



Part of Energy Queensland

4 October 2024

Ms. Stephanie Jolly  
Executive General Manager  
Australian Energy Regulator  
[RITguidelines@aer.gov.au](mailto:RITguidelines@aer.gov.au)

Dear Ms Jolly,

### **2024 cost thresholds review for the regulatory investment test**

Ergon Energy Corporation Limited (Ergon Energy) and Energex Limited (Energex), both distribution network service providers (DNSPs) operating in Queensland, welcome the opportunity to provide a response to the Australian Energy Regulator (AER) on its [2024 cost thresholds review draft determination](#) for the Regulatory Investment Test (RIT) (2024 draft determination).

Cost thresholds have always been a vital component of RITs but its importance has become more apparent in light of the AER's concurrent [2024 Review of the cost benefit analysis and regulatory investment test guidelines](#) which proposes additional obligations on RIT proponents. Thus, it is critical that the methodology employed to reflect changes in thresholds remains fit for purpose by ensuring these keep pace with changes in RIT proponents' costs.

### **Simplification of the current methodology**

In its 2024 draft determination, the AER chose the construction Producer Price Index ( $PPI_{\text{construction}}$ ) for its proxy of RIT proponents' cost increases because it believes the 18.77 percent<sup>1</sup> increase/escalator more accurately reflects changes in network service providers' (NSP) costs, compared to other price indexes it considered.

This escalator was then applied to the unrounded thresholds from the previous review in 2021 and then rounded to produce the 2024 thresholds. We believe this calculation should be simplified by using the 2021 rounded, published values as the starting base values.

This is illustrated in the tables below which shows the outputs of two different threshold escalation methodologies for two DNSPs' thresholds:

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<sup>1</sup> For the three-year period to June 2024.

- **Threshold over which a RIT-D applies (5.15.3(d)(1))**

| Method | Cost Threshold           | Current value (\$m) | 2021 unrounded threshold (\$m) | 2021 rounded threshold (\$m) | Escalator applied (%) | 2024 unrounded threshold (\$m) | Proposed 2024 threshold (\$m) |
|--------|--------------------------|---------------------|--------------------------------|------------------------------|-----------------------|--------------------------------|-------------------------------|
| (A)    | 2024 draft determination | 6                   | 5.57                           | n/a                          | 18.77                 | 7.01                           | 7                             |
| (B)    | Simplified methodology   | 6                   | n/a                            | 6                            | 18.77                 | 7.13                           | 8                             |

In relation to the above two methodologies:

- Method (A) is from Table 5 of the 2024 draft determination<sup>2</sup>; and
- Method (B) applies the PPI<sub>construction</sub> escalator to the 2021 rounded, published threshold (\$6m) which derives the 2024 unrounded threshold of \$7.13m.

Furthermore, we would support this being rounded up to \$8m, given that analysis of Ergon Energy's and Energex's cost increases from 2021 to 2024 have revealed that these have far exceeded the PPI<sub>construction</sub> escalator.

- **Threshold under which the Draft Project Assessment Report (DPAR) can be skipped (5.15.3(d)(3))**

| Method | Cost Threshold           | Current value (\$m) | 2021 unrounded threshold (\$m) | 2021 rounded threshold (\$m) | Escalator applied (%) | 2024 unrounded threshold (\$m) | Proposed 2024 threshold (\$m) |
|--------|--------------------------|---------------------|--------------------------------|------------------------------|-----------------------|--------------------------------|-------------------------------|
| (A)    | 2024 draft determination | 11                  | 11.13                          | n/a                          | 18.77                 | 14.01                          | 14                            |
| (B)    | Simplified methodology   | 12                  | n/a                            | 12                           | 18.77                 | 14.25                          | 15                            |

In relation to the above two methodologies:

- Method (A) is from Table 5 in the 2024 draft determination<sup>3</sup>; and
- Method (B) applies the PPI<sub>construction</sub> escalator to the 2021 rounded, published threshold (\$12m) which derives the 2024 unrounded threshold of \$14.25m.

<sup>2</sup> However, it appears the 2021 unrounded threshold of \$5.57m is incorrect as this appears to be the 2018 unrounded threshold. The correct 2021 unrounded threshold is \$5.90m. See [2021 RIT and APR cost thresholds review, p5](#).

<sup>3</sup> However, it appears the Current value (\$11m) and 2021 unrounded threshold (\$11.13m) are incorrect and should be \$12m and \$11.80m respectively. See [2021 RIT and APR cost thresholds review, p5](#).

For the same reason discussed above, we would support this being rounded up to \$15m. With project costs escalating, a \$15m threshold is more appropriate as a reflection of projects that will benefit from consultation through the publishing of a DPAR.

The use of unrounded 2021 thresholds as the starting base values, adds unnecessary complexity for little gain and this is demonstrated in the above two sets of examples where the 2024 unrounded thresholds are less than two percent between the two different methods.

Alternatively, rather than use the  $PPI_{\text{construction}}$  escalator, the AER may wish to consider a different threshold escalation methodology, which is discussed in further detail below.

### **Alternative methodology**

Compared to the  $PPI_{\text{construction}}$  escalator, we consider using NSPs' Regulatory Information Notice<sup>4</sup> (RIN) data submissions to be a superior input to calculate changes in RITs' thresholds, as these are comprised of actual cost data which is arguably better than the proxy that the  $PPI_{\text{construction}}$  serves.

Furthermore, our assessment of RIN data against the AER's principles which promote the reasonableness of inputs and assumptions<sup>5</sup> is as follows:

- Internal consistency: RIN data is generally consistent each year and across all DNSPs (and Transmission Network Service Providers).
- Plausibility: cost data in the RINs is actual data stemming from NSPs' operations in the market.
- Verifiable sources: RIN data is produced by NSPs in accordance with set definitions and guidelines and is externally audited to ensure consistency and regulatory compliance.
- Relevance: RIN data is produced each year based on market transactions
- Transparency: RIN data is accompanied by basis of preparation explanatory notes that describe how the data was derived.

Should the AER wish to explore RIN data as an alternative to the use of the  $PPI_{\text{construction}}$ , escalator, it could calculate the escalator based on the weighted average change in replacement expenditure assets' unit costs<sup>6</sup> between 2021-22 and 2023-24<sup>7</sup>.

If the AER requires any additional information or wishes to discuss any aspect of this submission, please contact either myself, or Lindsay Chin on 0459 642 052.

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<sup>4</sup> Which will transition to [Annual Information Orders](#) in 2025.

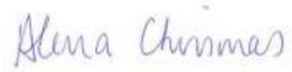
<sup>5</sup> [Guidelines to make the Integrated System Plan actionable](#) AER, October 2023, section 3.2.1.

<sup>6</sup> Using data in Category Analysis RIN Template 2.2 Repex.

<sup>7</sup> 2023-24 data will not be submitted to the AER until late this year, but the AER could request drafts from NSPs.

This submission does not contain confidential information and may be published.

Yours sincerely

A handwritten signature in blue ink that reads "Alena Christmas".

Alena Christmas  
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