Final Decision

TasNetworks
Electricity Transmission
Determination 2024 to 2029
(1 July 2024 to 30 June 2029)

Attachment 1
Maximum allowed revenue

April 2024

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List of attachments

This attachment forms part of the AER's final decision on the transmission determination that will apply to TasNetworks 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. The final decision attachments have been numbered consistently with the equivalent attachments to our draft decision. In these circumstances, our draft decision reasons form part of this final decision.

The final decision includes the following documents:

Overview

Attachment 1 – Maximum allowed revenue

Attachment 2 – Regulatory asset base

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 7 – Corporate income tax

Contents

1 Maximum allowed revenue

This attachment sets out our final decision on TasNetworks' maximum allowed revenue (MAR) for the provision of prescribed transmission services over the 2024–29 regulatory control period (period). Specifically, it sets out our final decision on:[1]

- the estimated total revenue cap, which is the sum of the annual expected MAR
- the annual building block revenue requirement
- the annual expected MAR
- the X factors.

We determine TasNetworks' annual building block revenue requirement using a building block approach. We determine the X factors by smoothing the annual building block revenue requirement over the 2024–29 period. The X factors are used in the CPI–X methodology to determine the annual expected MAR.

1.1 Final decision

We determine a total annual building block revenue requirement of $885.3 million ($ nominal, unsmoothed) for TasNetworks for the 2024–29 period. Our determination represents an increase of $13.8 million (1.6%) to TasNetworks' revised proposal. The increase is largely driven by the higher regulatory depreciation building block, which is $11.5 million higher than TasNetworks' revised proposal. The regulatory depreciation amount is the net total of the straight-line depreciation, less the inflation indexation of the regulatory asset base (RAB). Our final decision straight-line depreciation and indexation component are both lower than the revised proposal by $1.8 million and $13.2 million respectively. The lower indexation has more than offset the reduction in straight-line depreciation due to a lower expected inflation rate applied in our final decision compared to the revised proposal. This results in a net impact of a higher regulatory depreciation amount compared to the revised proposal. See Attachment 4 for further details.

We determine the annual expected MAR (smoothed) and X factor for each regulatory year of the 2024–29 period by smoothing the annual building block revenue requirement. For the 2024–29 period, our final decision is to approve an estimated total revenue cap of $886.6 million ($ nominal) for TasNetworks. Our approved X factor commencing in 2025–26 is –1.40% per annum for each regulatory year of the 2024–29 period.[2]

Table 1.1 sets out our final decision on TasNetworks' annual building block revenue requirement, the X factor, the annual expected MAR and the estimated total revenue cap for the 2024–29 period.

1 NER, cll. 6A.4.2(a)(1)–(3), 6A.5.3(c) and 6A.6.8.

2 TasNetworks is not required to apply an X factor for 2024–25 because we set the 2024–25 MAR in this decision.

Table 1.1 AER's final decision on TasNetworks' annual building block revenue requirement, annual expected MAR, estimated total revenue cap and X factor ($million, nominal)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Return on capital	97.4	100.8	104.2	107.4	111.4	521.2
Regulatory depreciation[a]	25.2	23.1	26.3	22.9	22.8	120.4
Operating expenditure[b]	40.9	43.8	46.0	47.4	48.7	226.7
Revenue adjustments[c]	2.0	–3.2	–0.2	0.9	0.6	0.1
Cost of corporate income tax	4.1	2.7	3.0	3.2	3.9	16.9
Annual building block revenue requirement (unsmoothed)	169.6	167.2	179.3	181.8	187.4	885.3
Annual expected MAR (smoothed)	**163.4**	**170.1**	**177.0**	**184.3**	**191.8**	**886.6**
X factor[e]	n/a[f]	–1.40%	–1.40%	–1.40%	–1.40%	n/a

Source: AER analysis.

(a) Regulatory depreciation is straight-line depreciation net of the inflation indexation on the opening regulatory asset base (RAB).

(b) Includes debt raising costs

(c) Includes revenue adjustments from the efficiency benefit sharing scheme (EBSS), the capital expenditure sharing scheme (CESS) and the demand management innovation allowance mechanism (DMIAM).

(d) The estimated total revenue cap is equal to the total annual expected MAR.

(e) The X factors will be revised to reflect the annual return on debt update. Under the CPI–X framework, the X factor measures the real rate of change in annual expected revenue from one year to the next. A negative X factor represents a real increase in revenue. Conversely, a positive X factor represents a real decrease in revenue.

(f) TasNetworks is not required to apply an X factor for 2024–25 because we set the 2024–25 expected revenue in this decision. The MAR for 2024–25 is around 1.4% higher than the approved MAR for 2023–24 in real terms, or 4.1% higher in nominal terms.

1.2 TasNetworks' revised proposal

TasNetworks revised proposal included a total (smoothed) revenue cap of $870.9 million ($ nominal) for the 2024–29 period. Table 1.2 sets out TasNetworks' revised proposed annual building block revenue requirement, the X factor, the annual expected MAR, and the estimated total revenue cap.

Table 1.2 TasNetworks' revised proposed annual building block revenue requirement, annual expected MAR, estimated total revenue cap and X factor ($million, nominal)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Return on capital	96.4	100.5	104.5	108.4	113.2	523.0
Regulatory depreciation[a]	23.0	20.8	24.0	20.6	20.5	108.9
Operating expenditure[b]	40.9	43.9	46.2	47.6	49.0	227.7
Revenue adjustments[c]	2.1	–3.2	–0.2	0.9	–1.6	–2.2
Cost of corporate income tax	3.5	2.1	2.5	2.7	3.3	14.1
Annual building block revenue requirement (unsmoothed)	165.9	164.1	177.0	180.2	184.4	871.5
Annual expected MAR (smoothed)	**165.9**	**169.9**	**174.1**	**178.3**	**182.7**	**870.9**[d]
X factor[e]	n/a[f]	0.34%	0.34%	0.34%	0.34%	n/a

Source: TasNetworks, *TasNetworks-Revised Proposal-Transmission-PTRM-Nov 2023-Public*, November 2023.
(a) Regulatory depreciation is straight-line depreciation net of the inflation indexation on the opening RAB.
(b) Includes debt raising costs.
(c) Includes revenue adjustments from the EBSS, CESS and DMIAM.
(d) The estimated total revenue cap is equal to the total annual expected MAR.
(e) The X factors will be revised to reflect the annual return on debt update. Under the CPI–X framework, the X factor measures the real rate of change in annual expected smoothed revenue from one year to the next. A negative X factor represents a real increase in revenue. Conversely, a positive X factor represents a real decrease in revenue.
(f) TasNetworks is not required to apply an X factor for 2024–25 because we set the 2024–25 MAR in this decision.

1.3 Assessment approach

We did not change the building block approach we use to determine the expected revenue from our draft decision. Attachment 1 (section 1.3) of our draft decision details that approach.[3]

1.3.1 Annual revenue adjustment process

We use an expected inflation rate in our post-tax revenue model (PTRM) to calculate the expected MAR (as shown in Table 1.1). The calculation of the actual MAR will therefore require an adjustment for actual inflation. To this end, the actual MAR from the second year onwards is adjusted for actual inflation. As discussed in the Rate of return instrument, the MAR is also subject to adjustment to reflect our update of TasNetworks' return on debt annually.[4] This means the actual MAR from the second year onwards will also be adjusted

3 AER, *Draft decision, Attachment 01 – Maximum allowed revenue requirement – TasNetworks – 2024 Transmission revenue proposal*, September 2023, pp. 3–6.

4 AER, *Rate of return instrument*, February 2023, cl. 24, Note 29.

for revised X factors after the annual return on debt update. This annual revenue adjustment process is set out below.

To enable the formula for the annual revenue adjustment process to operate correctly, we will refer to the expected MAR determined in this decision using the building block costs as the allowed revenue (AR). This is because the expected MAR determined using the building block costs does not incorporate performance incentive scheme revenue adjustments and pass through amounts that may apply to each regulatory year.

We determine the 2024–25 AR of $163.4 million for TasNetworks. TasNetworks then applies an annual adjustment to determine its AR for each subsequent year of the 2024–29 period, based on the previous year's AR and using the CPI–X methodology.[5] That is, the subsequent year's allowed revenue is determined by adjusting the previous year's AR for actual inflation and the X factor determined after the annual return on debt update:

$$AR_t = AR_{t-1} \times (1 + \Delta CPI) \times (1 - X_t)$$

where:

AR = the allowed revenue

t = time period/financial year (for t = 2 (2025–26), 3 (2026–27), 4 (2027–28), 5 (2028–29))

ΔCPI = the annual percentage change in the ABS Consumer price index all groups, weighted average of eight capital cities from December in year t – 2 to December in year t – 1

X = the smoothing factor determined in accordance with the PTRM as approved in the AER's final decision, and annually revised for the return on debt update in accordance with the formula specified in the Rate of return instrument calculated for the relevant year.[6]

The MAR used for transmission pricing is determined annually as part of the annual revenue adjustment process in accordance with the National Electricity Rules (NER). The MAR is determined each year by adding to (or deducting from) the allowed revenue:

- the service target performance incentive scheme revenue increment (or revenue decrement)[7]
- any approved pass through amounts.[8]

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5 In the case of making the annual adjustment for year 2, the previous year's AR would be the same as the approved expected MAR for year 1 as contained in the PTRM.

6 AER, *Rate of return instrument*, February 2023, cl. 9.

7 NER, cl. 6A.7.4.

8 NER, cll. 6A.7.2 and 6A.7.3.

The annual MAR is established according to the following formula:

$$MAR_t = \text{(allowed revenue)} + \text{(performance incentive)} + \text{(pass through)}$$

$$= AR_t + ((AR_{t-2} \times ½) + (AR_{t-1} \times ½)) \times S_{ct} + P_t$$

where:

MAR = the maximum allowed revenue

AR = the allowed revenue

S = the percentage revenue increment or decrement determined in accordance with the service target performance incentive scheme

P = the pass through amount (positive or negative) that the AER has determined in accordance with clauses 6A.7.2 and 6A.7.3 of the NER

t = time period/financial year (for *t* = 2 (2025–26), 3 (2026–27), 4 (2027–28), 5 (2028–29))

ct = time period/calendar year (for *t* = 2 (2024), 3 (2025), 4 (2026), 5 (2027)).

TasNetworks may also adjust the MAR for under or over-recovery amounts.[9] That is, if the revenue amounts earned from providing prescribed transmission services in previous regulatory years are higher or lower than the sum of the approved MAR for those years, the difference can be included in the subsequent year's MAR. In the case of an under-recovery, the amount is added to the subsequent year's MAR. In the case of an over-recovery, the amount is subtracted from the subsequent year's MAR.

Table 1.4 sets out the timing of the annual calculation of the AR and performance incentive.

Table 1.3 Timing of the calculation of allowed revenues and the performance incentive for TasNetworks

t	Allowed revenue (financial year)	*ct*	Performance incentive (calendar year)
2	1 July 2025 – 30 June 2026	2	1 January 2024 – 31 December 2024
3	1 July 2026 – 30 June 2027	3	1 January 2025 – 31 December 2025
4	1 July 2027 – 30 June 2028	4	1 January 2026 – 31 December 2026
5	1 July 2028 – 30 June 2029	5	1 January 2027 – 31 December 2027

Note: The performance incentive for the period 1 January 2023 to 31 December 2023 is to be applied to the AR determined for 2024–25 (AR_1).

9 NER, cl. 6A.23.3(e)(5).

1.4 Reasons for final decision

For this final decision, we determine a total annual building block revenue requirement of $885.3 million ($ nominal, unsmoothed) for TasNetworks for the 2024–29 period. This is an increase of $13.8 million (1.6%) to TasNetworks' revised proposed total annual building block revenue requirement of $871.5 million for this period. This increase reflects the impact of our final decision on the various building block costs.

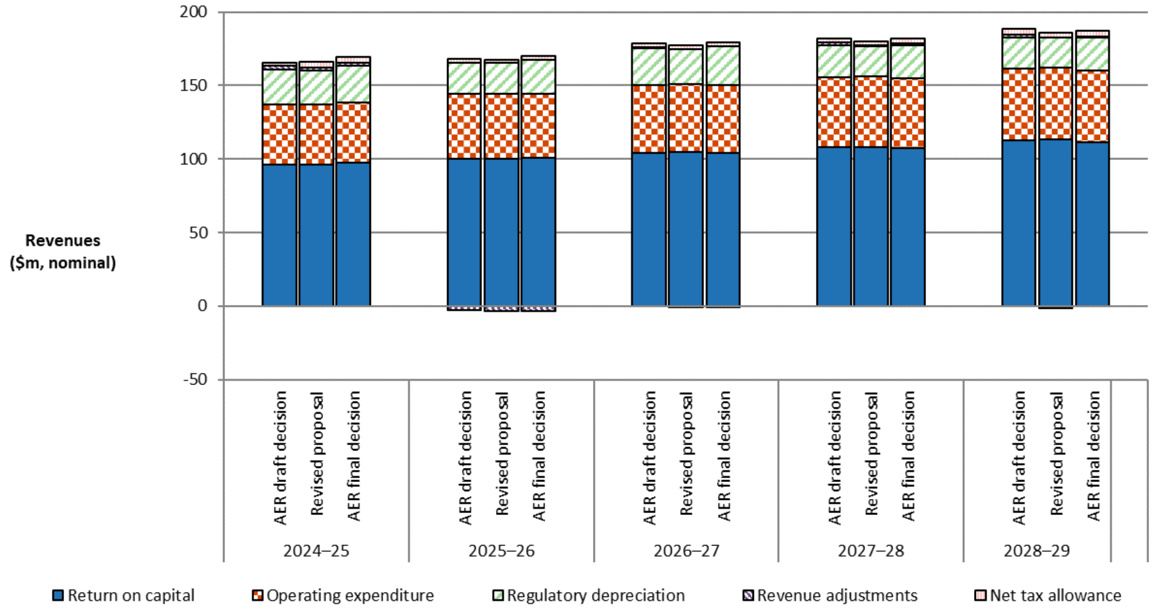
Figure 1.1 shows the building block components in this final determination that comprise the annual building block revenue requirement for TasNetworks, and the corresponding components from its revised proposal and our draft decision. The changes we made to TasNetworks' revised proposal building blocks are (in nominal terms):

- an increase in the regulatory depreciation of $11.5 million (10.5%) (Attachment 4). This is driven largely by a lower expected inflation rate for the 2024–29 period, which reduces the indexation adjustment to regulatory depreciation.[10] This has more than offset the reduction we made to the straight-line depreciation amount
- an increase in the cost of corporate income tax of $2.9 million (20.5%) (Attachment 7). This is largely driven by the higher regulatory depreciation[11]
- an increase in the revenue adjustments of $2.3 million (section 2.7 of the Overview). This is largely due to the higher revenue adjustment from lower EBSS penalties (section 3.2.2 of the Overview) in this final decision compared to TasNetworks' revised proposal
- a reduction in the return on capital of $1.8 million (0.3%) (sections 2.1, 2.2 and Attachment 5). This is largely driven by our final decision establishing a lower opening RAB as at 1 July 2024
- a reduction in the operating expenditure (opex) forecast of $1.0 million (0.4%) (section 2.5 of the Overview). This is because our final decision applied a lower expected inflation rate compared to the revised proposal when converting the approved opex in real 2023–24 dollar terms to nominal terms.

[10] Regulatory depreciation is straight-line depreciation net of the inflation indexation on the opening RAB. A lower indexation amount increases the regulatory depreciation, all else being equal.

[11] All else being equal, a higher regulatory depreciation increases the cost of corporate income tax as it is a component of revenue for tax purposes.

Figure 1.1 AER's draft and final decisions, and TasNetworks' revised proposed annual building block revenue requirement ($million, nominal)



Source: AER analysis; TasNetworks, *TasNetworks-Revised Proposal-Transmission-PTRM-Nov 2023-Public*, November 2023.

Note: Revenue adjustments include EBSS, CESS and DMIAM amounts. Opex includes debt raising costs.

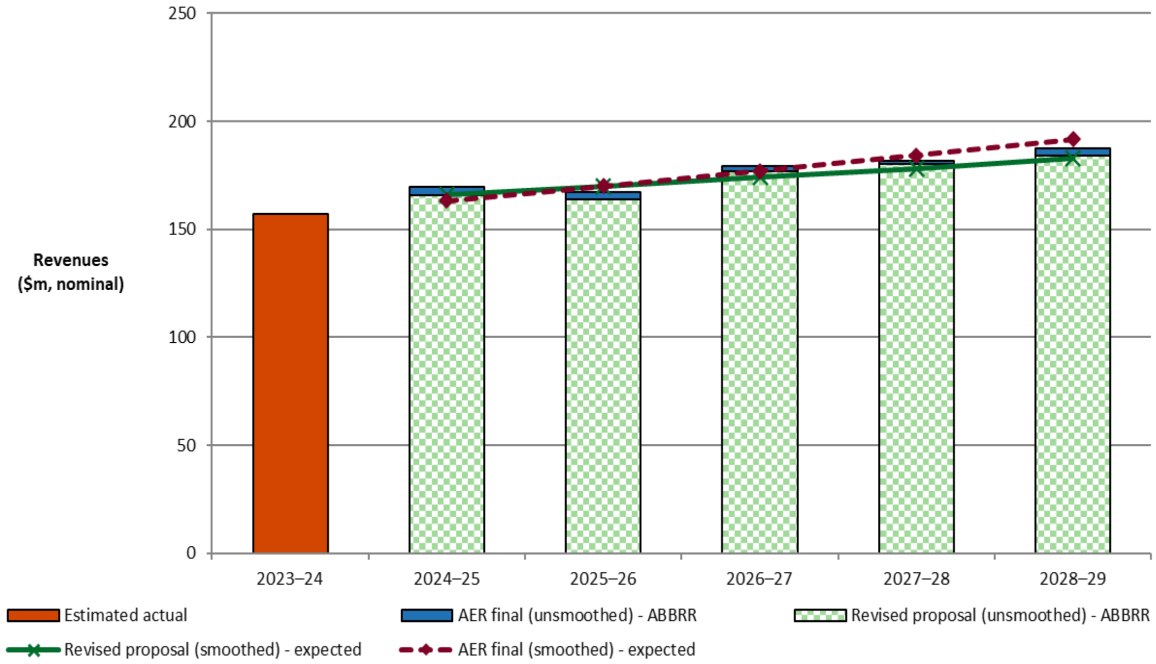
1.4.1 X factor, annual expected MAR and estimated total revenue cap

For this final decision, we determine an X factor for TasNetworks of –1.40% per annum for the four years of the regulatory control period from 2025–26 to 2028–29.[12] The net present value (NPV) of the annual building block revenue requirement is $744.8 million ($2023–24) as at 1 July 2024. Based on this NPV and applying the CPI–X method, we determine that the annual expected MAR (smoothed) for TasNetworks is $163.4 million in 2024–25 increasing to $191.8 million in 2028–29 ($ nominal). The resulting estimated total revenue cap for TasNetworks is $886.6 million for the 2024–29 period.

Figure 1.2 shows our final decision on TasNetworks' annual expected MAR (smoothed revenue) and the annual building block revenue requirement (unsmoothed revenue) for the 2024–29 period.

12 TasNetworks is not required to apply an X factor for 2024–25 because we set the 2024–25 MAR in this decision.

Figure 1.2 AER's final decision on TasNetworks' revenue for the 2024–29 period ($million, nominal)



Source: AER analysis.
Note: Annual building block revenue requirement (ABBRR).

To determine the expected MAR for TasNetworks, we have set the MAR for the first regulatory year at $163.4 million ($ nominal), which is $6.2 million lower than the annual building block revenue requirement. We then apply an expected inflation rate of 2.66% per annum and an X factor of –1.40% per annum to determine the expected MAR in subsequent years.[13] We consider that our profile of X factors results in an expected MAR in the last year of the regulatory control period that is as close as reasonably possible to the annual building block revenue requirement for that year.[14] We received one submission from Tasmanian Small Business Council supporting a revenue smoothing approach that avoids a large jump in revenue in the first year of the 2024–29 period, even though this comes at the expense of higher revenue (and prices) in the subsequent years.[15] Our final decision has taken account of this submission and provides for a revenue smoothing profile that spreads the revenue increases evenly over five years of the period.

Our final decision results in an average increase of 4.1% per annum ($ nominal) in the expected MAR over the 2024–29 period.[16] This consists of an initial increase of 4.1% from

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13 NER, cl. 6A.5.3(c)(3).

14 NER, cl. 6A.6.8(c)(2). We consider a divergence of up to 3% between the expected MAR and annual building block revenue requirement for the last year of the regulatory control period is appropriate, if this can promote smoother price changes for users over the regulatory control period. In the present circumstances, based on the X factors we have determined for TasNetworks, this divergence is around 2.4%.

15 Tasmanian Small Business Council, *Submission AER Draft Determination TasNetworks Combined Regulatory Proposal 2024-29*, p. 17.

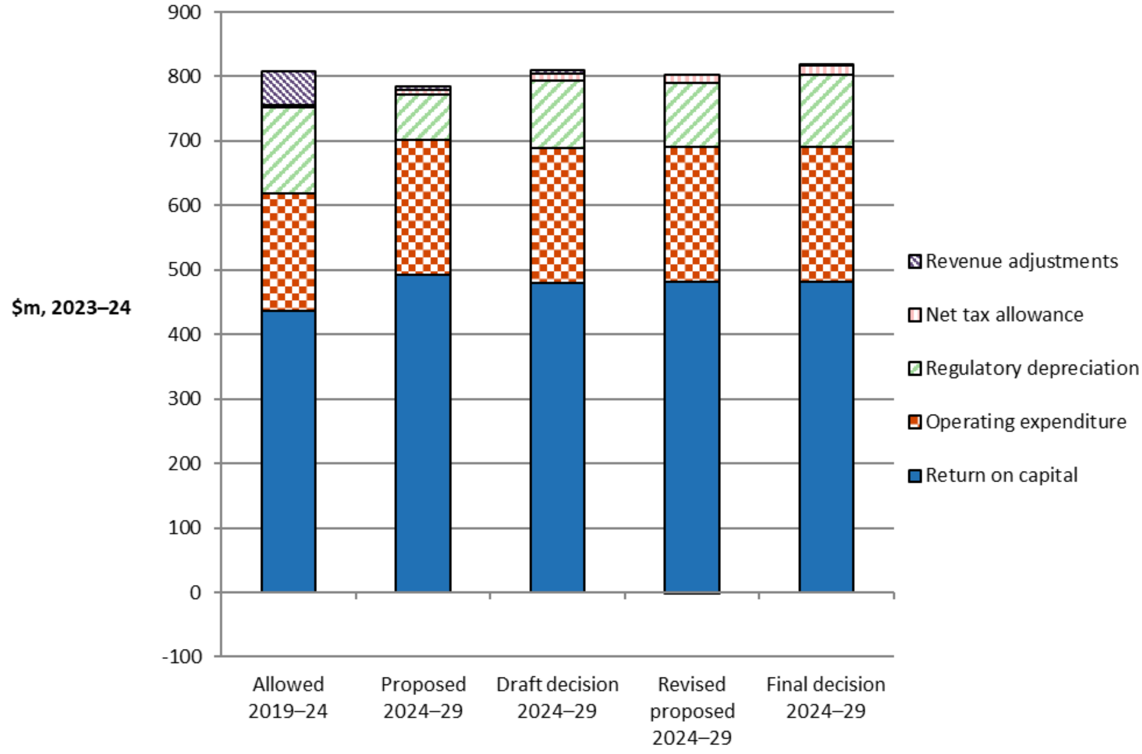
16 In real 2023–24 dollar terms, our approved expected MAR for TasNetworks results in an average increase of 1.4% per annum over the 2024–29 period.

2023–24 to 2024–25, followed by the same level of annual increase during the remainder of the 2024–29 period.[17]

Our final decision also results in an increase of 1.3% in real terms ($2023–24) to TasNetworks' total annual unsmoothed revenue relative to that allowed in the 2019–24 period. This is primarily because we have determined a higher rate of return (and therefore higher return on capital) and opex in this final decision for the 2024–29 period than that approved in the 2019–24 determination.

Figure 1.3 compares our final and draft decision building blocks for TasNetworks' 2024–29 period with its proposal and revised proposal for the same period, and the approved unsmoothed revenue for the 2019–24 period.

Figure 1.3 Total revenue by building block components ($million, 2023–24)



Source: AER analysis.

1.4.2 Shared assets

Our final decision is not to apply a shared assets revenue adjustment to TasNetworks' total expected MAR for the 2024–29 period.

In our draft decision, we did not apply a shared asset revenue adjustment to TasNetworks' revenues because we estimated that the unregulated revenues were less than 1% of its MAR in each year of the 2024–29 period. Therefore, the materiality threshold was not met in any year of the 2024–29 period.[18] Using the same assessment approach as the draft decision, we consider that this materiality threshold is also not met in any year of the 2024–

17 In real 2023–24 dollar terms, this is an initial increase of 1.4% from 2023–24 to 2024–25, followed by the same level of annual increase for the remainder of the 2024–29 period.

18 AER, *Draft decision, Attachment 01 – Maximum allowed revenue requirement – TasNetworks – 2024 Transmission revenue proposal*, September 2023, pp. 12–13.

29 period for this final decision, and therefore we do not apply a shared asset revenue adjustment.

1.4.3 Indicative average transmission charges

TasNetworks is the transmission network service provider for Tasmania. Therefore, our final decision on TasNetworks' expected MAR will ultimately affect the annual electricity bills paid by customers in Tasmania. There are several steps required to translate our revenue decision into indicative transmission charges. Since we regulate TasNetworks' prescribed transmission services under a revenue cap, changes in the consumption of electricity will affect the transmission charges ultimately paid by customers. We estimate the indicative effect of our final decision on forecast average transmission charges in Tasmania by:

- taking TasNetworks' annual expected MAR determined in this final decision, and
- dividing it by the forecast annual energy delivered in Tasmania published by the Australian Energy Market Operator (AEMO).[19]

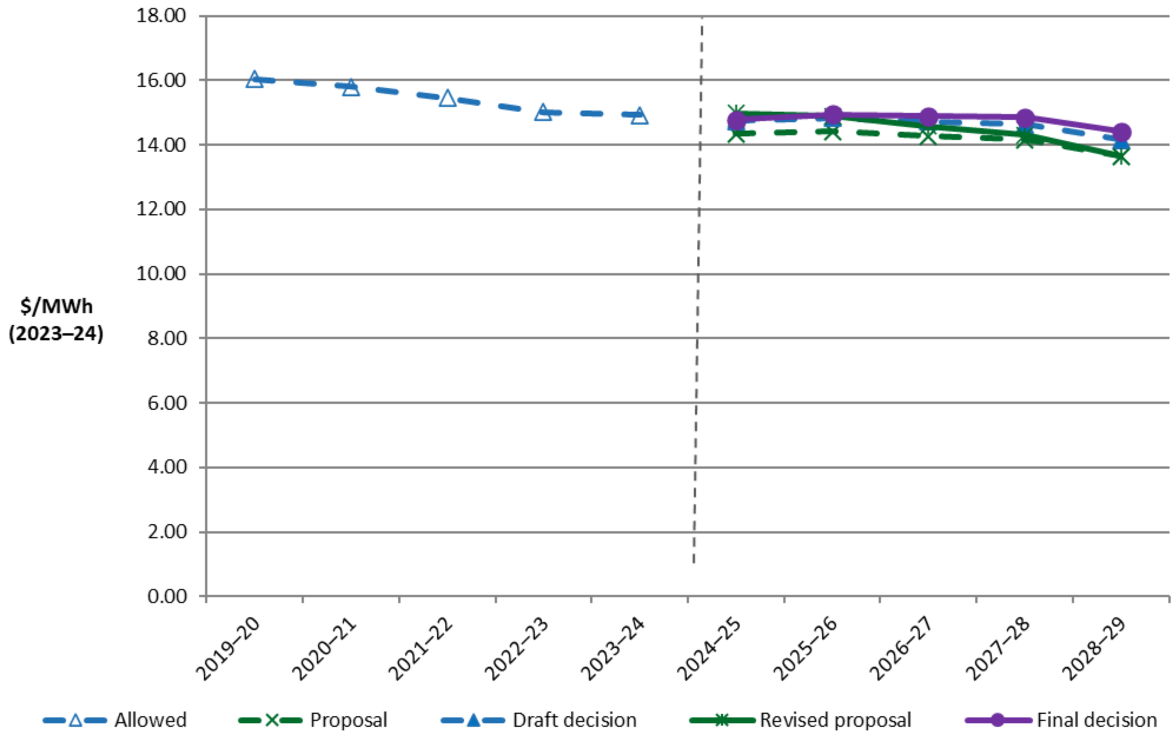
Based on our approach, we estimate that this final decision will result in a slight reduction in annual average transmission charges in real 2023–24 dollar terms from 2024–25 to 2028–2029.[20]

Figure 1.4 shows the indicative average transmission charges over the period 2019–24 to 2024–29 in real 2023–24 dollar terms based on the expected revenues established in our final decision compared to TasNetworks’ proposed revenue requirement. The average transmission charges are expected to reduce slightly from around $14.8 per MWh in 2023–24 to $14.4 per MWh in 2028–29.

19 AEMO, *National Electricity and Gas forecasting - 2023 Electricity Statement of Opportunities*, http://forecasting.aemo.com.au/Electricity/AnnualConsumption/Operational, accessed on 12 April 2024.

20 On average, the final decision transmission smoothed revenues will increase by 4.1% ($ nominal) per annum from 2023–24 to 2028–29. The forecast energy delivered in Tasmania will increase by an average of 2.0% per annum across that period. As a result, the indicative transmission charge will increase by 2.1% ($ nominal) per annum from 2023–24 to 2028–29, which is less than the expected inflation rate.

Figure 1.4 Indicative transmission price path for Tasmania ($/MWh, $2023–24)



Source: AER analysis.

Notes: The price path for the transmission network is based on actual and forecast energy throughput amounts for TasNetworks' transmission network across Tasmania.

1.4.4 Expected impact of final decision on electricity bills

The annual electricity bill for customers in Tasmania reflects the combined cost of all the electricity supply chain components—wholesale energy generation, transmission, distribution, metering, and retail costs. This final decision primarily relates to the transmission charges for TasNetworks' prescribed transmission services, which represent approximately 7% on average for residential customers' and 6% on average for small business customers' annual electricity bills in Tasmania.[21]

We estimate the expected bill impact by varying the transmission charges in accordance with our final decision in this attachment, while holding all other component costs that make up the electricity bill constant. This approach isolates the effect of our final decision on the core transmission charges for TasNetworks only. However, this does not imply that other components will remain unchanged across the regulatory control period.[22] Our final decision determines higher revenues than proposed by TasNetworks—largely due to the impact of updated market data on the expected inflation rate. As a result, expected bill increases are higher than TasNetworks' revised proposal, holding all else constant.

[21] Office of the Tasmanian Economic Regulator, *Typical Electricity Customers in Tasmania – 2022,* September 2022.

[22] It also assumes that actual energy consumption will equal the forecast adopted in our final decision. Since TasNetworks operates under a revenue cap, changes in energy consumption will also affect annual electricity bills across the 2024–29 period.

Based on this approach, we expect that our final decision on the transmission component will increase the average annual residential electricity bill in 2028–29 by about $17 ($ nominal) or 0.8% from the 2023–24 total bill level.

Similarly, we expect that our final decision will result in the transmission component of the average annual electricity bill for a small business customer in 2028–29 to increase by about $20 ($ nominal) or 0.7% from the 2023–24 total bill level.

Our estimated bill impact is based on the typical annual electricity usage of 7,428 kWh and 8,782 kWh for residential and small business customers in Tasmania, respectively.[23] Therefore, customers with different usage will experience different changes in their bills. We also note that there are other factors which we have not considered here, such as metering, wholesale and retail costs, which affect electricity bills.

Table 1.5 shows the estimated impact from our final decision and TasNetworks' revised proposal on the average annual electricity bills for residential and small business customers in Tasmania over the 2024–29 period.

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[23] Office of the Tasmanian Economic Regulator, *Typical Electricity Customers in Tasmania – 2022,* September 2022.

Table 1.4 Estimated impact of TasNetworks' revised proposal and AER's final decision on annual electricity bills for the 2024–29 period ($ nominal)

	2023–24	2024–25	2025–26	2026–27	2027–28	2028–29
AER final decision						
Residential annual electricity bill	2,170[a]	2,173	2,179	2,183	2,187	2,186
Annual change[b]	–	4 (0.2%)	6 (0.3%)	3 (0.2%)	4 (0.2%)	–1 (–0%)
Small business annual electricity bill	2,882[a]	2,886	2,893	2897	2,902	2,901
Annual change[b]	–	4 (0.2%)	7 (0.2%)	4 (0.1%)	5 (0.2%)	–1 (–0%)
TasNetworks revised proposal						
Residential annual electricity bill	2,170[a]	2,176	2,179	2,180	2,181	2,178
Annual change[b]	–	6 (0.3%)	3 (0.2%)	1 (0%)	1 (0.1%)	–3 (–0.1%)
Small business annual electricity bill	2,882[a]	2,889	2,893	2,894	2,896	2,892
Annual change[b]	–	7 (0.3%)	4 (0.1%)	1 (0%)	2 (0.1%)	–4 (–0.1%)

Source: AER analysis; TasNetworks, *TasNetworks-(T) Workbook 5 Indicative Bill-Dec-22-Public*, January 2023.

(a) TasNetworks, *TasNetworks-(T) Workbook 5 Indicative Bill-Dec-22-Public*, January 2023. Office of the Tasmanian Economic Regulator, *Typical Electricity Customers in Tasmania – 2022*, September 2022.

(b) Annual change amounts and percentages are indicative. They are derived by varying the transmission component of the 2023–24 bill amounts in proportion to yearly expected revenue divided by TasNetworks' forecast energy. Actual bill impacts will vary depending on electricity consumption and tariff class.

Shortened forms

Term	Definition
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
capex	capital expenditure
CESS	capital expenditure sharing scheme
CPI	consumer price index
DMIAM	demand management innovation allowance mechanism
EBSS	efficiency benefit sharing scheme
MAR	maximum allowed revenue
NER	National Electricity Rules
NPV	net present value
opex	operating expenditure
PTRM	post-tax revenue model
RAB	regulatory asset base