

Financeability guideline

Proposed

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1 Introduction

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).

On 29 March 2024 the Rules were amended following a consultation process to address challenges Transmission Network Service Providers (TNSPs) may have in raising finance to proceed with actionable Integrated System Plan (ISP) projects. The amended Rules provide greater flexibility to adjust the depreciation profiles of ISP related capital expenditure (capex) to address a demonstrable financeability issue.

As a result of this rule change we are required to develop and publish a financeability guideline in accordance with the transmission consultation procedures.¹ The first financeability guideline must be published and in effect by 31 December 2024.²

1.1 Contents of the guideline

The requirements of the guideline are set out in the NER.³ They require that the financeability guideline set out:

1. How the AER determines the financeability position of the TNSP for the purposes of demonstrating a financeability issue,⁴ which must be based on a selection of financial metrics and a specified weighting to apply to each of those metrics.
2. An explanation of the basis for the selection of each financial metric and the weighting to apply to each financial metric referred to in subparagraph (1).
3. How the financeability position for a TNSP relates to the financeability threshold for the purposes of demonstrating and addressing a financeability issue.⁵

The financeability guideline may also set out any other matters we consider appropriate.⁶

This proposed guideline sets out how we intend to implement the financeability rule change and assess financeability following a request related to actionable ISP projects. Once finalised, it is expected that a financeability guideline must always be in force. We may amend the guideline, but a guideline must always be in operation. The amended rules set out some specific requirements of the contents of the guideline, but also allow us to set out any other matters we consider appropriate.⁷

¹ NER, cl. 6A.6.3A(p).

² NER, cl. 11.167.2.

³ NER, cl. 6A.6.3A(r).

⁴ NER, cl. 6A.6.3A(l).

⁵ NER, cl. 6A.6.3A(l)–(m).

⁶ NER, cl. 6A.6.3A(s).

⁷ NER, cl. 6A.6.3A(r)–(s).

2 The guideline

This section sets out the elements of our guideline. The reasons for our decision are set out in our explanatory statement.

The guideline also includes a worked example (attachment A) showing how the guideline is expected to operate and the financeability guideline model (attachment B) that gives effect to the detail set out in this document.

2.1 Guiding principles

Our guiding principles will be informed by the requirements of the NER, and our obligation under the NEO to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers.

2.2 Information requirements

Applying the financeability guidelines in accordance with the NER requires certain information to be provided by the TNSP at the time of making a financeability request.⁸ Some of these requirements are set out in the NER, such as:

- the TNSP's proposed adjustments to the depreciation of the asset (or group of assets) and X factors (as applicable)⁹
- if applicable, the information required for any relevant concessional finance agreements.¹⁰

The TNSP must also provide any information required under the financeability guideline. These additional requirements are set out below.

2.2.1 Populated models

To apply the financeability test as specified by the NER a two-step process of calculating the financeability position is required.¹¹ If this test demonstrates a financeability issue a third scenario that addresses the issue must also be modelled.¹² For transparency, the financeability guideline requires a separate post-tax revenue model (PTRM) to be provided for each scenario where the financeability position needs to be calculated. These are:

1. The base case (prevailing determination) PTRM.
2. The unadjusted proposal PTRM.
3. The adjusted proposal PTRM.

In practice, this only requires the TNSP to provide one more PTRM (adjusted proposal) than would normally be required under a contingent project application (CPA). This is because the

⁸ NER, cl. 6A.6.3A(b).

⁹ NER, cl. 6A.6.3A(c)(1).

¹⁰ NER, cl. 6A.6.3A(c)(2) and 6A.6.3A(f).

¹¹ NER, cl. 6A.6.3A(k).

¹² NER, cl. 6A.6.3A(m).

'base case PTRM' is simply the latest approved PTRM at the time of the submission and the 'unadjusted proposal PTRM' is already required for a CPA.

The financeability guideline model must then be populated with the outputs from these individual PTRMs to demonstrate whether a financeability issue has been demonstrated, and whether the proposed adjustments effectively address the issue.

Base case PTRM

The 'base case PTRM' is the prevailing PTRM used for the first step of the financeability test.¹³ This PTRM is the latest approved PTRM for the TNSP and is used to determine a financeability position without the actionable ISP project and how it relates to the financeability threshold.

No further adjustments are required to the PTRM from that approved.

Unadjusted PTRM

The 'unadjusted PTRM' is the 'base case PTRM' where expenditure related to the actionable ISP project has been included. This PTRM is expected to be the same as the PTRM that would be submitted as part of a CPA if the TNSP was not eligible, or not requesting a financeability test. The depreciation schedules in this PTRM should reflect the requirements of clause 6A.6.3(b) without the exception for a financeability adjustment.

Adjusted PTRM

The 'adjusted PTRM' is the 'unadjusted PTRM' that includes the TNSP's proposed adjustments to the depreciation of the asset (or group of assets) and X factors (as applicable) for addressing a demonstrated financeability issue.¹⁴ This is the PTRM that underpins the revenue modelling of the overall CPA for incremental revenues associated with the actionable ISP project expenditure.

Financeability guideline model

The financeability guideline model is where the financeability test is performed. The purpose of the model is to:

1. take the relevant outputs from the above PTRMs as inputs to the financeability model
2. combine it with any adjustments specified in applicable concessional finance agreements
3. calculate the financeability position for each case (section 2.3).

The model then compares these financeability positions to each other and the financeability threshold (section 2.4.1) and shows whether a financeability issue has been demonstrated (section 2.4.2) for the unadjusted case. If it has been demonstrated in the unadjusted case, it will also show if the proposed adjustment addresses the demonstrated financeability issue (section 2.5).

¹³ NER, cl. 6A.6.3A(k).

¹⁴

2.2.2 Concessional finance information

Consistent with clause 6A.6.3A(f)(1) of the NER, as part of a financeability request submission the TNSP must provide:

- a) a copy of every concessional finance agreement (including any amendments to it) relating to any actionable ISP project it, or a related entity of it, has entered into;
- b) if applicable, the written approval of the government funding body to which the financeability request relates;
- c) if a concessional finance agreement was entered into by a related entity of the TNSP, the name, ACN and contact details of the related entity that is party to the agreement, and an explanation of the benefit of the concessional finance to the TNSP;
- d) a description of the capital expenditure in relation to which the concessional finance is being provided; and
- e) a description of the benefits of the concessional finance to the TNSP and an explanation of how the benefits are to be taken into account by the AER in applying the financeability test, in accordance with the concessional finance agreement.

We may also consult with the relevant government funding body about the financeability request. This may include requesting information from the government funding body and/or disclosing any information received from the TNSP in the financeability request in order to confirm the treatment of benefits.¹⁵

2.2.3 Justification of proposal

As part of its proposal and financeability request, the TNSP must provide an explanation of why the proposed adjustment is appropriate and addresses the demonstrated financeability issue to the extent possible. It should also provide detail of any alternative approaches that were considered as part of developing its proposal.

2.3 Determining financeability position

The calculation that is used to determine the financeability position is set out in the financeability guideline model formulae. We have also set out the detailed equations below.

Our proposed guideline is based on the approach that Moody's set out in its methodology for scoring the leverage and coverage factor in regulated electric and gas networks using cash flows from the relevant PTRM, including any adjustments required for concessional finance.

The key metrics that are used to determine the financeability position are:

- Adjusted interest coverage ratio (AICR)
- Net debt/regulatory asset base (a measure of gearing)
- Funds from operations (FFO)/Net debt
- Retained cash flows (RCF)/Net debt.

¹⁵ NER, cl. 6A.6.3A(g).

To determine the financeability position using these metrics, each individual metric is first calculated based on the equations set out in sections 2.3.1 to 2.3.4. Then these individual metrics are matched to a numeric score between 1 and 18 (section 2.3.5).

A weighted average score is then calculated by multiplying each metric's individual score by the relevant weighting. The weighting attributed to each metric reflects its base weighting plus an adjustment factor that increases the relative weight of weaker scoring metrics (section 2.3.6).

The resulting weighted average numeric score is what will be used as the 'financeability position'.

2.3.1 Adjusted interest coverage ratio

The adjusted interest coverage ratio (AICR) is a measure of recurring operating earnings compared to the expected interest costs. It is calculated as the ratio between the expected funds from operations (FFO) *plus* interest expenses *less* regulatory depreciation, to interest expenses. The assumed interest expense is required to be adjusted for any amendment to interest costs specified in a concessional finance agreement. It is calculated on a 3-year forward average.

$$AICR_t = \frac{\sum_t^{t+2} (FFO_t + interest_t - RegDepn_t) / interest_t}{3}$$

Where:

- a) $FFO_t = \text{maximum allowed revenue (MAR)}_t - \text{operating expenditure (opex)}_t - \text{interest}_t - \text{tax}_t$
- b) $interest_t = \text{benchmark interest payments}_t - \text{cash flow (CF) interest adjustment}_t$
- c) $CF \text{ interest adjustment}_t = \text{adjustment as described in financeability request in accordance with clause 6A.6.3A(f)(1) of the NER.}$
- d) $t = \text{regulatory year}$

2.3.2 Net debt/regulatory asset base (Gearing)

Net debt to regulatory asset base (RAB) or gearing is the level of debt compared to the overall value of the RAB. It will normally reflect the benchmark gearing ratio set out in the applicable Rate of Return Instrument (RoRI) which is 60% (at time of publishing). However, it may be adjusted downwards to reflect an increase in equity if specified in an applicable concessional finance agreement. It is calculated on a 3-year forward average.

$$Gearing_t = \frac{\sum_t^{t+2} Net\ debt_t / RAB_t}{3}$$

Where:

- a) $Net\ debt_t = \frac{\sum_t^{t+1} Net\ debt\ (start\ period)_t}{2}$
- b) $RAB_t = \frac{\sum_t^{t+1} RAB\ (start\ period)_t}{2}$
- c) $Net\ debt\ (start\ period)_t = \text{benchmark debt ratio} \times RAB\ (start\ period)_t - CF\ gearing\ adjustment$
- d) $\text{benchmark debt ratio} = 60\%$

- e) *CF gearing adjustment_t* = adjustment as described in financeability request in accordance with clause 6A.6.3A(f)(1) of the NER.
- f) *t* = *regulatory year*

2.3.3 FFO/Net debt (FFOND)

FFO/Net debt is a measure of recurring operating earnings compared to the amount of debt held by a TNSP. It is calculated as the expected FFO divided by the debt proportion of the RAB. The assumed interest expense (within FFO) and the value of the debt portion of the RAB must also reflect any adjustments specified in an applicable concessional finance agreement. It is calculated on a 3-year forward average.

$$FFOND_t = \frac{\sum_t^{t+2} FFO_t / Net\ debt_t}{3}$$

- a) $FFO_t = MAR_t - opex_t - interest_t - tax_t$
- b) $interest_t = benchmark\ interest\ payments_t - CF\ interest\ adjustment_t$
- c) *CF interest adjustment_t* = adjustment as described in financeability request in accordance with clause 6A.6.3A(f)(1) of the NER.
- d) $Net\ debt_t = \frac{\sum_t^{t+1} Net\ debt\ (start\ period)_t}{2}$
- e) $Net\ debt\ (start\ period)_i = benchmark\ debt\ ratio \times RAB\ (start\ period)_i - CF\ gearing\ adjustment_t$
- f) *CF gearing adjustment_t* = adjustment as described in financeability request in accordance with clause 6A.6.3A(f)(1) of the NER.
- g) *t* = *regulatory year*

2.3.4 RCF/Net debt (RCFND)

RCF/Net debt is a measure of the net change in cash and cash equivalents compared to the amount of debt held by a TNSP. It is calculated as the internal cash flow less expected dividend payments divided by the debt proportion of the RAB. The assumed interest expense (within the internal cash flow) and the value of the debt portion of the RAB must also reflect any adjustments specified in any relevant concessional finance agreement. It is calculated on a 3-year forward average.

$$RCFND_t = \frac{\sum_t^{t+2} RCF_t / Net\ debt_t}{3}$$

Where:

- a) $RCF_t = internal\ cash\ flow_t - dividend\ payments_t$
- b) $internal\ cash\ flow_t = MAR_t - opex_t - interest_t - tax_t - revenue\ adjustments_t$
- c) $interest_t = benchmark\ interest\ payments_t - CF\ interest\ adjustment_t$
- d) *CF interest adjustment_t* = adjustment as described in financeability request in accordance with clause 6A.6.3A(f)(1) of the NER.
- e) $dividend\ payments_t = \frac{tax_t}{tax\ rate_t} * (1 - tax\ rate_t) \times imputation\ credit\ payout\ ratio_t$
- f) $Net\ debt_t = \frac{\sum_t^{t+1} Net\ debt\ (start\ period)_t}{2}$
- g) $Net\ debt\ (start\ period)_t = benchmark\ debt\ ratio \times RAB\ (start\ period)_t - CF\ gearing\ adjustment$
- h) *benchmark debt ratio* = 60%

- i) *CF gearing adjustment* = adjustment as described in financeability request in accordance with clause 6A.6.3A(f)(1) of the NER.
- j) *t = regulatory year*

2.3.5 Individual metric scores

Once each metric has been calculated for each year it is matched to a numeric score between 1 and 18 based on the table below depending on the relevant range that it falls into.

Table 2.1 Ranges for financial metric results and rating category score mapping

Score (Metric _s)	AICR	Net debt/RAB	FFO/Net debt	RCF/Net debt
1	>=5.5	>30%	>=35%	>=30%
3	3.5<5.5	45%>30%	26%<35%	21%<30%
6	2.0<3.5	60%>45%	18%<26%	14%<21%
9	1.4<2.0	75%>60%	11%<18%	7%<14%
12	1.1<1.4	90%>75%	5%<11%	1%<7%
15	0.9<1.1	100%>90%	0%<5%	-4%<1%
18	<0.9	>100%	<0%	<-4%

Source: Moody's Investor Service, *Rating Methodology - Regulated Electric and Gas Networks*, 13 April 2022, pp. 4–8, 20.

2.3.6 Overall quantitative score (Financeability position)

The individual scores for each metric above are then combined together to calculate the weighted average quantitative score which is the measure of the financeability position.

The base weightings for each individual metric (before any adjustments) are shown in Table 2.2.

Table 2.2 Base weighting for financial metrics

Metric	Base weighting
AICR	25.0%
Net debt/RAB	31.25%
FFO/Net debt	31.25%
RCF/Net debt	12.5%

To reflect that a particularly weak performance in one metric cannot be exactly offset by better performance in another metric, there is an added weighting multiplier applied to metrics that score above 6. The weighting multiplier increases the worse the metric scores below this point as illustrated in Table 2.3.

Table 2.3 Weighting multiplier for financial metrics

Score (Metric _s)	Weighting multiplier (Metric _{WM})
1	1
3	1
6	1
9	1.15
12	2
15	3
18	5

Source: Moody's Investor Service, *Rating Methodology - Regulated Electric and Gas Networks*, 13 April 2022, p. 20.

The overall financeability position is then calculated based on the individual scores and their weighting after adjusting for the weighting multiplier. The formula below sets out the calculation.

$$Position_t = AICR_{St} \frac{AICR_{Wt}}{Total_{Wt}} + Gearing_{St} \frac{Gearing_{Wt}}{Total_{Wt}} + FFOND_{St} \frac{FFOND_{Wt}}{Total_{Wt}} + RCFND_{St} \frac{RCFND_{Wt}}{Total_{Wt}}$$

Where:

- a) S = individual metric's score as per Table 2.1.
- b) t = regulatory year
- c) $AICR_{Wt} = (25\% \times AICR_{WMt})$
- d) $Gearing_{Wt} = (31.25\% \times Gearing_{WMt})$
- e) $FFOND_{Wt} = (31.25\% \times FFOND_{WMt})$
- f) $RCFND_{Wt} = (12.5\% \times RCFND_{WMt})$
- g) WM = individual metric's weighting multiplier as per Table 2.3.
- h) W = metric's adjusted weighting.
- i) $Total_{Wt} = AICR_{Wt} + Gearing_{Wt} + FFOND_{Wt} + RCFND_{Wt}$

2.4 Financeability threshold and demonstrating issue

Once the financeability position has been determined for each case in accordance with section 2.3 it must be compared against the threshold to determine both whether there is a financeability issue under the unadjusted case, and whether the proposed adjustment appropriately addresses the issue.

2.4.1 Threshold

The financeability threshold for the purposes of this test means the benchmark credit rating used to estimate the return on debt component in the applicable RoRI. At time of publishing this guideline this is a credit rating of BBB+. ¹⁶

¹⁶ AER, *Explanatory Statement - Rate of Return Instrument*, 24 February 2023, pp. 222–228.

The method for calculating the financeability position is based on Moody’s rating methodology for regulated electric and gas networks. BBB+ is not a relevant Moody’s credit rating, however, this is broadly equivalent to Baa1 under Moody’s rating approach.

Table 2.4 below shows the range of numeric scores that reflect each ‘scorecard indicated outcome’ credit rating. The highest numeric score before falling outside the Baa1 outcome (equivalent to BBB+) is 8.50. As such, this score is translated to the financeability threshold that is used in our financeability guideline.

If a financeability position is at or above 8.5 it is considered outside the threshold, if it scores lower than 8.5 it is considered within the threshold.

Table 2.4 Moody’s overall scorecard-indicated outcome

Numeric score	Moody’s Outcome	S&P equivalent rating
$x < 1.5$	Aaa	AAA
$1.5 \leq x < 2.5$	Aa1	AA+
$2.5 \leq x < 3.5$	Aa2	AA
$3.5 \leq x < 4.5$	Aa3	AA-
$4.5 \leq x < 5.5$	A1	A+
$5.5 \leq x < 6.5$	A2	A
$6.5 \leq x < 7.5$	A3	A-
$7.5 \leq x < 8.5$	Baa1	BBB+
$8.5 \leq x < 9.5$	Baa2	BBB
$9.5 \leq x < 10.5$	Baa3	BBB-
$10.5 \leq x < 11.5$	Ba1	BB+
$11.5 \leq x < 12.5$	Ba2	BB
$12.5 \leq x < 13.5$	Ba3	BB-
$13.5 \leq x < 14.5$	B1	B+
$14.5 \leq x < 15.5$	B2	B
$15.5 \leq x < 16.5$	B3	B-

Within threshold
Outside threshold

2.4.2 Demonstration a financeability issue

To demonstrate that a financeability issue exists the financeability position must be calculated for each case described in section 2.2.1:

1. The base case = $Position_B$
2. The unadjusted case = $Position_U$
3. The adjusted case = $Position_A$

If the base case is below 8.5 but after the inclusion of the ISP project the financeability position deteriorates to 8.5 or beyond, the financeability test is satisfied and the project is

eligible for a financeability adjustment. (i.e. if $Position_B < 8.5$, then a financeability issue is demonstrated if $Position_U \geq 8.5$).

If the base case financeability position is already at or above 8.5 and inclusion of the ISP project deteriorates it further beyond this level, it will satisfy the financeability test and be eligible for a financeability adjustment. (i.e. if $Position_B \geq 8.5$ then a financeability issue is demonstrated if $Position_U > Position_B$).

2.5 Addressing a financeability issue

The proposed adjustment to address the demonstrated financeability issue should be the minimum adjustment required to satisfy the financeability test. If the base case financeability position is within the threshold the adjustment should only bring the financeability position to the threshold (8.5) and not to the previous financeability position level. Otherwise, the adjustment should bring the financeability position back to the base case position, but not beyond this. In other words:

- If the base case position is within the financeability threshold ($Position_B < 8.5$), then a financeability issue has been addressed for a given regulatory year if the financeability position for the adjusted case is within the financeability threshold ($Position_A < 8.5$).
- If the base case position is already outside the threshold for a given regulatory year, then a financeability issue has been addressed if the financeability position for the adjusted case is equal to the financeability position from the base case position ($Position_A \leq Position_B$).

Consistent with clause 6A.6.3A(n) of the NER, the financeability issue may be addressed by doing any one or more of the following:

1. depreciating the asset (or group of assets) forming part of the actionable ISP project using an alternative profile,
2. adjusting the X factors for each regulatory year in the remainder of the relevant regulatory control period.¹⁷

Option 1 can take a number of forms. It may be adjusting the ‘as-commissioned’ capex profile in the PTRM to bring forward a portion of ISP related expenditure to the year it is expected to be incurred (effectively applying as-incurred depreciation). It may also involve reducing the assumed asset life for some ISP related expenditure. This can be done by either amending the assumed standard life for the asset class (assuming this asset class only includes ISP related assets) or reallocating some ISP related expenditure to a new asset class with an accelerated life applied to it. If the template regulatory models allow, option 1 may also include applying an alternative method of depreciation to ISP related expenditure, such as shaped depreciation.

Depending on the magnitude of adjustment required this adjustment may be made to either a proportion of annual ISP expenditure across various asset classes, a single asset class, or the entire ISP project expenditure.

¹⁷ The Rules also noted that a financeability issue may be addressed by “taking other steps through another mechanism available to the AER under the Rules”. We are not aware of any appropriate alternative mechanisms that may be used to address a financeability issue in a net present value neutral manner.

If the depreciation adjustment encompasses a subsequent regulatory control period, then the depreciation adjustment is binding on the AER and the TNSP for that subsequent regulatory control period.

Following any change to the underlying building block revenues within the regulatory control period, the X factors for the remaining years of the regulatory period will require amending. Option 2 can therefore be used to smooth a greater portion of revenue into years where there is a particular drop in cash flow metrics. However, when considering this option, we must still have regard to the requirement of the Rules to ensure that the expected maximum allowed revenue in the final year of a regulatory period is as close as reasonably possible to the annual building block revenue requirement for that year.¹⁸

¹⁸ NER, cl. 6A.6.8(c).

3 The financeability guideline model

As discussed in section 2.2.1, the Rules require a TNSP submitting a financeability request to provide information that allows for the calculation of the financeability position using the financeability guideline model. This requires the provision of 3 separate PTRMs which demonstrate the TNSP's base case position, the unadjusted position and the adjusted position.

To populate the unadjusted PTRM, the TNSP should follow the same methodology for a CPA. There should be no adjustments made to depreciation or X factors that would otherwise apply in the standard approach for a CPA.

The adjusted PTRM should reflect the unadjusted case with the proposed amendments made to depreciation and X factors as applicable and described in section 2.5.

3.1 Using the model

The financeability guideline model is used to compare the outputs of each case by calculating the financeability position and determining the outcomes of the assessment process.

3.1.1 Updating the model 'Inputs'

The first step to doing this is updating the 'Inputs' sheet to reflect the outputs of each PTRM.

1. Begin by updating the 'Common inputs' at the top of the sheet to reflect variables that are consistent across all cases (rows 6 to 11).
2. Next, the individual cases should be updated (rows 13 to 73). All numbers can be found under the 'Analysis' sheet in the PTRM except for the Revenue (smoothed) numbers which are found in the 'X factors' sheet.
3. Finally, the 'Expected concessional finance inputs' should be populated to reflect any concessional finance or hybrid loan information that is applicable (rows 75 to 96).

With these steps, the 'Inputs' will be complete and the calculation sheets will update to reflect the calculation of the metrics.

3.1.2 Interpreting the 'Results'

The 'Results' sheet sets out the two-step financeability test. Step 1 (row 14) will identify whether there is a financeability issue in the unadjusted case due to the inclusion of an actionable ISP project. This test is calculated with reference to the financeability threshold (section 2.4.1) and the process for demonstrating a financeability issue (section 2.4.2).

Step 2 (row 16) will determine if the adjusted case adequately addresses the issue identified in Step 1. It confirms whether the approach applied using the methods in section 2.5 have appropriately solved the financeability issue.

If Step 1 does not indicate an issue, the ISP project in its current state does not require a financeability adjustment under the Rules. If Step 2 fails to solve the issue (or exceeds the 'minimum adjustment required') then the TSNP is expected to alter the approach taken in the adjusted PTRM to reflect the requirements of the Rules.

Shortened forms

Term	Definition
AER	Australian Energy Regulator
AICR	adjusted interest coverage ratio
capex	capital expenditure
CPA	contingent project application
FFO	funds from operation
ISP	Integrated System Plan
NEL	National Electricity Law
NER	National Electricity Rules
NEO	National Electricity Objective
MAR	maximum allowed revenue
PTRM	post-tax revenue model
RAB	regulatory asset base
RCF	retained cash flows
TNSP	transmission network service provider

Attachment A Worked example

This section describes a worked example of how we expect the financeability guideline would be put into practice following a TNSP submitting a financeability request related to an actionable ISP project. The key assumptions for the worked example are included as PTRM attachments to this document along with a financeability model which sets out the financial metrics and financeability test outcomes.

In this example the TNSP operates a network with an opening RAB value of \$5 billion and ongoing capex that approximately offsets the depreciation of the opening RAB. The TNSP has a 5-year regulatory control period. In the first year of this regulatory control period, the TNSP submits a contingent project application (CPA) for an actionable ISP project with a total capex value of \$1 billion incurred over 3 years—\$250 million in year 1, \$500 million in year 2 and \$250 million in year 3. The project is to be commissioned in year 3.

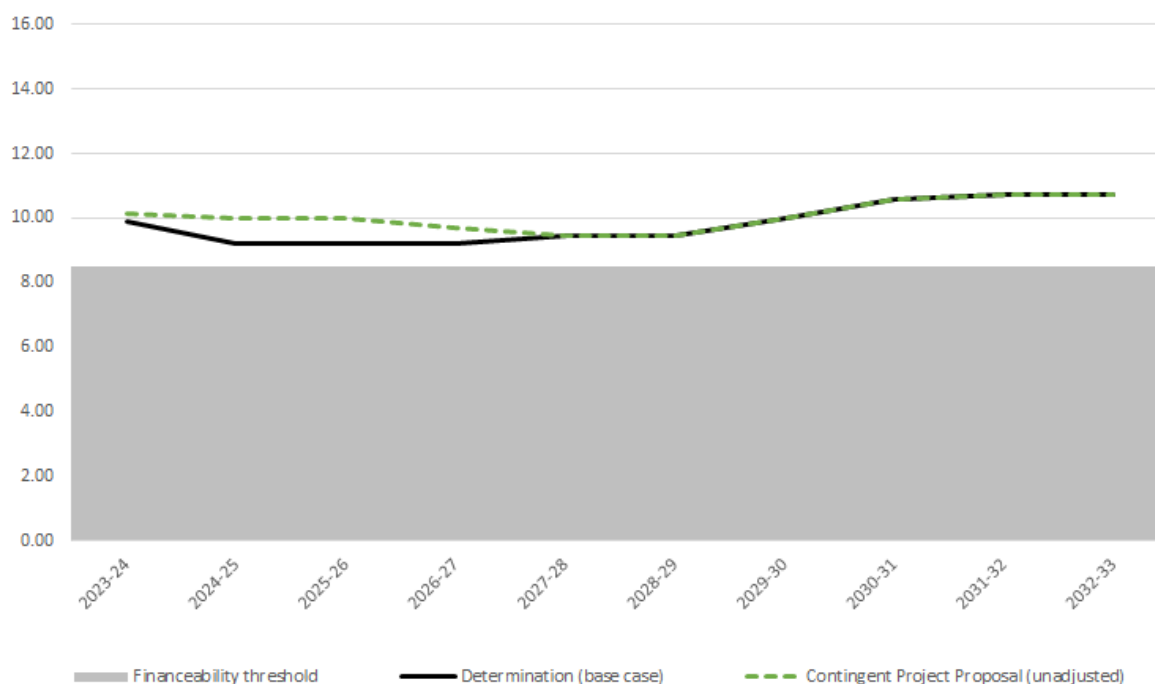
The TNSP has also secured a financing agreement from a government funding body (GFB) for \$300 million in senior debt at a concessional rate of 3.0% per annum (compared to the market rate of 6.0% per annum). However, the TNSP considers that this concessional finance is not sufficient to address its financeability issues, and as part of this agreement, the GFB has allowed the TNSP to also submit a financeability request as part of its CPA.

The proposed guideline requires the TNSP to populate two PTRMs and the financeability model to demonstrate that it has a financeability issue and its proposal to address this issue.

The first PTRM is the same PTRM that would be submitted under any other CPA proposal. This reflects the TNSP's latest approved determination PTRM with its forecast CPA related expenditure included. To demonstrate that the financial metrics resulting from this 'unadjusted PTRM' exhibit a financeability issue the financeability model takes the relevant cash flow outputs from this PTRM and compares it against those in the latest approved determination PTRM. Since the TNSP has entered into a concessional finance agreement for the actionable ISP project which relates to the financeability request, it must also populate the 'expected concessional finance inputs' section of the financeability model. In this case the TNSP has only received a concessional rate on senior debt, therefore it does not need to populate the 'Hybrid loans' section.

As required by the rules, the financeability model calculates the financeability position (as described in 2.3) of the TNSP before and after including the actionable ISP expenditure and compares it to the financeability threshold (described in 2.4). If there is a demonstrated financeability issue the 'Results' sheet in the financeability model will show "YES" for the year where a financeability issue is demonstrated. In the worked example, there is a financeability issue demonstrated in the first 4 years of the regulatory control period—after accounting for its concessional finance arrangements (see Figure A.1). Consistent with Moody's scorecard methodology a higher score means a worsening financeability position.

Figure A.1 Worked example of financeability position prior to any adjustments (lower=better)



As illustrated, the financeability position under the ‘base case’ (latest determination PTRM) is already outside the financeability threshold in each year shown. After including the actionable ISP related expenditure, it deteriorates further over the next 5 years. Consistent with clause 6A.6.3A(I)(2) in the amended Rules the financeability test in this case has demonstrated that a financeability issue exists.

The next step following the demonstration that a financeability issue exists is to address the financeability issue. To show how the TNSP proposes to address the financeability issue a second PTRM should be populated with the same actionable ISP expenditure as used above, but including any adjustments to the depreciation schedules and/or revenue smoothing that is proposed to resolve the financeability issue to the extent possible.

In the worked example as-incurred depreciation has been applied to all actionable ISP related capex. However, this was not sufficient to fully address the financeability issue. Therefore, a portion (\$30 million) of its forecast ‘Transmission lines’ capex in year 2 has been reallocated to accelerated depreciation asset classes and depreciated over 10 years (\$15 million) and 5 years (\$15 million), instead of the standard asset life of 50 years. The smoothing profile of revenues has also been adjusted slightly to provide greater revenues in the years where capital expenditure cashflows are at their highest.

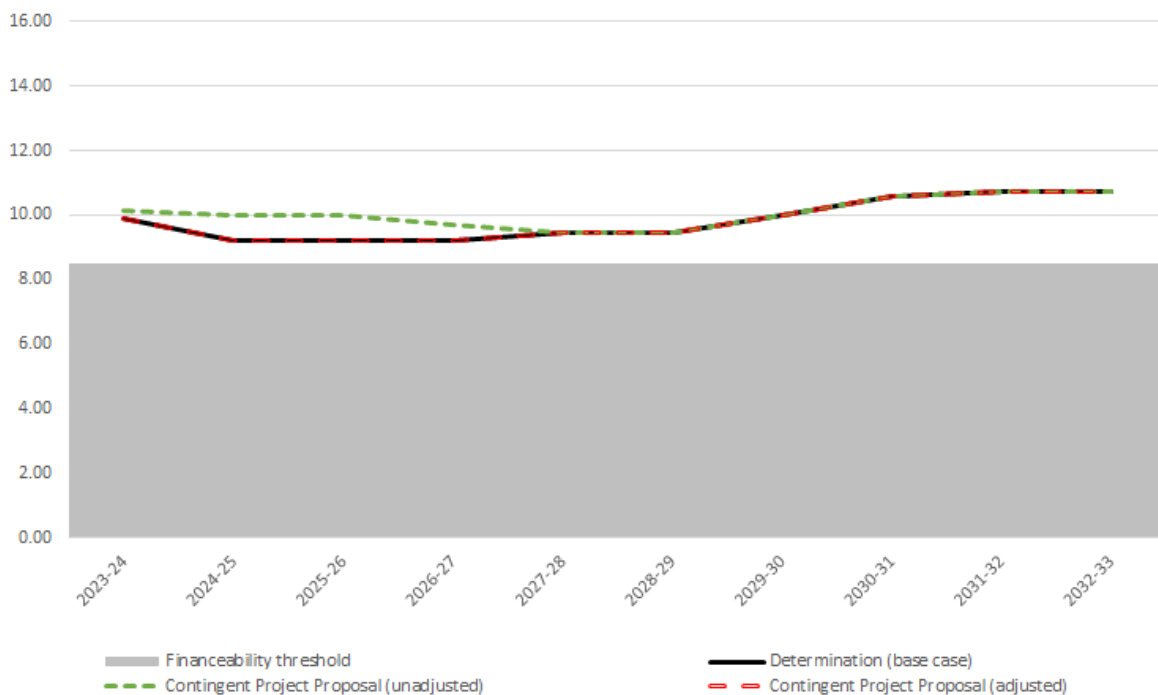
Once the outputs of the ‘adjusted PTRM’ are included in the financeability model, it shows that for the years where there was a demonstrated financeability issue, this has been addressed by the proposed adjustments. This is illustrated by the green “YES” values for the ‘Step 2’ checks shown in Figure A.2.

Figure A.2 Worked example of financeability position checks in financeability guideline model after making proposed adjustments to PTRM

TNSP - Financeability checks - Outputs

Year	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33
Numeric Result (reweighted) - 3y forward average										
Determination (base case)	9.88	9.22	9.22	9.22	9.44	9.44	10.02	10.59	10.72	10.72
Contingent Project Proposal (unadjusted)	10.16	9.99	9.99	9.71	9.44	9.44	10.02	10.59	10.72	10.72
Contingent Project Proposal (adjusted)	9.88	9.22	9.22	9.22	9.44	9.44	10.02	10.59	10.72	10.72
Financeability threshold	8.50	8.50	8.50	8.50	8.50	8.50	8.50	8.50	8.50	8.50
Step 1										
Financeability problem?	YES	YES	YES	YES	NO	NO	NO	NO	NO	NO
Step 2										
Problem addressed?	YES	YES	YES	YES	n/a	n/a	n/a	n/a	n/a	n/a

Figure A.3 Worked example of financeability position checks after proposed adjustments (lower=better)



There are numerous combinations of reallocated capital expenditure, depreciation schedules and revenue smoothing profiles that may be able to accomplish the task of addressing the financeability issue. The worked example shows just one approach that is available in our current template models that may be used to address the financeability issue in this case. It may also not be possible to perfectly match the base case financeability position in each year. We consider that provided the proposed adjustment solves the financeability issue to the extent possible, and does not put the TNSP in a materially better position than it was in the 'base case', then the proposed adjustment is likely to be reasonable.

Attachment B Financeability guideline model

The financeability guideline model is set out in a Microsoft Excel file.