines an estimated cost of corporate income tax amount of $50.5 million ($ nominal) for Essential Energy over the 2024–29 period. This is an increase of $18.4 million (57.2%) from Essential Energy's revised proposal of $32.1 million.

61 The difference is calculated using our opex allowance for the 5 year 2019–24 period converted to real 2023–24 dollars using unlagged inflation. The difference of $225.1 million ($2023–24) stated in section 1.1 has been calculated using lagged inflation.

This increase is primarily due to our final decision on a higher regulatory depreciation amount and a higher return on equity amount (see sections 2.2 and 2.3). Regulatory depreciation and return on equity are both components of revenue for tax purposes. Therefore, higher regulatory depreciation and higher return on equity increase the estimated taxable income for Essential Energy which in turn increase the estimated cost of corporate income tax.

2.7 Revenue adjustments

Our calculation of Essential Energy's total revenue includes adjustments for incentive schemes that applied in its determination for the current period, such as under the EBSS and CESS. These mechanisms provide a continuous incentive for Essential Energy to pursue efficiency improvements in opex and capex, and a fair sharing of these between Essential Energy and its users.

Our final decision includes:

- A revenue adjustment of –$6.93 million ($2023–24) for the CESS. This is from the application of the CESS in the 2019–24 period and the corresponding CESS carryover true-up for 2018–19. Our final decision is $0.60 million more than Essential Energy's proposed decrement of $7.53 million, due to including a true-up carryover amount and updating capex to reflect latest available information.
- EBSS carryover amounts totalling –$302.0 million ($2023–24) from the application of the EBSS in the 2019–24 regulatory period. This is a $5.1 million ($2023–24) decrease compared to Essential Energy's proposed carryover amounts totalling –$296.9 million ($2023–24). The key driver of this difference is that we have updated the non-recurrent efficiency adjustment used in our draft decision for the latest opex data. We have done this as Essential Energy did not use our standard approach for forecasting opex in the final year of the current period. This ensures consistency between forecast opex and the EBSS so there is fair sharing of efficiency gains and losses between the distributor and consumers, consistent with the intent of the EBSS and NER requirements.
- An allowance of $5.6 million ($2023–24) for the Demand Management Innovation Allowance Mechanism (DMIAM). In each year of the 2024–29 period, Essential Energy will submit demand management projects for approval under the DMIAM. Any part of the $5.6 million that is not spent on an approved project will be returned to consumers in the subsequent regulatory control period.

The combined effect of these revenue adjustments is a negative $303.4 million ($2023–24) revenue adjustment building block in this final decision compared to the negative $299.0 million in Essential Energy's revised proposal.

3 Incentive schemes

Incentive schemes are a component of incentive-based regulation and complement our approach to assessing efficient costs. They provide important balancing incentives under network determinations, encouraging businesses to pursue expenditure efficiencies while maintaining the reliability and overall performance of the network.

Our final decision is that the following incentive schemes will continue to apply to Essential Energy in the 2024–29 period.

3.1 Capital Expenditure Sharing Scheme

The CESS mechanism was updated in April 2023. The changes to the CESS only apply to its application in the 2024–29 period and onwards. Our decision on CESS revenue increments to be added to capex allowance in the 2024–29 uses the CESS mechanism as it was before the update.[62]

Our final decision is set out in Table 5, which includes the capital expenditure sharing scheme carryover amount and true up calculation. This includes $20.84 million (nominal) in deferred capex for its billing system project, which we accept in our draft decision.[63] Essential Energy has not proposed to exclude any capex from the CESS.

Table 5 CESS revenue increments in 2024–29 ($ million 2023–24)

Revenue Adjustments	2024–25	2025–26	2026–27	2027–28	2028–29	Total
CESS revenue increments as per NER 6.4.3(a)(5)	-5.29	-5.29	-5.29	-5.29	-5.29	-26.44
CESS carryover true-up for 2018-19	3.90	3.90	3.90	3.90	3.90	19.51
AER final decision CESS	**-1.39**	**-1.39**	**-1.39**	**-1.39**	**-1.39**	**-6.93**

Source: AER analysis; Essential Energy, *3.06 Capital Expenditure Sharing Scheme Model*, 30 November 2023.
Note: Numbers may not sum due to rounding.

Essential Energy's revised proposal adjusted its actual/estimate capex for the current regulatory period, resulting in an increase in CESS benefit of $0.60 million.[64] This adjustment

62 That is, for CESS revenue increments based on spending in the 2019–24 regulatory period, we follow this guideline: AER, *Capital expenditure incentive guideline*, November 2013. However, in applying the CESS in the 2024–29 period, we refer to this guideline: AER, *Final decision - Capital expenditure incentive guideline*, April 2023.

63 AER, *Draft Decision Attachment 09 – Capital expenditure sharing scheme – Essential Energy – 2024–29 Distribution revenue proposal,* September 2023, p. 5.

64 Essential Energy, 3.*06 Capital Expenditure Sharing Scheme Model*, November 2023.

has increased the overspend from our draft decision and resulted in a CESS total decrement of $6.93 million. The reasoning for our final decision is consistent with our draft decision.

3.2 Efficiency Benefit Sharing Scheme

Our final decision is to include EBSS carryover amounts totalling –$302.0 million ($2023–24) from the application of the EBSS in the 2019–24 period. This is a $5.4 million ($2023–24) decrease compared to Essential Energy's revised proposed carryover amount of –$296.9 million ($2023–24). This difference primarily reflects an update to the non-recurrent efficiency adjustment (to reflect actual base year opex data) to ensure consistent application of the EBSS rewards and penalties despite the non-standard approach Essential Energy proposed to forecast its final year (2023–24) opex.

We set out our final decision on Essential Energy's EBSS carryover amounts in Table 6.

Table 6 Essential Energy's EBSS carryover amounts in 2024–29 ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Essential Energy's revised proposal	–66.6	–65.0	–49.5	–75.7	–40.0	–296.9
AER final decision	–67.4	–66.1	–50.6	–76.8	–41.2	–302.0
Difference	**–0.9**	**–1.1**	**–1.1**	**–1.1**	**–1.1**	**–5.4**

Source: AER analysis; Essential Energy, *Revised Proposal – 3.05 Efficiency Benefit Sharing Scheme Model*, 30 November 2023.
Note: Numbers may not sum due to rounding.

We will continue to apply version 2 of the EBSS to Essential Energy in the 2024–29 period, consistent with our draft decision.

Essential Energy's EBSS concerns

Essential Energy adopted a similar approach to the calculation of the EBSS carryover amounts for its revised proposal as our draft decision.[65] However, Essential Energy raised some concerns with the operation of the EBSS mechanism and its implementation in the current reset, and urged us to consider an amended EBSS penalty for the 2019–24 period.[66] Essential Energy identified several reasons why it was not able to reduce its actual opex down to the level it forecast in its 2019–24 proposal, including extreme weather events and an ambitious productivity forecast. It submitted that these factors distorted the outcomes under the EBSS and resulted in an unfair sharing of EBSS rewards and penalties between Essential Energy and its customers.[67] Essential Energy requested we consider the application of EBSS penalties based on an amended opex forecast for the 2019–24

65 Essential Energy, *2024–29 Revised Regulatory Proposal*, November 2023, pp. 6-7.

66 Essential Energy, *2024–29 revised regulatory proposal - 3.07 – EBSS concerns*, November 2023, p. 2.

67 Essential Energy, 2024–29 revised regulatory proposal, *3.07 – EBSS concerns*, November 2023, p. 2.

regulatory period where the annual productivity growth rate was reduced to 0.5%, consistent with our standard approach, which it considered would reduce the EBSS penalty by approximately $68 million.

We have considered Essential Energy's submission in relation to the calculation of EBSS carryover amounts from the application of the EBSS in the 2019–24 period. We have applied Essential Energy's opex forecast as approved for the 2019–24 period to determine the EBSS carryover amounts, consistent with the intended operation of the scheme and with our draft decision. We are not satisfied that the factors identified by Essential Energy as impacting its actual expenditure in the 2019–24 period justify us amending the intended sharing of efficiency rewards and penalties as determined under the scheme.

We recognise the occurrence of extreme weather events is not within Essential Energy's control and acknowledge it may not be able to recover all costs associated with extreme weather events through the cost pass through mechanism (for example, including where such costs are not 'material'). This is the case for all network service providers. However, we consider a network service provider has some control as to the way in which it prepares for and responds to these extreme weather events. As such, to the extent that emergency response costs are not recoverable through the cost pass through mechanism, we consider it is appropriate to incentivise prudent and efficient responses to such events through the application of the EBSS.

The nature of the EBSS is such that it shares the burden of these unexpected costs between Essential Energy and its customers. If costs incurred this way were not subject to the EBSS, Essential Energy would bear 100% of the cost burden itself. The operation of the EBSS should not be viewed in isolation, but rather considered together with our approach to forecasting opex on the basis of revealed efficient base year costs. Essential Energy's forecast opex for the 2024–29 period, which we have approved, is $207.1 million higher than its forecast for the 2019–24 period, reflecting the higher than anticipated expenditure in the current period.

We also recognise that in its 2019–24 revenue proposal, Essential Energy proposed an ambitious annual productivity growth rate and did not follow our (now) standard approach for the trend aspect of its operating expenditure forecast. Essential Energy noted that consumers have benefited from this approach in the current period, and that applying a significant penalty due to not meeting its productivity growth forecasts may disincentivise other network service providers from proposing ambitious productivity targets.[68] In applying the EBSS, we do not seek to discourage network service providers from choosing to pursue productivity targets that may benefit their customers. However, it is also important that the operation of the scheme is transparent, consistent and predictable over time. We note that the incentive properties and operation of the EBSS have not changed since Essential Energy's 2019–24 determination. The risks/rewards and potential EBSS outcomes associated with Essential Energy's proposed operating expenditure forecast were known or estimable at the time Essential Energy made its 2019–24 proposal. If we were to amend forecast opex for EBSS purposes on an ex-post basis, this would undermine the incentive

[68] Essential Energy, 2024–29 revised regulatory proposal, *3.07 – EBSS concerns*, November 2023, p. 2.

properties of the scheme, and the certainty it provides to network service providers as to how rewards and penalties will be calculated. These are central features of the regulatory framework under the NER and we consider there should be a very high bar for deviating from this approach.

We do not consider that it is appropriate to retrospectively amend the operation of the EBSS by substituting Essential Energy's 2019–24 opex forecast with an alternative opex forecast in order to alter the rewards and penalties applicable under the EBSS. If there is any uncertainty as to the forecast opex amounts that will be used to calculate EBSS rewards and penalties, it will distort the incentives for networks to incur only efficient costs. This would not be in the long term interests of consumers.

3.3 Service Target Performance Incentive Scheme (STPIS)

Essential Energy accepted our draft decision on the continued application of the STPIS excluding the customer service component (telephone answering parameter). In lieu of the STPIS customer service component, Essential Energy is applying the Customer Service Incentive Scheme (CSIS). [69]

Our final decision is consistent with attachment 10 of our draft decision, albeit with changes to reliability targets, incentive rates and value of customer reliability as a result of updates to the final revenue numbers and the CPI. The reasoning behind our position outlined in the draft decision.[70]

Further, Essential Energy must continue to report on the telephone answering parameter in the upcoming regulatory 2024–29 period.

Our final decision on each of these parameters is contained in Table 7, Table 8 and Table 9. The parameters that will apply to each component of the STPIS are published as part of this final decision.

Table 7 Final decision - STPIS reliability targets for Essential Energy for the 2024–29 period

	Urban	Short rural	Long rural
SAIDI (minutes)[71]	71.6482	210.3401	497.7318
SAIFI (interruptions)[72]	0.8538	1.7185	2.8102

Source: AER analysis.

69 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p.35.

70 AER, *Draft Decision Attachment 10 - Service target performance incentive scheme -Essential Energy – 2024–29 Distribution revenue proposal*, September 2023, p. 4.

71 System Average Interruption Duration Index (SAIDI).

72 System Average Interruption Frequency Index (SAIFI).

Table 8 Final decision - STPIS incentive rates for Essential Energy for the 2024–29 period

	Urban	Short rural	Long rural
ir - SAIDI	0.0125	0.0394	0.0093
ir - SAIFI	0.6974	3.2189	1.0976

Source: AER analysis.
Note: ir is the incentive rate (expressed in a percentage per unit of the parameter).

Table 9 Value of customer reliability (VCR) ($/MWh)

Feeder types	Urban	Short rural	Long rural
VCR	49,333	49,333	49,333

Source: AER analysis.

3.4 Demand Management Incentive Scheme (DMIS) and DMIAM

Our final decision is to apply the DMIS and DMIAM to Essential Energy in the 2024–29 period. This approach is consistent with Essential Energy's revised proposal[73] and our draft decision on DMIS and DMIAM.[74] The reasoning behind our position is also explained in the draft decision.[75]

The DMIAM allowance for Essential Energy for the 2024–29 period, based on the final PTRM for Essential Energy is contained in section 2.7.

3.5 Customer Service Incentive Scheme (CSIS)

Our final decision is that a CSIS will apply because Essential Energy's customer service incentive design meets the requirements of the scheme.[76] This is consistent with our draft decision and Essential Energy's revised revenue proposal.[77] The reasoning is outlined in our draft decision.[78]

---

73 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p. 35.

74 AER, *Draft Decision Attachment 11 - DMIS and DMIAM - Essential Energy – 2024–29 Distribution revenue proposal*, September 2023; Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p. 35.

75 AER, *Draft Decision Attachment 11 - DMIS and DMIAM - Essential Energy – 2024–29 Distribution revenue proposal*, September 2023; Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p. 7.

76 AER, *Draft Decision Attachment 12 – Customer service incentive scheme - Essential Energy – 2024–29 Distribution revenue proposal*, September 2023; Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023, p. 35.

77 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal,* November 2023, p. 35.

78 AER, *Draft Decision Attachment 12 – Customer service incentive scheme - Essential Energy – 2024–29 Distribution revenue proposal*, September 2023, pp. 5–10.

CCP26 commented that Essential Energy presented the final CSIS targets and incentive rates to its customers at phase 5 of its consultation process. Essential Energy's customers approved the revised CSIS targets and incentive rates when provided for consideration.[79]

Table 10 presents our final decision on the applicable performance targets, revenue at risk and incentive rates that will apply to Essential Energy for the 2024–29 period.

Table 10 Final decision – CSIS targets and incentive rates for Essential Energy for the 2024–29 period

Parameter	Baseline target	Cap[a]	Floor[b]	Incentive rate	Revenue at risk
Percentage of unplanned outages with estimated time to restore	19%	29%	9%	0.0500%	0.25%
Time to resolve customer complaints	14.4	13.4	15.4	-0.0050%	0.15%
Customer ease (post call survey score out of 5)	4.39	4.51	4.27	0.0417%	0.10%

Source: AER analysis; Essential Energy, *6.02 Customer Service Incentive Scheme*, November 2023, pp. 5–9.
Notes: (a) best performance
(b) worst performance.

Ongoing compliance with this determination

To comply with this determination, Essential Energy must submit its annual CSIS compliance model (provided as part of its proposal) used to calculate the annual revenue adjustment for the CSIS (H-factor). Robust data oversight is a vital component of the CSIS. The data used to populate the annual CSIS compliance model must be audited in accordance with our explanatory statement on CSIS[80] and/or the assurance requirements of our regulatory information order.

[79] CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision - Essential Energy*, January 2024, pp. 6, 18-19.

[80] AER, *CSIS Explanatory Statement*, July 2020, p. 13.

4 Tariff structure statement

Essential Energy's revised 2024–29 regulatory proposal includes its third tariff structure statement. This 2024–29 tariff structure statement will apply from 1 July 2024 and remain in effect for the 2024–29 regulatory period.

Our final decision is to approve Essential Energy's revised 2024–29 tariff structure statement with one amendment that:

- changes references to 'battery' tariffs to 'storage' tariffs to reflect that these tariffs should be applicable to storage technologies with similar connections and load profiles.

This amendment is in addition to the changes Essential Energy already made in its revised tariff structure statement to align with our draft decision. Those changes included:

- providing more information on the approach to setting individually calculated tariffs
- justifying removal of the rebate from the high voltage storage tariff
- responding to our suggested improvements to clarify some aspects of its tariff structure statement and to expand its customer impact analysis
- explaining how Essential Energy will give effect to the *Electricity Supply (General) Amendment (Green Hydrogen Limitation) Regulation* (network tariff exemptions for approved green hydrogen producers) through individually calculated tariffs
- simplifying its two-way tariff by adopting an energy-based kWh export tariff and basic export level and removing export pricing bands.[81, 82]

On energy storage, the amendment was discussed with Essential Energy after our draft decision was published. It is intended to ensure that Essential Energy's tariffs are consistent with cl. 6.18.4(a)(2) of the NER (retail customers with a similar connection and distribution service usage profile should be treated on an equal basis).

In Attachment 19 we describe our assessment of Essential Energy's revised tariff structure statement and explain our final decision to approve it.

---

81 kWh = kilowatt hour.

82 For a complete list of changes we encouraged Essential Energy to include in its revised tariff structure statement, see AER, *Draft Decision Attachment 19, Tariff Structure Statement, Essential Energy 2024–2029 Distribution Revenue Proposal,* September 2023, pp 4 – 5.

5 Other price terms and conditions

In this section, we consider the other aspects of our determination, which include the classification of the services, the application of the AEMC metering review and Essential Energy's connection policy and negotiated services.

5.1 Metering services

Smart meters are foundational to a more connected, modern, and efficient energy system and one mechanism to ensure that future technologies, services, and innovations are supported. Throughout the 2024–29 regulatory determinations we signalled that the AEMC's final decision on the transitioning of legacy meters may require us to consider different classification and/or price/revenue control settings for the businesses.

The key objective of the AEMC's final decision, released in August 2023, is to target a 100% replacement of distribution network owned accumulation meters with smart meters offered by other parties by 30 June 2030.[83] Our draft decision indicated this would constitute a material change in circumstances, which would justify departure from the classification of legacy meter services in the Framework and approach (F&A). [84]

We had identified concerns that customers whose meters are replaced later in the replacement program would incur inequitably higher prices than those whose meters are replaced earlier. While socialisation of metering costs generally occurs at the retail level, we were concerned that retailer's ability to socialise differs based on a number of settings, so socialisation at the network level would produce more consistent outcomes for customers.

Our draft decisions asked businesses to consider whether reclassification of legacy meter services to standard control services was likely to be more appropriate, as this would result in the socialisation of metering costs across a wider customer group.

Since the publication of our draft decision, we have engaged with the businesses on the most appropriate outcome to ensure customers are not inequitably impacted from rising costs in the transition and prevented from realising the benefits the smart meters provide.

While we looked to maintain consistency of approach to legacy metering services across the 2024–29 businesses, further consideration of the individual circumstances of the businesses identified that a tailored approach would be required to ensure we are providing an outcome that is in the long term interest of consumers.

For Essential Energy, our final position is to accept its revised proposal to reclassify legacy metering services as standard control services.

---

83 AEMC, *Final Report: Review of the regulatory framework for metering services*, August 2023.

84 AER, *Draft Decision Attachment 20 – Metering services – Essential Energy – 2024–29 Distribution revenue proposal, September 2023*.

The reasons for our decision are discussed in detail at attachment 20. Outcomes relating to service classification to support the AEMC's intention are discussed at attachment 13.

5.2 Classification of services

As discussed in section 5.1, the AEMC's final decision on metering resulted in a material change of circumstance to justify a departure from final F&A.[85] Our final decision for Essential Energy is to accept the majority of changes proposed to support the transition of legacy meters under the AEMC's final decision.

In addition, Essential Energy also proposed changes to include new unregulated distribution services, submitting that a material change of circumstance had occurred as a result of the continued growth and path of the energy transition. The NSW businesses all raised concerns that during this transition period they will be required to play an expanded role in providing services in the contestable market.

We have considered the concerns raised, and note that these issues were also extensively consulted on during the development of the F&A. Following consideration of the new services proposed for classification by the businesses in their revised proposal, our final position is to maintain our final F&A decision and not classify the new support services proposed, except for including a clarifying example of the leasing space on electricity infrastructure for EV charging.

Details of our reasoning and the final list of classified services for Essential Energy are set out in attachment 13 to this decision.

5.3 Negotiating framework and criteria

In our draft decision, we approved Essential Energy's proposed distribution negotiating framework for the 2024–29 period.[86] We did not receive any objections or submissions on our draft decision. Our final decision maintains the decision to approve Essential Energy's negotiating framework.

We are also required to decide on the Negotiated distribution service criteria for the distributor. Our final decision is to retain the Negotiated distribution service criteria published for Essential Energy in February 2023 for the 2024–29 period.[87] Details of Negotiated distribution service criteria are set out in attachment 17 of our draft decision.[88]

---

85 AER, *Final framework and approach for Ausgrid, Endeavour Energy and Essential Energy for the 2024–29 regulatory control period*, July 2022.

86 AER, *Attachment 17 - Negotiated services framework and criteria | Draft decision - Essential Energy distribution determination 2024–29*, September 2023.

87 AER, *Proposed Negotiated Distribution Service Criteria 2024–29 for Essential Energy*, February 2023.

88 AER, *Attachment 17 - Negotiated services framework and criteria | Draft decision - Essential Energy distribution determination 2024–29*, September 2023, pp. 4-6.

5.4 Connection policy

As detailed in our draft decision, we sought amendment to Essential Energy's connection policy to make it compliant with the NER and our connection charge guidelines. We also requested more clarity on Essential Energy's approach to interconnection network and regulated SAPS.[89]

Essential Energy is the first industry participant to signal its intention to introduce SAPS penetration within its customer base. Following its revised proposal, we liaised with Essential Energy on the further engagement it has undertaken with its customers, including an in-depth survey undertaken by Woolcott Research. During this survey, customers were informed of the appropriate threshold at which they would need to contribute, if the size of a regulated SAPS needed to be increased after installation.[90]

Our final decision is to approve the connection policy for 2024–29 as it complies with the NER. We observed that Essential Energy's approach in implementing SAPS will create two classes of customers (SAPS and network customers). Consequently, a customer on a SAPS wanting to augment the network to increase capacity may pay more than if they were connected to the network.

Currently, under the NER SAPS principle, there is no requirement that customers on a SAPS should be no worse off economically than grid connected customers. Therefore, our final decision has requested Essential Energy to inform customers about the potential costs of augmentation when engaging with them about transitioning to SAPS. We will consider this issue further when we review Essential Energy's connection agreements[91] with customers. This assessment will require us to determine whether the terms and conditions of the SAPS connection are fair and reasonable.

Attachment 18 of this final decision further explain our considerations on Essential Energy's connection policy.

89 AEMC, *Updating the regulatory frameworks for distributor led stand-alone power systems, Final report*, 28 May 2020, p. 90.

90 Essential Energy, *Revised Proposal – 2024–29 Revised Regulatory Proposal*, November 2023. p. 44.

91 Model standing offer for connection services.

6 Constituent decisions

Our final decision on Essential Energy's distribution determination for the 2024–29 regulatory control period includes the following constituent components:

Constituent component
In accordance with clause 6.12.1(1) of the NER, the AER's final decision is that the classification of services set out in Attachment 13 will apply to Essential Energy for the 2024–29 regulatory control period, for the reasons set out in that attachment.
In accordance with clause 6.12.1(2)(i) of the NER, the AER's final decision is to not approve the annual revenue requirement set out in Essential Energy's building block proposal. Our final decision on Essential Energy's annual revenue requirement for standard control services other than metering services (main standard control services) for each year of the 2024–29 regulatory control period is set out in Attachment 1. Our final decision on Essential Energy's metering annual revenue requirement for each year of the 2024–29 regulatory control period is set out in Attachment 20.
In accordance with clause 6.12.1(2)(ii) of the NER, the AER's final decision is to approve Essential Energy's proposal that the regulatory control period will commence on 1 July 2024. Also in accordance with clause 6.12.1(2)(ii) of the NER, the AER's final decision is to approve Essential Energy's proposal that the length of the regulatory control period will be five years from 1 July 2024 to 30 June 2029.
The AER did not receive a request for an asset exemption under clause 6.4B.1(a)(1) and therefore has not made a decision in accordance with clause 6.12.1(2A) of the NER.
In accordance with clause 6.12.1(3)(i) and acting in accordance with clause 6.5.7(c) of the NER, the AER's final decision is to accept Essential Energy's proposed total net capital expenditure forecast. For main standard control services, this amount is $2,655.4 million ($2023–24). The is set out in section 2.4 of this overview. For metering, this amount is $15.9 million ($2023–24). This is set out in Attachment 20.
In accordance with clause 6.12.1(4)(i) and acting in accordance with clause 6.5.6(c) of the NER, the AER's final decision is to not accept Essential Energy's revised proposed total forecast operating expenditure. For main standard control services, we accept Essential Energy's proposed total forecast operating expenditure, inclusive of debt raising costs and exclusive of DMIAM, of $2,323.0 million ($2023–24). The reasons for our final decision are set out in section 2.5 of this overview. For metering, we do not approve Essential Energy's proposed total forecast operating expenditure forecast of $154.86 million ($2023–24) and replace it with a forecast of $154.95 million ($2023–24), reflecting latest labour cost escalation and inflation forecasts. This is set out in Attachment 20.
In accordance with clause 6.12.1(4A) of the NER, the AER's final decision is that the proposed Bushfire Risk Reclassification project is a contingent project for the purpose of this revenue determination. For the purposes of assessing the Bushfire Risk Reclassification project as a contingent project in this final decision, the AER determines capital expenditure of between $70-80 million reasonably reflects the capex criteria. The AER determines that the trigger events for the

Constituent component

Bushfire Risk Reclassification contingent project are appropriate. Our decision, including the accepted trigger events, are set out in Attachment A of this final decision.

In accordance with clause 6.12.1(5) of the NER and the 2022 Rate of Return Instrument, the AER's final decision is that the allowed rate of return for the 2024–25 regulatory year is 5.92% (nominal vanilla) for the reasons set out in section 2.2 in the overview. The rate of return for the remaining regulatory years of the 2024–29 period will be updated annually because our decision is to apply a trailing average portfolio approach to estimating debt which incorporates annual updating of the allowed return on debt.

In accordance with clause 6.12.1(5A) of the NER and the 2022 Rate of Return Instrument, the AER's final decision on the value of imputation credits as referred to in clause 6.5.3 is to adopt a value of 0.57. The reasons for our final decision are set out in section 2.2 in the overview.

In accordance with clause 6.12.1(6) of the NER, and acting in accordance with clause 6.5.1 and schedule 6.2 of the NER, the AER's final decision on Essential Energy's main standard control services regulatory asset base as at 1 July 2024 is $10,332.3 million ($ nominal). The reasons for our final decision are set out in Attachment 2.

The AER's final decision on Essential Energy's metering regulatory asset base as at 1 July 2024 is $80.3 million ($ nominal). This is discussed in Attachment 20.

In accordance with clause 6.12.1(7) of the NER, the AER's final decision on Essential Energy's estimated cost of corporate income tax for main standard control services is $50.5 million ($ nominal) for the 2024–29 regulatory control period. The reasons for our final decision are set out in Attachment 7 and the amount for each regulatory year of the 2024–29 regulatory control period is set out in the table below.

($ million, nominal)	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Tax payable	6.3	14.3	26.8	33.9	36.1	117.4
Less: value of imputation credits	3.6	8.2	15.3	19.3	20.6	66.9
Net cost of corporate income tax	**2.7**	**6.2**	**11.5**	**14.6**	**15.5**	**50.5**

The AER's final decision on Essential Energy's cost of corporate income tax for metering is $8.2 million ($ nominal) for the 2024–29 regulatory control period.

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 Essential Energy.

For main standard control services, our final decision substitutes alternative depreciation schedules set out in Attachment 20, which we determine accord with clause 6.5.5(b). The regulatory depreciation amount approved in this final decision is $675.7 million ($ nominal) for the 2024–29 regulatory control period. The reasons for our final decision are set out in Attachment 4.

For metering, our final decision substitutes alternative schedules amounting to regulatory depreciation for the 2024–29 period of $95.3 million ($ nominal). This is discussed in Attachment 20.

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), export services incentive scheme (ESIS), service target performance incentive scheme (STPIS), demand management incentive scheme (DMIS), demand management innovation allowance mechanism (DMIAM) or small-scale incentive scheme customer service incentive scheme (CSIS) is to apply to Essential Energy:

Constituent component
• We will apply version 2 of the EBSS to Essential Energy in the 2024–29 regulatory control period. Our reasons are set out in section 3.2. • We will apply the CESS as set out in the Capital Expenditure Incentives Guideline to Essential Energy in the 2024–29 regulatory control period. Our reasons are set out in section 3.1. • We will not apply the ESIS for the 2024–29 regulatory control period as set out in the Overview of our draft decision. • We will apply the STPIS version 2 to Essential Energy for the 2024–29 regulatory control period for the reasons set out in section 3.3. • We will apply the DMIS and DMIAM to Essential Energy for the 2024–29 regulatory control period for the reasons set out in section 3.4. • We will apply the CSIS to Essential Energy for the 2024–29 regulatory control period for the reasons set out in section 3.5.
In accordance with clause 6.12.1(10) of the NER, the AER's final decision is that all other appropriate amounts, values and inputs are as set out in this draft determination including attachments.
In accordance with clause 6.12.1(11) of the NER and our framework and approach paper, the AER's final decision on the form of control mechanisms (including the X factor) for standard control services is a revenue cap. The revenue cap for Essential Energy for any given regulatory year is the total annual revenue calculated using the formula in Attachment 14, which includes any adjustment required to move the Distribution Use of Service (DUoS) unders and overs account to zero. The reasons for our final decision are set out in Attachment 14.
In accordance with clause 6.12.1(12) of the NER and our framework and approach paper, the AER's final decision on the form of the control mechanism for alternative control services is to apply price caps for all alternative control services. The reasons for our final decision are set out in Attachment 14 and Attachment 16.
In accordance with clause 6.12.1(13) of the NER, to demonstrate compliance with its distribution determination, the AER's final decision is that Essential Energy must maintain both DUoS and metering unders and overs mechanisms. It must provide information on these mechanisms to us in its annual pricing proposal. The reasons for our final decision are set out in Attachment 14.
In accordance with clause 6.12.1(14) of the NER the AER's final decision is to apply the following nominated pass through events to Essential Energy for the 2024–29 regulatory control period in accordance with clause 6.5.10: • Insurance coverage event • Insurer's credit risk event • Terrorism event • Natural disaster event

Constituent component
These events have the definitions set out in Attachment 15 of the draft decision. Our reasons for this constituent decision are also set out in that attachment.[92]
In accordance with clause 6.12.1(14A) of the NER, the AER's final decision is to approve the tariff structure statement proposed by Essential Energy with one amendment. The reasons for our final decision are set out Attachment 19 of our final decision.
In accordance with clause 6.12.1(15) of the NER, the AER's final decision is that the negotiating framework as proposed by Essential Energy will apply for the 2024–29 regulatory control period. The reasons for our final decision are set out in section 5.3 of overview and Attachment 17 of our draft decision.
In accordance with clause 6.12.1(16) of the NER, the AER's final decision is to apply the Negotiated distribution services criteria published in February 2023 to Essential Energy. The reasons for our final decision are set out in section 5.3 of overview and Attachment 17 of our draft decision.
In accordance with clause 6.12.1(17) of the NER, the AER's final decision on the procedures for assigning retail customers to tariff classes for Essential Energy is set out in Attachment 19 of the draft decision.
In accordance with clause 6.12.1(18) of the NER, the AER's final decision is that the depreciation approach to be used to establish the RAB at the commencement of Essential Energy's regulatory control period as at 1 July 2029 is to be based on forecast capex. The reasons for our final decision are set out in Attachment 2.
In accordance with clause 6.12.1(19) of the NER, the AER's final decision on how Essential Energy is to report to the AER on its recovery of designated pricing proposal charges, and how it must account for the under and over recovery of designated pricing proposal charges, is that it must use the unders and overs mechanism described in attachment 14. It must provide information on this mechanism to us in its annual pricing proposal. The reasons for our final decision are set out in Attachment 14.
In accordance with clause 6.12.1(20) of the NER, the AER's final decision on how Essential Energy is to report to the AER on its recovery of jurisdictional scheme amounts, and how it must account for the under and over recovery of jurisdictional scheme amounts, is that it must use the unders and overs mechanism described in Attachment 14. It must provide information on this mechanism to us in its annual pricing proposal. The reasons for our final decision are set out in Attachment 14.
In accordance with clause 6.12.1(21) of the NER, the AER's final decision is to approve the connection policy proposed by Essential Energy as set out in section 5.4 and Attachment 18.

[92] Essential Energy included a new nominated pass through event in its revised proposal for a Bushfire Risk Reclassification project. The event was to address the potential costs related to a reclassification of bushfire risk areas reflecting Essential Energy's application of updated bushfire simulation modelling. However, Essential Energy subsequently instead proposed a contingent project. Our final decision on this matter is set out in Attachment A.

7 List of submissions

We received 10 submissions in response to Essential Energy's revised revenue proposal and our draft decision. These are listed below.[93]

Submissions from
ACEnergy
Consumer Challenge Panel, sub-panel 26
Evie Networks
Independent Pricing and Regulatory Tribunal (IPART)
Origin Energy
Public Interest Advocacy Centre (PIAC)
Red and Lumo Energy
Stakeholder submission
Southern Lights
Tesla

93 Submissions are available on the AER website at: https://www.aer.gov.au/industry/registers/determinations/essential-energy-determination-2024-29/consultation-submissions-draft-decision-and-revised-proposal.

Shortened forms

Terms	Definition
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
ARR	annual revenue requirement
capex	capital expenditure
CCP26	Consumer Challenge Panel, sub-panel 26
CESS	capital expenditure sharing scheme
CER	consumer energy resources
CPI	consumer price index
CSIS	customer service incentive scheme
DMIAM	demand management innovation allowance mechanism
DMIS	demand management incentive scheme
DNSP or distributor	Distribution Network Service Provider
DUoS	Distribution Use of System Charges
EBSS	efficiency benefit sharing scheme
F&A	framework and approach
(the) Handbook	Better Resets Handbook
ICT	information and communication technologies
NEL	National Electricity Law
NEO	National Electricity Objectives
NER	National Electricity Rules
opex	operating expenditure
PIAC	Public Interest Advocacy Centre
PTRM	post-tax revenue model
RAB	regulated asset base
RBA	Reserve Bank of Australia
repex	replacement capital expenditure
SAPS	stand-alone power systems
SAIDI	System Average Interruption Duration Index
SAIFI	System Average Interruption Frequency Index
SCC	Stakeholder Collaboration Collective
SMP	Statement on Monetary Policy
STPIS	service target performance incentive scheme
WACC	weighted average cost of capital
WPI	wage price index
VCR	value of customer reliability