

# Final Decision

## Evoenergy Electricity Distribution Determination 2024 to 2029

(1 July 2024 to 30 June 2029)

### Attachment 8 Efficiency benefit sharing scheme

April 2024

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#### **Amendment record**

<b>Version</b>	<b>Date</b>	<b>Pages</b>
1	30 April 2024	11

## List of attachments

This attachment forms part of the AER's final decision on the distribution determination that will apply to Evoenergy for the 2024–29 period. It should be read with all other parts of the 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 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency benefit sharing scheme

Attachment 13 – Classification of services

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## 8 Efficiency benefit sharing scheme

The efficiency benefit sharing scheme (EBSS) is intended to provide a continuous incentive for service providers to pursue efficiency improvements in operating expenditure (opex) and provide for a fair sharing of the benefits of these efficiencies between network service providers and consumers. Consumers benefit from improved efficiencies through lower regulated prices.

This attachment sets out our final decision and reasons on the EBSS carryover amounts Evoenergy has accrued over the 2019–24 regulatory control period (2019–24 period). It also sets out how we will apply the EBSS over the 2024–29 regulatory control period (2024–29 period).

### 8.1 Final decision

Our final decision is to include EBSS carryover amounts totalling \$14.7 million (\$2023–24) from the application of the EBSS in the 2019–24 period.<sup>1</sup> This is \$1.1 million less than Evoenergy’s revised proposal of \$15.8 million.<sup>2</sup> This difference reflects adjustments we have made to:

- remove forecast and actual expenditure related to the administration costs for the Large Feed-in Tariff Scheme (LFIT)
- update actual and forecast inflation.

We set out our final decision in Table 8.1.

**Table 8.1 Final decision on Evoenergy’s carryover amounts (\$million, 2023–24)**

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Evoenergy’s revised proposal	4.9	2.3	3.2	5.3	–	15.8
AER’s final decision	4.7	2.2	3.0	4.8	–	14.7
<b>Difference</b>	<b>–0.2</b>	<b>–0.2</b>	<b>–0.2</b>	<b>–0.6</b>	<b>–</b>	<b>–1.1</b>

Note: Numbers may not add up due to rounding.

Source: Evoenergy, *EBSS model*, November 2023; AER analysis.

We will continue to apply version 2 of the EBSS to Evoenergy in the 2024–29 period.<sup>3</sup> In applying the scheme, we will continue to exclude debt raising costs because we have forecast them on a category specific basis. We will also make other adjustments as permitted by the EBSS, such as removing movements in provisions.

<sup>1</sup> NER, cl. 6.4.3(a)(5).

<sup>2</sup> Evoenergy, *Revised regulatory proposal*, November 2023, p. 44.

<sup>3</sup> AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013.

## 8.2 Evoenergy’s revised proposal

### 8.2.1 Carryover amounts accrued during the 2019–24 regulatory control period

Evoenergy included carryover amounts totalling \$15.8 million (\$2023–24) in its revenues for the 2024–29 period from the application of the EBSS in the 2019–24 period.<sup>4</sup>

Evoenergy excluded the following cost categories in calculating its EBSS carryover amounts:<sup>5</sup>

- debt raising costs
- demand management innovation allowance mechanism (DMIAM) opex
- movements in provisions related to opex.

### 8.2.2 Application in the 2024–29 control period

Evoenergy proposed that we continue to apply version 2 of the EBSS in the 2024–29 period.<sup>6</sup>

### 8.2.3 Stakeholder submissions

We received no stakeholder submissions on Evoenergy’s EBSS revised proposal.

## 8.3 Assessment approach

Under the National Electricity Rules (NER) we must determine:

- the revenue increments or decrements for each year of the 2024–29 period arising from the application of the EBSS during the 2019–24 period<sup>7</sup>
- how the EBSS will apply to Evoenergy in the 2024–29 period.<sup>8</sup>

The EBSS must provide for a fair sharing of opex efficiency gains and efficiency losses between Evoenergy and network users.<sup>9</sup> We must also have regard to the following matters when implementing the EBSS:<sup>10</sup>

- the need to provide Evoenergy with a continuous incentive to reduce opex
- the desirability of both rewarding Evoenergy for efficiency gains and penalising it for efficiency losses
- any incentives that Evoenergy may have to inappropriately capitalise expenditure

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<sup>4</sup> Evoenergy, *Revised regulatory proposal*, November 2023, p. 44.

<sup>5</sup> Evoenergy, *EBSS model*, November 2023.

<sup>6</sup> Evoenergy, *Revised regulatory proposal*, November 2023, p. 43.

<sup>7</sup> NER, cl. 6.4.3(a)(5).

<sup>8</sup> NER, cl. 6.3.2(a)(3) and cl. 6.12.1(9).

<sup>9</sup> NER, cl. 6.5.8(a).

<sup>10</sup> NER, cl. 6.5.8(c).

- the possible effects of the scheme on incentives for implementing non-network alternatives.

### 8.3.1 Interrelationships

The EBSS is closely linked to our revealed cost approach to forecasting opex. When we assess or develop the opex forecast, the NER requires us to have regard to whether the opex forecast is consistent with any incentive schemes.<sup>11</sup>

Our opex forecasting method typically relies on using the ‘revealed costs’ of the service provider in a chosen base year to develop a total opex forecast if the chosen base year opex is not considered to be ‘materially inefficient’. Under this approach, a service provider would have an incentive to spend more opex in the expected base year. Also, a service provider has less incentive to reduce opex towards the end of the regulatory control period, where the benefit of any efficiency gains is retained for less time.

The application of the EBSS therefore serves two important functions:

- it removes the incentive for a service provider to inflate opex in the expected base year in order to gain a higher opex forecast for the next regulatory control period
- it provides a continuous incentive for a service provider to pursue efficiency improvements across the regulatory control period.

The EBSS does this by allowing a service provider to retain efficiency gains (or losses) for a total of six years, regardless of the year in which the service provider makes them. Where we do not propose to rely on the single year revealed costs of a service provider in forecasting opex, this has consequences for the service provider's incentives and our decision on how we apply the EBSS.

When a business makes an incremental efficiency gain, it receives a reward through the EBSS, and consumers benefit through a lower revealed cost forecast for the subsequent regulatory control period. This is how efficiency improvements are shared between consumers and the business. If we subject costs to the EBSS that are not forecast using a revealed cost approach, a business would in theory receive a reward for efficiency gains through the EBSS (at a cost to consumers), but consumers would not benefit through a lower revealed cost forecast in the subsequent regulatory control period. Therefore, we typically exclude costs that we do not forecast using a single year revealed cost forecasting approach.

For these reasons, our decision on how we will apply the EBSS to Evoenergy has a strong interrelationship with our decision on its opex (see Attachment 6 of this final decision). We have careful regard to the effect of our EBSS decision when making our opex decision, and our EBSS decision is made largely in consequence of (and takes careful account of) our past and current decisions on Evoenergy's opex.

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<sup>11</sup> NER, cl. 6.5.6(e)(8). Further, we must specify and have regard to the relationship between the constituent components of our overall decision: NEL, s. 16(1)(c).

## 8.4 Reasons for final decision

This section provides the reasons for our final decision on the carryover amounts that arise from applying the EBSS during the 2019–24 period, and how we will apply the EBSS in the 2024–29 period.

### 8.4.1 Carryover amounts from the 2019–24 control period

Our final decision is to include EBSS carryover amounts totalling \$14.7 million (\$2023–24) from the application on the EBSS in the 2019–24 period. Our final decision is \$14.7 million higher than our draft decision, and \$1.1 million less than Evoenergy’s revised proposal of \$15.8 million. This difference is because we:

- did not include carryover amounts in our draft decision
- removed forecast and actual expenditure related to the administration costs of the LFiT
- update forecast inflation.

We discuss each of these in detail below.

We consider that the EBSS carryover amounts we have calculated provide for a fair sharing of efficiency gains and losses between Evoenergy and its network users. It provides rewards to Evoenergy for any efficiency gains it has made, and penalises Evoenergy for any efficiency losses. Further, we consider that the benefit to consumers, through lower forecast opex, is significant and sufficient to warrant the EBSS carryover amounts we have determined.

#### 8.4.1.1 Excluded carryovers in the draft decision

Our draft decision was to not include Evoenergy’s negative carryover amounts from the application of the EBSS in the 2019–24 period. This was because we did not use a revealed cost forecasting approach to forecast opex for the draft decision. We therefore considered that applying the EBSS penalties would not be consistent with the intended operation of the EBSS, nor give effect to the objective of fair sharing of efficiency losses in accordance with the NER. We provide further detail on this matter in our EBSS draft decision (Attachment 8).<sup>12</sup>

For the final decision, and as discussed in Attachment 6, we consider that Evoenergy’s opex in its revised proposed base year of 2022–23 is not materially inefficient. We have therefore used a revealed cost forecasting approach to forecast opex for the final decision. For this reason, we have also applied Evoenergy’s accrued EBSS carryover amounts in the 2024–29 period.

#### 8.4.1.2 Removed forecast and actual Large Feed-in-Tariff administration expenditure

Evoenergy’s revised proposal stated that the LFiT administration costs will now be reported and included as a jurisdictional scheme. This was an outcome of the ACT Government’s

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<sup>12</sup> AER, *Draft decision, Attachment 8 – Efficiency benefit sharing scheme – Evoenergy – 2024–29 Distribution revenue proposal*, September 2023, pp. 4–5.



2022–23 Reasonable Cost Determination.<sup>13</sup> This has implications when calculating carryovers, and specifically results in an incremental efficiency gain in 2022–23 because these costs are no longer in reported opex. In our EBSS explanatory statement, we considered whether we should exclude cost categories for services that will not be standard control services in the following period. We concluded that such costs are unlikely be forecast using a single year revealed cost forecasting approach and should be excluded from the EBSS on that basis.<sup>14</sup> Similarly, in this case, LFIT administration costs have not been forecast on a single year revealed costs basis. Instead, Evoenergy will be compensated for these costs as a jurisdictional scheme.

To avoid efficiency gains principally due to reporting changes, we have removed both actual and forecast LFIT administration expenditure from Evoenergy’s opex.

#### **8.4.1.3 Inflation**

Consistent with our standard approach and opex forecast, we used unlagged inflation to convert opex amounts to 2023–24 real terms. This is consistent with Evoenergy’s approach for its revised proposal.<sup>15</sup>

We used an updated consumer price index (CPI) value, compared to that used by Evoenergy in its revised proposal. For 2023–24, we used the inflation forecast for the year to June 2024 in the Reserve Bank of Australia's February 2024 *Statement on monetary policy*,<sup>16</sup> which was published after Evoenergy submitted its revised proposal.

### **8.4.2 Application in the 2024–29 control period**

Our final decision is to continue to apply version 2 of the EBSS to Evoenergy during the 2024–29 period. We consider applying the scheme will benefit the long-term interests of electricity consumers by providing a continuous incentive for Evoenergy to reduce its opex. Provided we forecast Evoenergy's future opex using its revealed costs in the 2024–29 period, any efficiency gains that Evoenergy achieves will lead to lower future opex forecasts, and thus lower network tariffs.

Version 2 of the EBSS specifies our approach to adjusting forecast or actual opex when calculating carryover amounts.<sup>17</sup> We provide details on these below.

#### **8.4.2.1 Adjustments to forecast or actual opex when calculating carryover amounts**

The EBSS allows us to exclude categories of costs that we do not forecast using a single year revealed cost forecasting approach in the following control period. We do this to fairly share efficiency gains and losses. For instance, where a service provider achieves efficiency improvements, it receives a benefit through the EBSS and consumers receive a benefit

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<sup>13</sup> Evoenergy, *Attachment 3 Operating expenditure*, November 2023, p. 27.

<sup>14</sup> AER, *Explanatory statement, Efficiency benefit sharing scheme*, November 2013, p. 16.

<sup>15</sup> Evoenergy, *EBSS model*, November 2023.

<sup>16</sup> Reserve Bank of Australia, *Statement on monetary policy, Appendix: Forecasts*, February 2024.

<sup>17</sup> AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013.

through lower forecast opex in the next regulatory control period. This is the way consumers and the service provider share in the benefits of an efficiency improvement.

If we do not use a single year revealed cost forecasting approach, we may not pass the benefits of these revealed efficiency gains to consumers. It follows that consumers should not pay for EBSS rewards where they do not receive the benefits of a lower opex forecast.

We do not forecast debt raising costs using a single year revealed cost forecasting approach. Instead, we provide a benchmark forecast. Accordingly, we have excluded these costs from the EBSS for the 2024–29 period, since any achieved efficiency gains (or losses) would not be passed on to network users.

We will also exclude projects under the DMIAM, because including them in the EBSS would distort the incentives provided under these schemes and allowances.

In addition to the excluded cost categories discussed above, we will also make the following adjustments when we calculate the EBSS carryover amounts accrued during the 2024–29 period:

- adjust forecast opex to add (subtract) any approved revenue increments (decrements) made after the initial regulatory determination, such as approved pass through amounts or opex for contingent projects
- adjust reported actual opex for the 2024–29 period to reverse any movements in provisions
- adjust reported opex to add capitalised opex that has been excluded from the regulatory asset base
- adjust forecast opex and actual opex for inflation<sup>18</sup>
- adjust opex for any services that will not be classified as standard control services in the 2029–34 regulatory period, to the extent these costs are not forecast using a single year revealed cost approach and excluding these costs better achieves the requirements of clause 6.5.8 of the NER.<sup>19</sup>

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<sup>18</sup> AER, *Efficiency Benefit Sharing Scheme for Electricity Network Service Providers*, November 2013, p. 7.

<sup>19</sup> AER, *Explanatory Statement – Efficiency Benefit Sharing Scheme for Electricity Network Service Providers*, November 2013, pp. 14–16.

## Shortened forms

Term	Definition
AER	Australian Energy Regulator
DMIAM	demand management innovation allowance mechanism
EBSS	efficiency benefit sharing scheme
LFIT	Large Feed-in Tariff Scheme
NER	national electricity rules
opex	operating expenditure

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