Draft Decision

SA Power Networks Electricity Distribution Determination 2025 to 2030

(1 July 2025 to 30 June 2030)

Attachment 9
Capital expenditure sharing scheme

September 2024

AUSTRALIAN ENERGY REGULATOR

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

AER reference: AER213704

Amendment record

Version	Date	Pages
1	27 September 2024	6

Contents

9 Capital expenditure sharing scheme

The capital expenditure sharing scheme (CESS) provides financial rewards for network service providers whose capital expenditure (capex) becomes more efficient and financial penalties for those that become less efficient. Consumers benefit from improved efficiency through lower regulated prices.

The CESS approximates efficiency gains and efficiency losses by calculating the difference between forecast and actual capex. It shares these gains or losses between service providers and consumers.

The CESS mechanism was recently updated in April 2023. The changes to the CESS will apply to SA Power Networks' 2025–30 regulatory period as follows:

- we calculate the cumulative underspend or overspend for the current regulatory control period in net present value terms
- we apply the sharing ratio of 30 per cent all efficiency loses, and a tiered rate for efficiency gains, to work out what the service provider's share of the underspend or overspend should be[1]
- we calculate the CESS payments taking into account the financing benefit or cost to the service provider of the underspend or overspend.[2] We can also make further adjustments to account for deferral of capex and ex post exclusions of capex from the regulatory asset base (RAB)[3]

The CESS payments will be added or subtracted to the service provider's regulated revenue as a separate building block in the next regulatory control period.

For the current regulatory period, the CESS version referred to in the regulatory information notice will apply.[4]

We consider in addition to greater incentives to improve capex efficiency, the CESS provides a consistent incentive to incur capex efficiently during a regulatory control period and encourages more efficient substitution between capex and operating expenditure (opex).

This attachment sets out our decision for the determination of the revenue impact from the CESS in the 2020–25 regulatory control period and the application of the CESS for SA Power Networks in the 2025–30 regulatory control period.

---

1 The tiered rate calculation for efficiency gains will apply a 30 per cent sharing ratio for any underspend amount up to and including 10 per cent of the approved forecast capex allowance, while any amount greater will incur a 20 per cent sharing ratio.

2 We calculate benefits as the benefits to the service provider of financing the underspend since the amount of the underspend can be put to some other income generating use during the period. Losses are similarly calculated as the financing cost to the service provider of the overspend.

3 The capex incentive guideline outlines how we may exclude capex from the RAB and adjust the CESS payment for deferrals. AER, *Capital Expenditure Incentive Guideline for Electricity Network Service Providers*, November 2013, pp. 9, 13–20.

4 AER, *Capital Expenditure Incentive Guideline for Electricity Network Service Providers*, November 2013.

9.1 Draft decision

9.1.1 Revenue impacts in the 2025–30 period

Our draft decision is to apply a CESS revenue increment amount of $48.5 million ($2024–25) across the 2025–30 regulatory control period. This is from the application of the CESS in the 2020–25 regulatory control period and the corresponding CESS carryover true-up for 2019–20. This is $25.2 million more than SA Power Networks' forecast of $23.4 million.

The CESS increment arises as a result of an underspend in total capex to which the CESS applies against the forecast for the 2020–25 period. On 25 March 2024, the AER published its revocation and substitution determination for the 2020–25 regulatory control period. This corrected a material error relating to cable and conductor minor repairs that impacted our operating and capital expenditure decisions. Our draft decision on the revenue impact of the application of the CESS in the 2020–25 period and the corresponding CESS carryover true-up for 2019–20 is summarised in Table 9.1.

Table 9.1 CESS revenue increments from 2025–30 ($ million, 2024–25)

CESS item	2025–26	2026–27	2027–28	2028–29	2029–30	Total
CESS revenue increment as per NER 6.4.3(a)(5)	2.77	2.77	2.77	2.77	2.77	13.86
CESS carryover true-up for 2019–20	6.93	6.93	6.93	6.93	6.93	34.67
AER draft decision CESS	**9.7**	**9.7**	**9.7**	**9.7**	**9.7**	**48.53**

Source: SA Power Networks, *2025–30 Revenue proposal, Capital expenditure sharing scheme* model - *CESS True-up model*, January 2024, AER, *Final decision - SA Power Networks Distribution Determination 2020 to 2025 (1 July 2020 to 30 June 2025) - Revocation and substitution determination,* 25 March 2024 and AER analysis.

Note: Numbers may not sum due to rounding.

Given the timing of this draft decision, we calculated the CESS revenue increments in Table 9.1 using estimates of SA Power Networks' capex for the 2023–24 and 2024–25 regulatory years. The CESS revenue increment we calculated ($48.5 million) is different to the revenue increment that SA Power Networks proposed ($23.4 million) because SA Power Networks' forecast did not include our revocation and substitution determination in March 2024 that revoked our decision to approve forecast net capex of $1,595.8 million ($2019–20) and substitute it with forecast net capex of $1,696.0 million ($2019–20).[5] In addition, we applied updated modelling inputs, including inflation, rate of return and an adjustment for 2019–20 to reflect the difference between actual and estimated capex.

9.1.2 Application of the CESS in the 2025–30 period

We will apply the CESS as set out in the 2023 capital expenditure incentives guideline.[6] The reasons for adopting this CESS are set out in our final decision for the review of incentive

5 AER, *Final decision - SA Power Networks Distribution Determination 2020 to 2025 (1 July 2020 to 30 June 2025) - Revocation and substitution determination,* 25 March 2024, p. 4.

6 AER, *Final decision - Capital expenditure incentive guideline*, April 2023, pp.3–9.

schemes for networks, and the final decision for capital expenditure incentive guideline.[7] This is consistent with the proposed approach we set out in our framework and approach paper.[8]

9.2 SA Power Networks' proposal

9.2.1 CESS revenue increments from the 2020–25 regulatory control period

SA Power Networks proposed a $11.6 million ($2024–25) CESS revenue decrement to its regulated revenue in the 2025–30 regulatory control period.[9] This reflects an overspend of $19.0 million.

9.2.2 Final year actual capex true up for 2019–20

SA Power Networks submitted a true-up calculation method, which proposed a true-up increment of $35.0 million ($2024–25) to be added to its CESS revenue increments in the 2025–30 period.[10]

9.2.3 Application of CESS in the 2025–30 regulatory control period

SA Power Networks proposed to apply the CESS in the 2025–30 regulatory period.[11]

9.3 Assessment approach

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

- the revenue impacts on SA Power Networks arising from applying the CESS in the 2020–25 regulatory control period[12]
- whether or not to apply the CESS to SA Power Networks in the 2025–30 regulatory control period and how any applicable scheme will apply.[13]

We must determine the appropriate revenue increments or decrements (if any) for each year of the 2025–30 regulatory control period arising from the application of the CESS during the 2020–25 period regulatory control period.[14]

---

7 AER, *Final decision - Review of incentive schemes for networks*, April 2023, pp. 14–22; and AER, *Final decision - Capital expenditure incentive guideline*, April 2023.

8 AER, *Final framework and approach for SA Power Networks for the 2025-30 regulatory control period,* 3 July 2024, p. 20.

9 SA Power Networks*, Revenue Proposal 2025–30, Capital Expenditure Sharing Scheme Model*, 31 January 2024.

10 SA Power Networks, *Revenue Proposal 2025–30, CESS True-up Model*, 31 January 2024.

11 SA Power Networks*, Revenue Proposal 2025–30, Attachment 9 – Capital Expenditure Sharing Scheme*, 31 January 2024, p. 9.

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

13 NER, cl. 6.12.1(9).

14 Increments or decrements arising from the application of applicable incentive mechanisms, including any capital expenditure sharing scheme, form one of the building blocks that must be used to determine the annual building block revenue requirement for distribution network service providers for each regulatory year of a regulatory control period: NER, cl. 6.4.3(a)(5).

In deciding whether to apply a CESS to SA Power Networks for the 2025–30 period, and the nature and details of the scheme, we must:[15]

- make that decision in a manner that contributes to the capex incentive objective[16]
- take into account the CESS principles,[17] the capex objectives and, where relevant, the opex objectives,[18] the interaction with other incentive schemes,[19] and the circumstances of the service provider.[20]

Broadly, the capex incentive objective is to ensure that only capex that meets the capex criteria enters the RAB used to set prices. Therefore, consumers only fund capex that is efficient and prudent.

9.3.1 Interrelationships

The approval of CESS revenue increment/decrement determines the associated CESS building block as part of SA Power Networks' overall forecast revenue requirement for the 2025–30 regulatory control period.

The CESS relates to other incentives SA Power Networks faces to incur efficient opex, conduct demand management, and maintain or improve service levels. Related schemes include the efficiency benefit sharing scheme (EBSS) for opex, the service target performance incentive scheme (STPIS) for service levels and demand management incentive allowance mechanism (DMIAM). We aim to incentivise network service providers to make efficient decisions on when and what type of expenditure to incur and to balance expenditure efficiencies with service quality.

9.4 Reasons for draft decision

Our draft decision is to include an overall CESS revenue increment of $48.5 million ($2024–25) in the 2025–30 period, comprising a $13.9 million increment for the 2020–25 capex performance and a $34.7 million increment for the final year true-up (for 2019–20). This is a $25.2 million increase from SA Power Networks' proposed CESS revenue increment of $23.4 million ($2024–25). We set out our reasons in the sections below.

9.4.1 CESS revenue increments from the 2020–25 regulatory control period

Our draft decision includes a CESS increment of $48.5 million ($2024–25) for SA Power Networks' capex performance in the 2020–25 period. This means that SA Power Networks' allowed revenue in the 2025–30 regulatory control period is $48.5 million more than it would

---

15 NER cl. 6.5.8A(e).

16 NER, cl. 6.5.8A(e)(3); the capex incentive objective is set out in cl. 6.4(a).

17 NER, cl. 6.5.8A(e)(4)(i); the CESS principles are set out in cl.6.5.8A(c).

18 NER, cll. 6.5.8A(e)(4)(i) and 6.5.8A(d)(2); the capex objectives are set out in cl. 6.5.7(a); the opex objectives are set out in cl. 6.5.6(a).

19 NER, cl. 6.5.8A(d)(1).

20 NER, cl. 6.5.8A(e)(4)(ii).

otherwise have been due to the application of the CESS to SA Power Networks in the 2020–25 regulatory control period.

9.4.2 Revocation and substitution determination March 2024

On 25 March 2024, we published our revocation and substitution determination for SA Power Networks for the 2020–25 regulatory control period.[21] This corrected a material error relating to cable and conductor minor repairs that impacted our operating and capital expenditure decisions.[22]

9.4.3 Final year actual capex true-up for 2019–20

Our draft decision includes a true-up adjustment of $34.7 million to account for SA Power Networks' updated actual capex for 2019–20. This is $0.3 million less than SA Power Networks' forecast true-up adjustment of $35.0 million.

21 AER, *Final decision - SA Power Networks Distribution Determination 2019 to 2025 (1 July 2019 to 30 June 2025) - Revocation and substitution determination,* 25 March 2024.

22 The revocation also included the additional net capex approved for the April 2022 emergency standards cost pass through event, which we approved since our final decision for 2020–25 distribution determination for SA Power Networks in June 2020.

Shortened forms

Term	Definition
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
NER	national electricity rules
opex	operating expenditure
RAB	regulatory asset base
STPIS	service target performance incentive scheme
WACC	weighted average cost of capital