Draft Decision

Energex Electricity Distribution Determination 2025 to 2030

(1 July 2025 to 30 June 2030)

Attachment 8
Efficiency benefit sharing scheme

September 2024

AUSTRALIAN ENERGY REGULATOR

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AER reference: AER213703

Amendment record

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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.[1] Consumers benefit from improved efficiencies through lower regulated prices.

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

8.1 Draft decision

Our draft decision is to include EBSS carryover amounts totalling –$119.7 million[2] from the application of the EBSS in the 2020–25 regulatory control period.[3] This represents a $2.1 million difference compared to Energex's proposed carryover amount of –$121.8 million.[4] This difference reflects our use of the most recent inflation figures to convert amounts into 2024–25 dollars, which were not available when Energex submitted its proposal.[5]

In our final decision, we will update our EBSS carryover calculations to reflect actual opex for 2023–24 and for the most recent inflation data. Our draft decision is based on the estimate of base year opex included in Energex's initial proposal, because actual data for 2023–24 was not available at the time the proposal was submitted. During consultations with us, Energex indicated that its actual opex for 2023–24 is likely to significantly exceed the estimate it provided in its initial proposal.[6] This is likely to result in an increase in the size of the EBSS penalty applied in our final decision.

We set out our draft decision on the EBSS carryover amounts Energex accrued during the 2020–25 regulatory control period in table 8.1, along with Energex's proposal and the difference. We discuss this further in section 8.4.1.

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1 AER, *Explanatory statement – efficiency benefit sharing scheme*, November 2013, p. 5.

2 All dollars in this document are in $2024–25 terms unless otherwise stated.

3 Increments or decrements in revenue from the application of any EBSS constitutes one of the building blocks that must be used to determine a distributor's annual revenue requirement: NER, cl. 6.4.3(a)(5).

4 Energex, *RIN.03 – SCS EBSS Model,* January 2024.

5 Australian Bureau of Statistics, *Consumer Price Index, Australia, released on 31 July 2024* (accessed on 31 July 2024: https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release); Reserve Bank of Australia (RBA), *Statement on monetary policy*, *August 2024*, (accessed on 6 August 2024: https://www.rba.gov.au/publications/smp/2024/aug/outlook.html#3-5-detailed-forecast-information).

6 Energex, *Response to AER information request, IR#039 – Operating expenditure, Q3 (spreadsheet),* 17 July 2024.

Table 8.1 Draft decision on carryover amounts ($million, 2024–25)

	2025–26	2026–27	2027–28	2028–29	2029–30	Total
Energex's proposal	–68.8	–32.1	–24.0	3.1	–	–121.8
AER's draft decision	–68.3	–31.6	–23.5	3.6	–	–119.7
Difference	**0.6**	**0.5**	**0.5**	**0.5**	**–**	**2.1**

Source: Energex, *RIN.03 – SCS EBSS Model*, January 2024; AER analysis.
Note: Numbers may not add up due to rounding. '–' represents zero.

Our draft decision is also to continue to apply version 2 of the EBSS to Energex in the 2025–30 regulatory control period.[7] It will apply to the opex associated with the main standard control services, as discussed in Attachment 6, but not the metering standard control services opex, as discussed in Attachment 20. Consistent with Energex's proposal, we will exclude debt raising costs from the scheme because we have forecast them on a category specific basis and expect to continue doing so in the 2030–35 regulatory control period.[8] We will also make other adjustments as permitted by the EBSS, such as removing demand management innovation allowance mechanism (DMIAM) costs, movements in provisions, and adding approved opex for pass throughs and contingent projects to forecast opex.

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 Energex's proposal

8.2.1 Carryover amounts accrued during the 2020–25 period

Energex included EBSS carryover amounts totalling –$121.8 million in its proposed revenues for the 2025–30 period from the application of the EBSS in the 2020–25 regulatory control period.

Energex adjusted approved forecast opex to include the opex approved for the 2021–22 flood cost pass event. Energex also excluded the following cost categories in calculating its EBSS carryover amounts:[9]

- debt raising costs
- DMIAM costs
- movements in provisions related to opex.

7 We must decide on how any EBSS is to apply to distributors as part of this determination under cl. 6.12.1(9) of the NER; See also AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013.

8 Energex, *2025–30 Regulatory Proposal,* January 2024, p. 148.

9 Energex, *RIN.03 – SCS EBSS Model,* January 2024.

8.2.2 Application in the 2025–30 control period

Energex proposed that we apply version 2 of the EBSS to it in the 2025–30 regulatory control period, with adjustments for the following cost categories: [10]

- approved pass through amounts or opex for contingent projects
- movements in provisions
- capitalisation policy changes
- debt raising costs
- DMIAM costs.

8.2.3 Stakeholder submissions

Submissions from Energex's Reset Reference Group (RRG) and our Consumer Challenge Panel sub-panel 30 (CCP30) commented on the EBSS proposal.

The RRG supported the continued application of the EBSS in the 2025–30 regulatory control period for Energex, while noting that the network will likely overspend against its opex forecast in the next period. The RRG also questioned whether the EBSS provides the same incentive for Energex to move to efficient levels of expenditures as it does for privately owned distribution businesses. The RRG noted that '70% of any opex overrun is paid for by consumers, irrespective of whether it is efficient and prudent' and Government electricity rebates cushion the affordability impacts on households.[11]

The CCP30 also highlighted a trend of over expenditure by Energex in its operating costs, noting there is a clear risk that this over expenditure will impact consumers.[12] CCP30 further stated that this over expenditure in opex indicates that Energex does not respond strongly to our incentive schemes, including the EBSS. It highlighted that the penalties flowing from the incentive schemes in the current period, including the EBSS, form part of 'lower costs for consumers in the next regulatory control period.'[13]

We have taken these submissions into account in developing the positions set out in this draft decision. In particular, we agree that we should continue to apply the scheme over the 2025–30 regulatory control period to ensure there is some ongoing discipline, via the EBSS penalties and lower revenues, for Energex to manage its operating 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 regulatory control period arising from the application of the EBSS during the 2020–25 regulatory control period[14]

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10 Energex, *2025–30 Regulatory Proposal,* January 2024, p. 148.

11 RRG, *Submission – 2025–30 Electricity Determination – Energex & Ergon*, May 2024, pp. 54–55.

12 CCP30, *Submission – 2025–30 Electricity Determination – Energex & Ergon*, May 2024, p. 26.

13 CCP30, *Submission – 2025–30 Electricity Determination – Energex & Ergon*, May 2024, p. 31.

14 NER, cl. 6.4.3(a)(5).

- how the EBSS will apply to Energex in the 2025–30 regulatory control period.[15]

The EBSS must provide for a fair sharing of opex efficiency gains and efficiency losses between Energex and network users.[16] We must also have regard to the following matters when implementing the EBSS:[17]

- the need to ensure that benefits to electricity consumers likely to result from the scheme are sufficient to warrant any reward or penalty under the scheme
- the need to provide Energex with a continuous incentive to reduce opex
- the desirability of both rewarding Energex for efficiency gains and penalising it for efficiency losses
- any incentives that Energex 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 our opex forecast, the NER require us to have regard to whether the opex forecast is consistent with any incentive schemes.[18]

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:

1. 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.
2. 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 6 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.

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15 NER, cl. 6.3.2(a)(3); cl. 6.12.1(9).

16 NER, cl. 6.5.8(a).

17 NER, cl.6.5.8(c).

18 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: National Electricity Law (NEL), s. 16(1)(c).

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 Energex has a strong interrelationship with our decision on its opex (see Attachment 6). We have 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 account of) our past and current decisions on Energex'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 period.

8.4.1 Carryover amounts from the 2020–25 regulatory control period

Our draft decision is to include EBSS carryover amounts totalling –$119.7 million from the application of the EBSS in the 2020–25 regulatory control period. This represents a $2.1 million difference from Energex's proposed carryover amount of –$121.8 million. This difference reflects our use of the most recent inflation figures to convert amounts into 2024–25 dollars. We discuss the impact of inflation below. Full details of our draft decision are set out in our EBSS model, which is available on our website.

Consistent with Energex's proposal and our standard approach in calculating EBSS carryover amounts, we have also made the same adjustments and exclusions as discussed in section 8.2.1. This included adding the approved opex for the 2021–22 flood cost pass through event to total forecast opex.

Our assessment also considered the proposed change in treatment of opex related to the Electrical Safety Office Levy in the next regulatory control period, and any impacts on the EBSS carryovers in the current period.[19] We consider Energex's approach of not making any adjustment to forecast or actual opex for the change in treatment in Electrical Safety Office Levy expenditure to be appropriate in this circumstance.[20]

We consider that the EBSS carryover amounts we have calculated provide for a fair sharing of the efficiency losses Energex has made between itself and its network users.

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19 Energex, *2025–30 Regulatory Proposal,* January 2024, p. 136.

20 NER, cl. 6.5.8(c)(1).

In our final decision, we will update our EBSS carryover calculations to reflect actual opex for 2023–24. Our draft decision is based on an estimate because actual data for 2023–24 is not yet available. We will also update inflation.

8.4.1.1 Inflation

Consistent with our standard approach, and our opex forecast, we used unlagged inflation to convert amounts to 2024–25 dollars.[21] This approach is also consistent with the approach Energex adopted in its proposal.[22]

We have also used the latest inflation forecasts which were not available at the time Energex submitted its proposal, which increased our draft decision EBSS carryover amount by $2.1 million compared to Energex's estimate. For 2023–24, we used the actual headline Consumer Price Index figure published by the Australian Bureau of Statistics.[23] For 2024–25, we used the inflation forecast in the Reserve Bank of Australia's August 2024 *Statement on monetary policy*.[24]

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 Energex during the 2025–30 regulatory control period. It will apply to the opex associated with the main standard control services, as discussed in Attachment 6, but not the metering standard control services opex, as discussed in Attachment 20. We consider applying the scheme will benefit the long-term interests of electricity consumers as it will provide continuous incentives for Energex to reduce its opex. Provided we forecast Energex's future opex using its revealed costs in the 2025–30 period, any efficiency gains that Energex achieves will lead to lower opex forecasts, and thus lower network tariffs.

While, as set out in Attachment 6, we are using benchmarking, rather than revealed costs, to determine base opex in our alternative estimate, our draft decision is to accept Energex's total proposed opex. Given this, we consider applying the EBSS to Energex in the 2025–30 regulatory control period is reasonable and consistent with the NER.

Version 2 of the EBSS specifies our approach to adjusting forecast or actual opex when calculating carryover amounts.[25] 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. 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 network users receive a benefit through lower forecast opex

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21 This ensures Energex is not accruing carryovers that are not being passed on to customers.

22 Energex, *RIN.03 – SCS EBSS Model*, January 2024.

23 Australian Bureau of Statistics (ABS), *Consumer Price Index, Australia, released on 31 July 2024* (accessed on 31 July 2024: https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release).

24 Reserve Bank of Australia, *Statement on monetary policy*, *August 2024*, (accessed on 6 August 2024: https://www.rba.gov.au/publications/smp/2024/aug/outlook.html#3-5-detailed-forecast-information).

25 AER, *Efficiency benefit sharing scheme*, November 2013, pp. 7–8.

in the next regulatory control period. This is the way network users 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 network users. It follows that network users should not pay for EBSS rewards where they do not receive the benefits of a lower opex forecast.

For the 2025–30 regulatory control period, we have 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 regulatory control period, since any achieved efficiency gains (or losses) would not be passed on to network users.

In addition to excluding debt raising costs, we will also make the following adjustments when we calculate the EBSS carryover amounts accrued during the 2025–30 regulatory control period: [26]

- 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[27]
- adjust actual opex to remove DMIAM expenditure, because it is not included in the opex forecast (but is often reported by service providers as part of their standard control services opex)[28]
- adjust actual opex to add capitalised opex that has been excluded from the regulatory asset base[29]
- adjust forecast opex and actual opex for inflation[30]
- adjust actual opex to remove any movements in provisions related to opex
- adjust opex for any services that will not be classified as standard control services in the 2030–35 regulatory control 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.[31]

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26 AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013, pp. 7–8.

27 AER, *Efficiency benefit sharing scheme for electricity network service providers*, November 2013, p. 7.

28 Clause 6.5.8(c)(5) of the NER requires us to have regard to the possible effects of the scheme on incentives for the implementation of non-network options.

29 Clause 6.5.8(c)(4) of the NER requires us to have regard to any incentives the service provider may have to capitalise expenditure.

30 AER, *Efficiency benefit sharing scheme for electricity network service providers, November 2013*, p. 7.

31 AER, *Explanatory Statement – Efficiency benefit sharing scheme*, November 2013, pp. 14–16.

Shortened forms

Term	Definition
AER	Australian Energy Regulator
CCP30	Consumer Challenge Panel sub-Panel 30
DMIAM	Demand management innovation allowance mechanism
EBSS	efficiency benefit sharing scheme
NEL	National Electricity Law
NER	National Electricity Rules
opex	operating expenditure
RBA	Reserve Bank of Australia
RRG	reset reference group