

Draft Decision

Directlink Electricity Transmission Determination 2025 to 2030 (1 July 2025 to 30 June 2030)

Attachment 8 Efficiency benefit sharing scheme

September 2024

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Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601
Email: aerinquiry@aer.gov.au
Tel: 1300 585 165

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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 these between transmission businesses and network users. Consumers benefit from improved efficiencies through lower regulated prices.

This attachment sets out our draft decision and reasons on the EBSS carryover amounts Directlink has accrued over the 2020–25 regulatory control period (2020–25 period), and how we will apply the EBSS over the 2025–30 regulatory control period (2025–30 period).

8.1 Draft decision

Our draft decision is to include EBSS carryover amounts totalling -\$0.6 million (\$2024–25) from the application of the EBSS in the 2020–25 period. This is in line with Directlink’s proposal. We have updated our EBSS model to reflect the latest available data for inflation.

We set out our draft decision in table 8.1.

Table 8.1 Draft decision on Directlink’s carryover amounts (\$million, 2023–24)

	2025–26	2026–27	2027–28	2028–29	2029–30	Total
Directlink’s proposal	0.2	-0.3	-0.5	–	-0.0	-0.6
AER’s draft decision	0.2	-0.3	-0.5	–	0.0	-0.6
Difference	0.1	-0.0	-0.0	–	-0.0	0.0

Source: Directlink, *Attachment 3 - Revenue Proposal*, January 2024, p.65; AER analysis.

Note: Numbers may not add up due to rounding.

Our draft decision is also to continue to apply version 2 of the EBSS to Directlink in the 2025–30 period. Consistent with Directlink’s proposal, we will exclude debt raising costs and its insurance premium costs from the scheme because we have forecast them on a category specific basis and will continue doing so in the 2030–35 period. We will also make other adjustments as permitted by the EBSS, such as removing movements in provisions.

We discuss the reasons for our decision on applying the EBSS in the 2025-30 regulatory control period in section 8.4.2.

8.2 Directlink’s proposal

8.2.1 Carryover amounts from the 2020–25 regulatory control period

Directlink included EBSS carryover amounts totalling -\$0.6 million (\$2024–25) in its revenues for the 2025–30 period from the application of the EBSS in the 2020–25 period. Directlink excluded the following cost categories in calculating its EBSS carryover amounts:

- insurance premium costs
- debt raising costs.

8.2.2 Application in the 2025–30 regulatory control period

Directlink proposed to continue applying version 2 of the EBSS in the 2025–30 period. Directlink supported the adjustments we apply in version 2 of the EBSS, and additionally specified the following exclusions:

- insurance premium costs
- debt raising costs.

8.3 Assessment approach

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

- the revenue increments or decrements for each year of the 2025–30 period arising from the application of the EBSS during the 2020–25 period¹
- how the EBSS will apply to Directlink in the 2025–30 period.²

The EBSS must provide for a fair sharing of opex efficiency gains and efficiency losses between Directlink and network users.³ We must also have regard to the following matters when implementing the EBSS:⁴

- the need to provide Directlink with a continuous incentive to reduce opex
- the desirability of both rewarding Directlink for efficiency gains and penalising it for efficiency losses
- any incentives that Directlink may have to inappropriately capitalise expenditure
- the possible effects of the scheme on incentives for the implementation of 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.⁵

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.

¹ NER, cl. 6A.5.4(a)(5).

² NER, cll. 6A.14.1(1)(iv) and 6A.14.3(d)(2).

³ NER, cl. 6A.6.5(a).

⁴ NER, cl. 6A.6.5(b).

⁵ NER, cl. 6A.6.6(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).

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 Directlink has a strong interrelationship with our decision on its opex (see Attachment 6). 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 Directlink's opex.

8.4 Reasons for draft decision

This section provides the reasons for our draft decision on the carryover amounts that arise from applying the EBSS during the 2020–25 regulatory control period, and how we will apply the EBSS in the 2025–30 regulatory control period.

8.4.1 Carryover amounts from the 2020–25 regulatory control period

Our draft decision is to include EBSS carryover amounts totalling -\$0.6 million (\$2024–25) from the application on the EBSS in the 2020–25 period. Consistent with Directlink's approach, we have also used the formula in version 2 of the EBSS to calculate the carryover amount. This amount is in line with Directlink's proposal. However, we have updated our EBSS model to reflect the latest available actual and forecast inflation figures.

We discuss this below.

We consider that the EBSS carryover amounts we have calculated, which are consistent with those proposed by Directlink, provide for a fair sharing of efficiency gains and losses between Directlink and its network users. They provide for rewards to Directlink for any efficiency gains it has made, and penalise Directlink for any efficiency losses. Further, we consider that the benefit to consumers is sufficient to warrant the EBSS carryover amounts we have determined.

8.4.1.1 Inflation

Consistent with our standard approach and opex forecast, we used unlagged inflation to convert opex amounts to 2024–25 real terms. This approach is also consistent with the approach Directlink adopted in its proposal.

We used updated consumer price index (CPI) values compared to those Directlink used in its proposal. For 2022–23, we used the actual headline June quarter 2024 CPI figure published by the Australian Bureau of Statistics, which was released after Directlink submitted its proposal.⁶ For 2024–25, we used the inflation forecast for the year to June 2025 in the Reserve Bank of Australia's (RBA) August 2024 *Statement on monetary policy*,⁷ which was also published after Directlink submitted its proposal.

8.4.2 Application in the 2025–30 regulatory control period

Our draft decision is to continue to apply version 2 of the EBSS to Directlink during the 2025–30 period. We consider applying the scheme will benefit the long-term interests of electricity consumers by providing a continuous incentive for Directlink to reduce its opex. Provided we forecast Directlink's future opex using its revealed costs in the 2025–30 period, any efficiency gains (losses) that Directlink achieves will lead to lower (higher) future opex forecasts, and thus lower (higher) network tariffs.

Version 2 of the EBSS specifies our approach to adjusting forecast or actual opex when calculating carryover amounts.⁸ 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 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.

Debt raising costs

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 2025–30 period, since any achieved efficiency gains (or losses) would not be passed on to network users.

⁶ Australian Bureau of Statistics, *Consumer Price Index, Australia*, released on 31 July 2024 (accessed on 31 July 2024).

⁷ RBA, *Statement on monetary policy*, August 2024.

⁸ AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013.

Insurance costs

We have also excluded Directlink’s insurance premium costs from the EBSS for the 2025–30 period, due to the fact that we have not used a single year revealed cost forecasting approach to forecast these costs. We have excluded these costs from the EBSS for the 2025–30 period since any achieved efficiency gains (or losses) would not be passed on to network users.

Other adjustments

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 2025–30 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 2025–30 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 inflation⁹
- exclude categories of opex not forecast using a single year revealed cost approach for the regulatory control period beginning in 2025, where doing so better achieves the requirements of clause 6A.6.5 of the NER.¹⁰

⁹ AER, *Efficiency Benefit Sharing Scheme for Electricity Network Service Providers*, November 2013, p. 7.

¹⁰ AER, *Explanatory Statement - Efficiency Benefit Sharing Scheme for Electricity Network Service Providers*, November, p. 14.

Shortened forms

Term	Definition
AER	Australian Energy Regulator
CPI	Consumer price index
CESS	Capital expenditure sharing scheme
EBSS	Efficiency benefit sharing scheme
NEL	National Electricity Law
NER	National Electricity Rules
Opex	Operating expenditure
RAB	Regulatory asset base
RBA	Reserve Bank of Australia
