



# **DRAFT DECISION**

## **Directlink Transmission Determination 2020 to 2025**

### **Attachment 11 Pricing methodology**

October 2019

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## Note

This attachment forms part of the AER's draft decision on Directlink's 2020–25 transmission determination. It should be read with all other parts of the draft decision.

The draft decision includes the following attachments:

Overview

Attachment 1 – Maximum allowed revenue

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency benefit sharing scheme

Attachment 9 – Capital expenditure sharing scheme

Attachment 10 – Service target performance incentive scheme

Attachment 11 – Pricing methodology

Attachment 12 – Pass through events

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## Shortened forms

Shortened form	Extended form
AARR	aggregate annual revenue requirement
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
ASRR	annual service revenue requirement
MAR	maximum allowed revenue
NEL	national electricity law
NER	national electricity rules
STPIS	service target performance incentive scheme
TNSP	transmission network service provider
TUoS	transmission use of system

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# 11 Pricing methodology

This attachment sets out our draft decision on Directlink's proposed pricing methodology for the 2020–25 regulatory control period.

A pricing methodology forms part of our transmission determination.<sup>1</sup> Its role is to answer the question 'who should pay how much'<sup>2</sup> in order for a transmission business to recover its costs. To do this, a pricing methodology must provide a 'formula, process or approach'<sup>3</sup> that when applied:

- allocates the aggregate annual revenue requirement (AARR) to the categories of prescribed transmission services that a transmission business provides and to the connection points of network users<sup>4</sup>
- determines the structure of prices that a transmission business may charge for each category of prescribed transmission services.<sup>5</sup>

An approved pricing methodology does not relate to negotiated transmission services or other transmission services not subject to economic regulation under the rules.

## 11.1 Draft decision

Our draft decision is to accept Directlink's pricing methodology for the 2020–25 regulatory control period, subject to several editorial amendments.<sup>6</sup> This is because it gives effect to the pricing principles in the national electricity rules (NER) and complies with the information requirements set out in the pricing methodology guidelines.<sup>7</sup>

## 11.2 Directlink's proposal

Directlink's proposed 2020–25 pricing methodology is largely the same as its 2015–20 pricing methodology, with differences being editorial in nature and not substantive.

## 11.3 Assessment approach

We must approve a proposed pricing methodology if satisfied it:

- gives effect to, and complies with, the pricing principles for prescribed transmission services

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<sup>1</sup> NER, cl. 6A.2.2(4).

<sup>2</sup> AEMC, *Rule determination: National Electricity Amendment (Pricing of Prescribed Transmission Services) Rule 2006 No. 22*, 21 December 2006, p. 1.

<sup>3</sup> NER, cl. 6A.24.1(b).

<sup>4</sup> NER, cl. 6A.24.1(b)(1).

<sup>5</sup> NER, cl. 6A.24.1(b)(4).

<sup>6</sup> These editorial changes largely relate to updating or correcting references to the NER, as well as other edits (for example, updating references to relevant regulatory control periods).

<sup>7</sup> NER, cl. 6A.24.1(c).

- complies with information requirements of the pricing methodology guidelines.<sup>8</sup>

Our assessment approach was guided by these requirements along with the pricing methodology Directlink employed, and which we approved, during the 2015–20 regulatory control period.

### 11.3.1 Inter-relationships

There are several transmission network service providers (TNSPs) in the New South Wales (NSW) and Queensland regions.

TransGrid is the appointed Co-ordinating Network Service Provider for the NSW regions (including the Australian Capital Territory, ACT). As the appointed Co-ordinating Network Service Provider, TransGrid applies its pricing methodology to determine the transmission prices to be charged in the NSW region to recover the regulated transmission revenues of Ausgrid, ActewAGL, Directlink and itself in line with clause 6A.29.1 of the NER.<sup>9</sup>

Powerlink is the sole provider of prescribed transmission services in the Queensland region. Powerlink's pricing methodology does not apply to Directlink.<sup>10</sup>

## 11.4 Reasons for draft decision

Our draft decision is to approve Directlink's proposed pricing methodology, subject to several editorial amendments.<sup>11</sup>

We consider Directlink's proposed pricing methodology meets the requirements of the NER pricing principles. The pricing principles are intended to provide scope for transmission businesses to develop pricing arrangements that address the circumstances in which they operate their network.<sup>12</sup>

Much of Directlink's proposal refers to TransGrid's approved pricing methodology for its 2018–23 regulatory control period. We consider it is appropriate for Directlink to adopt aspects of TransGrid's pricing methodology. Directlink's proposed pricing methodology maintains its current pricing arrangement with TransGrid.

As the Co-ordinating Network Service Provider, TransGrid is responsible for allocating all relevant AARR in the NSW region.<sup>13</sup> This includes Directlink's AARR. We approved

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<sup>8</sup> NER, cl. 6A.24.1(c); AER, *Electricity transmission service providers pricing methodology guidelines*, July 2014.

<sup>9</sup> NER, cl. 6A.29; TransGrid, *Pricing Methodology 2018/19 - 2022/23*, 1 December 2017, p. 5.

<sup>10</sup> AER, *Powerlink 2017–22 - Transmission determination - Attachment B - Pricing methodology*, April 2017, p. 5.

<sup>11</sup> We communicated these editorial amendments to Directlink (AER, *Information request #013 – Pricing methodology suggested amendments*, 4 July 2019). Directlink agreed with the amendments and will liaise with the AER in developing its revised proposal (Directlink, *Directlink response to AER Information Request #013*, 10 July 2019).

<sup>12</sup> AEMC, *Rule Determination: National Electricity Amendment (Pricing of Prescribed Transmission Services) Rule 2006 No 22*, 21 December 2006, pp. 27–28.

<sup>13</sup> NER, cl. 6A.29.1(d).

TransGrid's current pricing methodology for the 2018–23 regulatory control period, which did not change from its pricing methodology for the 2013–18 regulatory control period.<sup>14</sup> Directlink's proposal is largely the same as its approved 2015–20 pricing methodology, which makes the same references to the TransGrid pricing methodology. It follows that we consider Directlink's adoption of aspects of TransGrid's proposal is appropriate and contributes to meeting the requirements of the NER pricing principles.

We did not receive any submissions regarding Directlink's proposed pricing methodology.

## Calculation and allocation of the aggregate annual revenue requirement

We assessed Directlink's method for calculating and allocating its AARR, and consider that it meets the NER requirements.

The AARR is the 'maximum allowed revenue' adjusted:

- in accordance with clause 6A.3.2 of the NER, for a number of factors such as cost pass throughs, service target performance incentive scheme outcomes and contingent projects
- by subtracting the operating and maintenance costs expected to be incurred in the provision of prescribed common transmission services.

Table 11-1 summarises our review of how Directlink's proposed pricing methodology calculates and allocates the business's AARR.

**Table 11-1 Directlink's proposed calculation and allocation of the AARR against the NER requirements**

NER requirements	Assessment
Requirement for the AARR to be calculated as defined in the NER—clause 6A.22.1.	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for the AARR to be allocated to each category of prescribed transmission services in accordance with attributable cost share for each such category of service—clause 6A.23.2(a).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for every portion of the AARR to be allocated and for the same portion of AARR not to be allocated more than once—clause 6A.23.2(c).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.

<sup>14</sup> AER, *Final decision: TransGrid transmission determination 2018 to 2023*, May 2018, p. 35; AER, *TransGrid, Revised Revenue Proposal 2018/19 – 2022/23*, 1 December 2017, p. 153; AER, *Draft decision: TransGrid transmission determination 2018 to 2023: Attachment 12 – Pricing methodology*, September 2017, p. 6.



NER requirements	Assessment
Subject to clause 11.6.11 of the NER, requirement for adjusting attributable cost share and priority ordering approach to asset costs that would otherwise be attributed to the provision of more than one category of prescribed transmission services—clause 6A.23.2(d).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.

## Allocation of the ASRR to transmission network connection points

We assessed Directlink's proposed pricing methodology for allocating the annual service revenue requirement (ASRR), and consider it meets the NER requirements. Table 11-2 summarises our assessment.

**Table 11-2 Directlink's proposed allocation of the ASRR against the NER requirements**

NER requirements	AER assessment
Requirement for whole ASRR for prescribed entry services to be allocated to transmission network connection points in accordance with the attributable connection point cost share for prescribed entry services that are provided by the TNSP at that connection point—clause 6A.23.3(i).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for the whole ASRR prescribed exit services to be allocated to transmission network connection points in accordance with the attributable connection point cost share for prescribed exit services that are provided by the TNSP at that connection point—clause 6A.23.3(j).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for the allocation of the ASRR for: <ul style="list-style-type: none"> <li>prescribed TUOS services</li> <li>locational components</li> <li>pre-adjusted non-locational components</li> </ul> —clause 6A.23.3(a).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for adjusting attributable cost share and priority ordering approach to asset costs that would otherwise be attributed to the provision of more than one category of prescribed transmission services—clause 6A.23.2(d).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for the recovery of the ASRR for prescribed common transmission services and the operating and maintenance costs incurred in the provision of those services to be recovered through prices charged to transmission customers and network service and network service provider transmission connection points set in accordance with price structure principles set out in clause 6A.23.4—clause 6A.23.3(h).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.

## Development of price structure

We assessed Directlink's proposed pricing methodology and process for developing different prices for recovering the ASRR, and consider it meets the NER requirements. Table 11-3 sets out the assessment.

**Table 11-3 Directlink's proposed pricing structure against the NER requirements**

NER requirements	AER assessment
Requirement for separate prices for each category of prescribed transmission services—clause 6A.23.4(a).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for fixed annual amount prices for prescribed entry services and prescribed exit services—clause 6A.23.4(g).	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for postage stamped prices for prescribed common transmission services—clause 6A.23.4(f)	Section 2.1 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for prices for locational component of prescribed TUOS services to be based on demand at times of greatest use of the transmission network and for which network investment is most likely to be contemplated—clause 6A.23.4(b)(1).	Section 2.2 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for prices for the locational component of ASRR for prescribed TUOS services not to change by more than 2 per cent per year compared with the load weighted average prices for this component for the relevant region—clause 6A.23.4(b)(2).	Section 2.2 of Directlink's proposed pricing methodology satisfies this requirement.
Requirement for prices for the adjusted non-locational component of prescribed TUOS services to be on a postage stamp basis—clause 6A.23.4(j).	Section 2.3 of Directlink's proposed pricing methodology satisfies this requirement.

## Information requirements

We are satisfied Directlink's proposed pricing methodology, particularly section 2.5, complies with the information requirements of the pricing methodology guidelines.