FINAL DECISION
Evoenergy
Distribution Determination

2019 to 2024

Overview

April 2019

AUSTRALIAN ENERGY REGULATOR

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Note

This Overview forms part of the AER's final decision on the distribution determination that will apply to Evoenergy for the 2019–24 regulatory control period. It should be read with all other parts of the final decision.

As a number of issues were settled at the draft decision stage or required only minor updates, we have not prepared all attachments. The attachments have been numbered consistently with the equivalent attachments to our longer draft decision. In these circumstances, our draft decision reasons form part of this final decision.

In addition to this Overview, the final decision includes the following attachments:

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 9 – Capital expenditure sharing scheme

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Attachment 12 – Classification of services

Attachment 13 – Control mechanisms

Attachment 15 – Alternative control services

Attachment A – Negotiated framework

Attachment B – Pricing methodology

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Shortened forms

Shortened form	Extended form
ACS	Alternative control services
ACT	Australian Capital Territory
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
ANS	Ancillary network services
Augex	Augmentation capital expenditure
Capex	Capital expenditure
CCP/CCP10	Consumer Challenge Panel, sub-panel 10
CESS	Capital expenditure sharing scheme
CPI	Consumer price index
DMIA/DMIAM	Demand management innovation allowance (mechanism)
DMIS	Demand management incentive scheme
DUoS	Distribution use of system
EBSS	Efficiency benefit sharing scheme
ERW	Emergency recoverable works
Evoenergy	The operating name of the energy network division of ActewAGL Distribution partnership, owned equally by Icon Water Limited and Jemena Ltd via subsidiary companies
F&A	Framework and Approach
ICRC	Independent Competition and Regulatory Commission (ACT)
NDSC	Negotiated distribution service criteria
NEL	National Electricity Law
NEM	National Electricity Market
NEO	National Electricity Objective
NER	National Electricity Rules
NGL	National Gas Law
Opex	Operating expenditure
PTRM	Post-tax revenue model
RAB	Regulatory asset base
RBA	Reserve Bank of Australia
Repex	Replacement capital expenditure

Shortened form	Extended form
RFM	Roll forward model
SCS	Standard control services
STPIS	Service target performance incentive scheme
TAB	Tax asset base
TSS	Tariff structure statement

About this decision

The Australian Energy Regulator (AER) works to make all Australian energy consumers better off, now and in the future. We regulate energy networks in all jurisdictions except Western Australia. We set the amount of revenue that network businesses can recover from customers for using these networks.

The National Electricity Law and Rules (NEL and NER) provide the regulatory framework governing electricity transmission and distribution networks. Our work under this framework is guided by the National Electricity Objective (NEO):[1]

> "…to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to—
>
> (a) price, quality, safety, reliability and security of supply of electricity; and
>
> (b) the reliability, safety and security of the national electricity system."

Evoenergy is the electricity distribution network service provider for the Australian Capital Territory (ACT). On 31 January 2018, Evoenergy submitted its regulatory proposal for the 2019–24 regulatory control period, commencing 1 July 2019 to 30 June 2024. We released our draft decision for Evoenergy on 27 September 2018. In response, Evoenergy submitted a revised regulatory proposal on 29 November 2018. Stakeholder consultation on our draft decision and Evoenergy's revised regulatory proposal closed on 11 January 2019. This final decision is released on 30 April 2019.

The key component of our distribution determination for Evoenergy is the total revenue it can recover from customers for the provision of common distribution services (standard control services (SCS)): those used by most, if not all, of Evoenergy's customers.[2] This is our building block determination, and will form the basis of Evoenergy's distribution tariffs for the 2019–24 regulatory control period. Evoenergy's tariff structure statement (TSS) sets out the tariff structure through which it will recover its regulated revenue for SCS from customers.

Evoenergy also provides alternative control services (ACS), the costs of which are recovered from users of those services only, through a capped price on the individual service. These costs are considered separately to our revenue determination. We discuss Evoenergy's ACS in Attachment 15 to this final decision. Evoenergy has not

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1 NEL, s. 7.

2 Evoenergy's proposal also includes revenue for its dual function (transmission) assets, which will be recovered through TransGrid as the coordinating transmission network service provider for NSW.

proposed to provide any services on a negotiated basis in the 2019–24 regulatory control period.[3]

Evoenergy's distribution business operates dual function assets, which are high-voltage transmission assets forming part of a distribution network.[4] Our framework and approach decision established that we would apply transmission pricing rules to Evoenergy's dual function assets.[5] A transmission pricing methodology forms part of our regulatory determination for Evoenergy (section 5.5).[6]

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3 Our distribution determination for Evoenergy includes an approved negotiating framework and negotiated distribution service criteria, as required by the NER. Because Evoenergy has not included any negotiated services in its proposal, these elements of our determination will be inactive for the 2019–24 regulatory control period.

4 ActewAGL Distribution, *Response to preliminary framework and approach, Regulatory control period commencing 1 July 2019*, April 2017. (Evoenergy was then known as ActewAGL.)

5 AER, *Framework and approach, ActewAGL Regulatory control period commencing 1 July 2019*, July 2017.

6 NER, cl. 6A.2.2(4).

1 Our final decision

Our final decision allows Evoenergy to recover $851.4 million ($ nominal, smoothed) from its customers for the 2019–24 regulatory control period, commencing 1 July 2019 to 30 June 2024.

As a result of this decision, the cost of electricity distribution network services in the ACT will be around 9.0 per cent ($ nominal) higher on average by 30 June 2024 compared to the current level.

Distribution network costs represent around 27 per cent of total electricity bills on average in the ACT.[7] As a result of this decision, the average annual electricity bill for a residential or small business customer on Evoenergy's network is estimated to be around 2.5 per cent ($ nominal) higher by 30 June 2024 compared to the current level, holding all other components of the bill constant.

This outcome is $20.0 million ($ nominal, smoothed) lower than our draft decision, and $76.6 million ($ nominal, smoothed) lower than Evoenergy's revised proposal. Having assessed Evoenergy's revised proposal, we consider our final decision is justified as it:

- builds on the operational efficiencies Evoenergy has achieved in response to our lower approved revenues for the current 2014–19 regulatory control period and locks in ongoing efficiency gains for future regulatory control periods for the benefit of customers
- is balanced against additional capital investment required by Evoenergy to maintain network safety and reliability for its customers.

Increased efficiency

This final decision for the upcoming 2019–24 regulatory control period continues the momentum built up over the current 2014–19 period as Evoenergy has become more efficient and more customer focused, so it is better able to provide the services consumers want at the price they value. The amount of revenue Evoenergy could recover from its customers fell from $913 million ($2018–19, smoothed) for the 2009–14 regulatory control period to $845.4 million ($2018–19)[8] for the 2014–19 period (a 7.4 per cent reduction).

The 2014–19 determination challenged Evoenergy to not only deliver network services more efficiently to its customers through prudent and efficient operating and capital expenditures, but to do so without compromising network safety and reliability.

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7 Including Evoenergy's dual function assets.

8 Based on the 2014–19 remade final decision.

In response, Evoenergy rationalised its business operations commensurate with lower recoverable revenues for 2014–19[9]. Over the past five years, we have seen Evoenergy continue to improve its efficiency through a range of measures, including a 24 per cent reduction in staffing levels.

Today, Evoenergy has become a more efficient network service provider that is at the forefront of transitioning to cost reflective pricing, with capability to operate and deliver network services from a lower revenue base — as evidenced by this final decision which accepts Evoenergy's revealed operating expenditure (opex) as a starting point for its forecast expenditure for the next five years. These savings are now locked in for consumers.

This final decision approves opex of $295.8 million ($2018–19) for the 2019–24 regulatory control period, which is $6.2 million (2.1 per cent) lower than proposed by Evoenergy in its revised proposal as it did not include the minimum 0.5 per cent per year forecast opex productivity growth that we apply in our determinations, and $11.6 million (3.9 per cent) higher than for the 2014–19 period.

In terms of capital expenditure (capex), we accept a total net capex of $314.3 million ($2018–19) for the 2019–24 regulatory control period, which is the same as proposed by Evoenergy in its revised proposal and $8.9 million (2.8 per cent) lower than for the 2014–19 period. This is reflected in the downward trend in Evoenergy's regulatory asset base (RAB) over the next five years as it works to explore and adopt more efficient capital investment strategies.

Listening to customers

As well as increasing efficiency to drive lower costs, Evoenergy has also improved its approach to consumer engagement, though more can be done.

Through its engagement, it is clear that predictability and certainty with respect to price changes is a priority for Evoenergy's customers. Energy affordability remains a key concern for many. At the same time, customers have told Evoenergy to:[10]

- maintain safety, quality, reliability and security of supply
- strike the right cost/reliability trade-off when investing in the network
- support new technology and the role it plays in the future of the electricity network, including the potential to provide innovative solutions and cost reflective outcomes
- support customers as they transition to more cost reflective pricing under the proposed refinements to Evoenergy's tariff structure statement (TSS).

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9 Adding further uncertainty to this environment would have been Evoenergy's legal challenge to the lower revenue we had approved for it for the 2014–19 regulatory control period. This matter was finalised in November 2018 following publication of our 2014–19 remade final decision (remittal) for Evoenergy, after our 2015 final decision was set aside.

10 Evoenergy-Attachment 2 Consumer engagement-January 2018_Public, pp. 2–11 - 2–12.

Our September 2018 draft decision for Evoenergy noted that in a number of respects, our decision agreed with it on the key drivers identified through its earlier stakeholder engagement as influencing its revenue requirement for the 2019–24 regulatory control period. However, we required further information in a few areas before we could accept Evoenergy's regulatory proposal.

Since our draft decision and prior to Evoenergy lodging its 2019–24 revised proposal in November 2018, Evoenergy has supplied additional information to us and consumer groups to narrow or eliminate the key areas of contention following our draft decision.

This is a clear example of the value to a network service provider from a comprehensively designed and well implemented consumer engagement program — in terms of successful passage through the regulatory determination process with a high degree of support from its stakeholders.

We are encouraged by the increasing number of network service providers that are devoting more resources to their respective consumer engagement programs, including greater emphasis on 'deep dive' workshops as part of their pre-lodgement engagement initiatives. Another positive development is the commitment of several network service providers to maintaining an open and ongoing dialogue with stakeholders throughout the regulatory control period, as opposed to engaging intensively once every five years when a regulatory proposal is being considered. By keeping the conversation going, constructive discussions around key and contentious issues could be had well before a regulatory proposal is finalised and submitted to us, with further possible refinements aired as part of our subsequent public consultation processes.

Helping to keep Evoenergy focussed during this regulatory determination process have been several consumer groups, including Evoenergy's Energy Consumer Reference Council (ECRC) and the ACT Energy Consumers Policy Consortium (ECPC).[11] We are especially appreciative of our Consumer Challenge Panel (CCP10) for their strong engagement and commitment to obtaining beneficial outcomes for consumers. Their enduring commitment not only challenges network service providers to consider alternative options for the delivery of services at least cost to consumers, but also challenges us in terms of testing the robustness of our decisions. For example, consumer groups played a key role in helping to resolve Evoenergy's 2014–19 remittal, and also advocated strongly for a more thorough consideration of the approach to forecasting opex productivity growth in our regulatory determinations — a matter we have addressed in this final decision for Evoenergy.

While an improvement on previous efforts, Evoenergy could have taken better advantage of the opportunity it had following our draft decision to more clearly

[11] The ACT Energy Consumers Policy Consortium is comprised of representatives of the ACT Council of Social Service (ACTCOSS), Care Financial Counselling Service, the Conservation Council ACT Region, SEE-Change and the Small Business Taskforce of the Canberra Business Chamber. ACTCOSS, the Canberra Business Chamber and SEE-Change are also members of Evoenergy's Energy Consumer Reference Council.

demonstrate in its 2019–24 revised proposal how it had undertaken additional engagement with consumer groups to further refine its regulatory proposal, particularly in respect of some of its capex requirements and its approach to forecasting opex productivity growth. General feedback on Evoenergy's engagement approach from consumer groups suggests that not only is more meaningful engagement required earlier in the regulatory process (such as part of 'deep dive' workshops), but Evoenergy also needs to maintain the strong momentum it had achieved by the midway point with its consumer engagement right through to the end of the regulatory determination process. Such an approach may have helped Evoenergy to further enhance consumer groups' perception of its revised proposal.

What the decision means

Looking ahead, we estimate our 2019–24 final decision would mean that by the end of the 2019–24 regulatory control period (as at 30 June 2024):

- average distribution network tariffs would increase by around 9.0 per cent ($ nominal) for Evoenergy compared to the 2018–19 level (as at 30 June 2019)
- average annual electricity bills would increase by around 2.5 per cent ($ nominal) for residential or small business customers on Evoenergy's distribution network compared to the 2018–19 level (as at 30 June 2019), holding all other components of the bill constant.[12] This suggests that average annual bills would be around $64 and $231 higher for residential and small business customers, respectively.

In making this final decision, we have had regard to a range of sources including Evoenergy's revised proposal, submissions received as well as additional analysis undertaken and published by us. We are satisfied that the revenue we have determined that Evoenergy can recover from its customers for the 2019–24 regulatory control period is in the long-term interests of consumers and that its customers are paying no more than they should for safe and reliable electricity.

Other relevant decisions

This final decision incorporates the outcomes of three reviews progressed in parallel to our consideration of Evoenergy's 2019–24 regulatory proposal, namely:

- 2018 rate of return guideline review:[13] We released our final decision on this review on 17 December 2018. Legislative amendments to the National Electricity Law (NEL) and National Gas Law (NGL) that established the guideline as a binding instrument were made on 13 December 2018. As the instrument is binding, we have determined a rate of return using the approach set out in the instrument.

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[12] We estimate the expected bill impact by varying the distribution and transmission network charges in accordance with our final decision, while holding all other components constant. This approach isolates the effect of our final decision on the core distribution and transmission network charges, and does not imply that other components will remain unchanged across the regulatory control period.

[13] AER, *Rate of return instrument*, 17 December 2018.

- Regulatory tax approach review:[14] We released our final report on this review on 17 December 2018. Our post-tax revenue model (PTRM) has been updated to implement the findings from this review, allowing for immediate expensing of forecast capex and applying the diminishing value method to calculate the tax depreciation for new assets.[15]
- Approach to forecasting opex productivity growth for electricity distributors review:[16] We released our final decision on 8 March 2019. Productivity growth is one element in the trend component of our opex forecasting approach. Our forecast of productivity growth is intended to capture the efficiency improvements distributors can make in providing distribution services. In our review, we determined that a prudent electricity distributor, acting efficiently, can achieve opex productivity growth of 0.5 per cent each year. We have applied this finding in our 2019–24 final decision for Evoenergy.

Our 2019–24 final decision also incorporates the revenue impact of the finalised remittal. In 2015, Evoenergy (formerly ActewAGL Distribution) appealed the 2014–19 revenue allowance we determined for it. In turn, the Australian Competition Tribunal set aside, and directed us to remake, our decision for Evoenergy. We remade our 2014–19 final decision in November 2018 following receipt of Evoenergy's remittal proposal in July 2018.[17] Key consumer groups, including our CCP10, were supportive of Evoenergy's remittal proposal and our decision. Evoenergy will return an estimated $0.9 million ($2018–19) to customers from 1 July 2019, being the difference between what it recovers under interim tariff undertakings and the 2014–19 revenue we approved in our remittal final decision.

1.1 What is driving revenue?

The changing impact of inflation over time makes it difficult to compare revenue from one period to the next on a like-for-like basis. To do this we use 'real' values based on a common year (in this case 2018–19[18]), which have been adjusted for the impact of inflation.

In real terms, the total revenue allowance in this 2019–24 final decision is 6.3 per cent lower than the allowed revenue in our 2014–19 remade final decision. Figure 1 shows real revenues decrease by 3.6 per cent from 2018–19 to 2019–20, followed by gradual annual increases of around 0.5 per cent.

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14 AER, *Final report – Review of regulatory tax approach*, 17 December 2018.

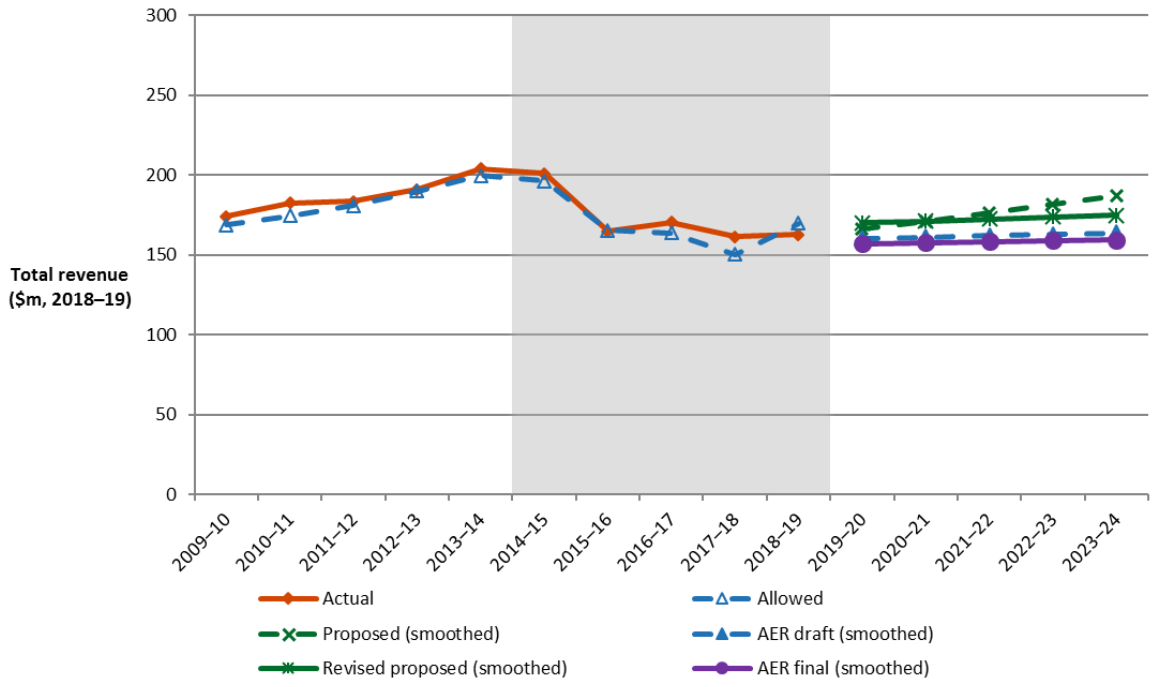
15 AER, *Distribution PTRM (version 4)*, April 2019.

16 AER, *Final decision – Forecasting productivity growth for electricity distributors*, 8 March 2019.

17 AER, *Final decision – Evoenergy 2014–19 distribution determination*, November 2018.

18 That is, 30 June 2019 dollar terms, based on Evoenergy's estimated actual revenue for 2018–19.

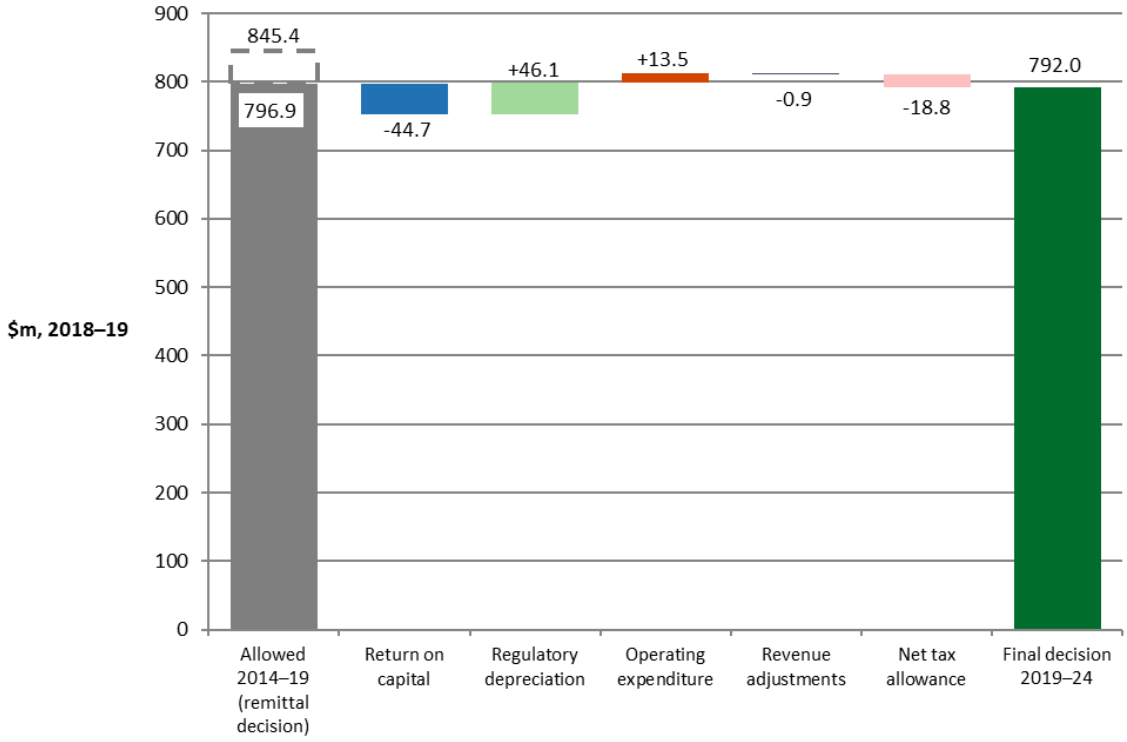
Figure 1 Revenue over time – distribution and transmission ($ million, 2018–19)



Source: AER analysis.

Figure 2 highlights the key drivers of the real change in Evoenergy's revenues from the current 2014–19 regulatory control period to this 2019–24 final decision, by reference to the revenue 'building blocks' that form the basis of our assessment.

Figure 2 Change in revenue from 2014–19 to 2019–24 – distribution and transmission ($m, 2018-19)



Note: 'Allowed 2014–19 (remittal decision)' shows an additional $48.6 million (dashed grey outline) on top of the $796.9 million total. The $796.9 million is the sum of the revenue building blocks in the remittal PTRM, and incorporates some of the remittal changes including expected inflation, return on debt updates and opex. The additional $48.6 million represents further changes in the remittal PTRM calculations including: yield calculation (updated for actual volumes), service target performance financial incentives, negotiated cap settlement amounts and difference in CPI adjustments.[19]
'Revenue adjustments' include increments/decrements accrued under incentives schemes, such as the capital expenditure sharing scheme (CESS) and demand management innovation allowance mechanism (DMIAM).

Source: AER analysis.

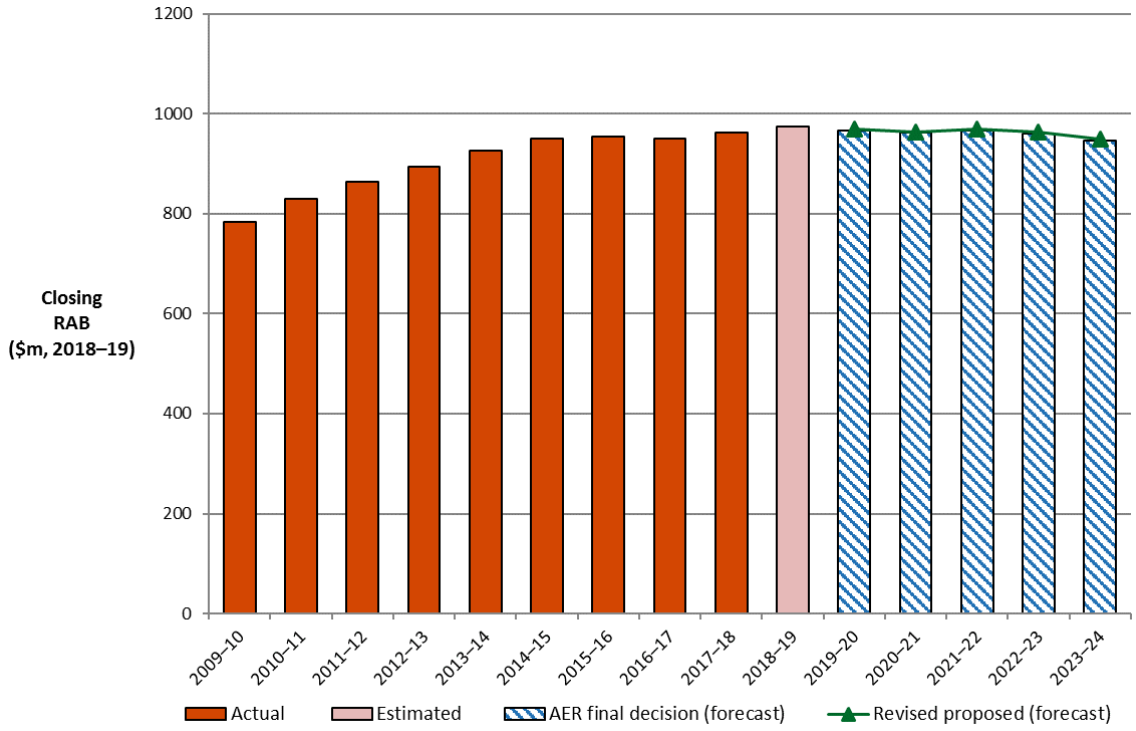
The return on capital (the product of the size of Evoenergy's RAB and the allowed rate of return) is one of the largest components of Evoenergy's regulated revenue. The return on capital under this final decision is lower than that for the current 2014–19 regulatory control period due to a lower rate of return.

In addition to the lower rate of return on the RAB, the size of Evoenergy's RAB is also reducing in real terms. After significant growth in the 2009–14 regulatory control period,

[19] Building block revenues are converted from nominal to real $2018-19 using both forecast and actual CPI, the 'Allowed 2014-19 (remittal draft decision)' amount is converted from nominal to real $2018-19 only using actual CPI.

Evoenergy's RAB is expected to reduce in size by a projected 2.9 per cent ($2018–19) under this final decision. This is illustrated in Figure 3.

Figure 3 Value of Evoenergy's RAB over time – distribution and transmission ($ million, 2018–19)



Source: AER analysis.

Note: Includes distribution and dual function (transmission) assets.

This lower return on capital is helping to offset the impact of an increase in the regulatory depreciation allowance (return of capital) component of our final decision on revenue. One of the key reasons Evoenergy's regulatory depreciation allowance is increasing is the nature of its capex in the current 2014–19 regulatory control period, reflecting Evoenergy's increased focus on customer service outcomes and network capabilities to open the way for greater penetration of distributed energy resources. This is one of the priorities identified in its discussions with consumers.

The information and communications technology (ICT) assets that Evoenergy invested in to deliver on these priorities have relatively short asset lives. This means they are depreciated (removed from the RAB as assets come to the end of their usefulness) over a relatively shorter period of time compared to 'poles and wires' (which have asset lives of 50 years or more). In the 2019–24 period, this is driving an increase in the regulatory depreciation allowance. The balancing effect of this is that depreciation of the RAB is helping to offset the addition of new assets to the RAB as Evoenergy's investment in other parts of its network continues. As noted above, the size of Evoenergy's RAB is expected to reduce in real terms from 1 July 2019 to 30 June 2024.

The other element of Evoenergy's revenue that is expected to increase in the 2019–24 regulatory control period is its opex. The significant opex efficiencies in labour and workforce practices Evoenergy achieved in 2014–19 — one of the benefits of its ICT investment — are expected to be maintained, and have been passed through to customers, in this 2019–24 final decision in the form of a lower opex base year.

Although total opex is increasing, this is to allow for additional efficient and prudent expenditure to meet Evoenergy's expanded responsibilities for vegetation management under the *Utilities (Technical Regulation) Amendment Act 2017* (ACT), which took effect from 1 July 2018. It also reflects expected increases in input costs, including the cost of labour, and the costs of operating a larger network with more customers connected.

The combined effect of a lower return on capital, and higher regulatory depreciation and opex allowances, means that our final decision on Evoenergy's total revenue for the 2019–24 regulatory control period is 6.3 per cent lower ($2018–19) compared to the 2014–19 period.

1.2 Key differences between our final decision and Evoenergy's revised proposal

While the total revenue in this 2019–24 final decision shares many of the same drivers that informed Evoenergy's revised proposal, our final decision does not allow the total revenue proposed by Evoenergy. Total revenue approved in this 2019–24 is final decision is $76.6 million ($ nominal) or 8.3 per cent lower than proposed by Evoenergy.

The biggest contributor to the difference between our 2019–24 final decision and Evoenergy's revised proposal is our change to the rate of return (and therefore the return on capital and tax).

As required under the NER, we have applied the 2018 Rate of Return Instrument (2018 Instrument) and estimate an allowed rate of return of 5.53 per cent (nominal vanilla).[20]

Our final decision also applies a value of imputation credits (gamma) of 0.585 as per the binding 2018 Instrument.[21] We do not accept Evoenergy's revised proposal of 0.4 for gamma.[22]

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[20] See https://www.aer.gov.au/networks-pipelines/guidelines-schemes-models-reviews/rate-of-return-guideline-2018/final-decision. The legislative amendments to replace the (previous) non-binding Rate of Return Guidelines with a binding legislative instrument were passed by the South Australian Parliament in December 2018. See, Statutes Amendment (National Energy Laws) (Binding Rate of Return Instrument) Act 2018 (SA). NGL, Chapter 2, Part 1, division 1A; NEL, Part 3, division 1B.

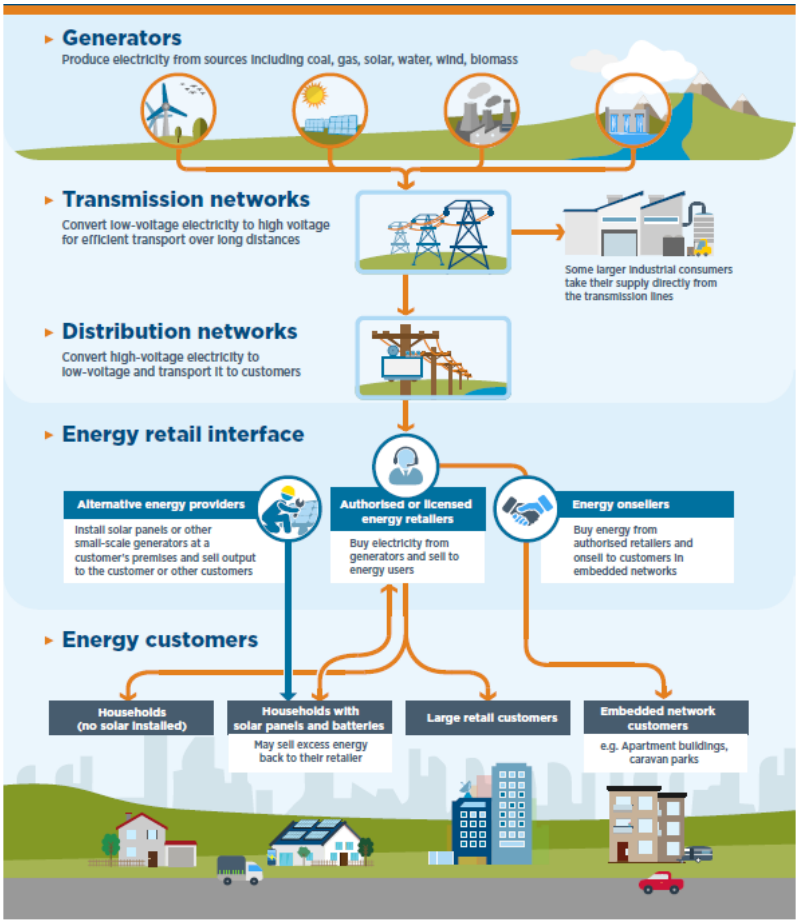
[21] AER, *Rate of return instrument*, December 2018, clause 27.

[22] Evoenergy, *Revised regulatory proposal ACT electricity distribution network 2019–24*, November 2018, p. 63.

1.3 Expected impact of our final decision on electricity bills?

The distribution network tariffs that will be set by reference to our final decision are only one contributor to electricity bills, and make up around 27 per cent of the total retail electricity bills Evoenergy's customers pay. Other components of the electricity bill include environmental policy costs, wholesale electricity costs and retail costs. Figure 4 illustrates the different components of the electricity supply chain. Each of these costs contributes to the retail prices charged to customers by their chosen electricity retailer.

Figure 4 Electricity supply chain



Source: AER, *State of the Energy Market*, December 2018, p. 28.

In the ACT, the Independent Competition and Regulatory Commission (ICRC) sets a default (standing offer) retail price for ActewAGL Retail.[23]

[23] ICRC, *Report 6 of 2017: Final Report - Standing Offer Prices for the Supply of Electricity to Small Customers from 1 July 2017 - June 2017*.

Table 1 shows the estimated average annual impact of our final decision for the 2019–24 regulatory control period on electricity bills for residential and small business customers. These estimates suggest a 2.5 per cent ($ nominal) increase over the five-year 2019–24 regulatory control period.

We estimate the expected bill impact by varying the distribution charges in accordance with our 2019–24 final decision, while holding all other components constant. This approach isolates the effect of our final decision on core distribution and transmission network tariffs from other parts of the bill. However, this does not imply that other components will remain unchanged across the regulatory control period.[24]

We expect the impact of our 2019–24 final decision would increase the average annual residential electricity bill by 2023–24 by around $64 or 2.5 per cent ($ nominal) from the current 2018–19 level. Had we accepted Evoenergy's revised proposal, the expected impact would have been a larger increase of around $137 or 5.3 per cent.

Similarly, for an average small business customer on Evoenergy's network, we expect the average annual electricity bill by 2023–24 to increase by around $231 or 2.5 per cent ($ nominal) from the current 2018–19 level. Again, had we accepted Evoenergy's revised proposal, the expected impact would have been a larger increase of around $495 or 5.3 per cent.

[24] It also assumes that actual energy consumption will equal the forecast adopted in our final decision. Since Evoenergy operates under a revenue cap, changes in energy consumption will also affect annual electricity bills across the 2019–24 regulatory control period.

Table 1 Estimated contribution to annual electricity bills for the 2019–24 regulatory control period ($ nominal)

	2018–19	2019–20	2020–21	2021–22	2022–23	2023–24
AER final decision						
Residential annual bill[a]	2580	2560	2565	2588	2614	2644
Annual change[c]		–20 (–0.8%)	5 (0.2%)	24 (0.9%)	25 (1%)	30 (1.2%)
Small business annual bill[b]	9320	9248	9265	9350	9442	9551
Annual change[c]		–72 (–0.8%)	18 (0.2%)	85 (0.9%)	92 (1%)	109 (1.2%)
Evoenergy's revised proposal						
Residential annual bill[a]	2580	2618	2625	2653	2682	2717
Annual change[c]		38 (1.5%)	7 (0.3%)	27 (1%)	30 (1.1%)	35 (1.3%)
Small business annual bill[b]	9320	9458	9484	9582	9689	9815
Annual change[c]		138 (1.5%)	25 (0.3%)	99 (1%)	107 (1.1%)	126 (1.3%)

Source: AER analysis; AER, Energy Made Easy website; AEMC *2017-Residential-Electricity-Price-Trends, ICRC final report on standing offer prices for the supply of electricity to small customers from 1 July 2017; ICRC, Retail electricity price recalibration 2018–19,* June 2018.

(a) Annual bill for 2018–19 is sourced from Energy Made Easy and reflects the average consumption of 8,000 kWh for residential customers in ACT (postcode 2600).

(b) Annual bill for 2018–19 is sourced from Energy Made Easy and reflects the average consumption of 25,000 kWh for small business customers in ACT (postcode 2600).

(c) Annual change amounts and percentages are indicative. They are derived by varying the network tariff contribution to the 2018–19 bill amounts in proportion to yearly expected revenue for network services, divided by AEMO's forecast energy delivered for NSW/ACT for transmission and forecast energy for distribution as proposed by Evoenergy. Actual bill impacts will vary depending on electricity consumption and tariff class.

1.4 Evoenergy's consumer engagement

The NEO puts the long-term interests of consumers at the centre of our decisions as a regulator and the way Evoenergy operates its network. An important part of this is ensuring the regulatory proposal Evoenergy puts to us for approval reflects the NEO, and that Evoenergy has engaged with its consumers to determine how best to provide services that align with their long-term interests.

Consumer engagement in this context is about Evoenergy working openly and collaboratively with consumers and providing opportunities for their views and preferences to be heard and to influence Evoenergy's decisions. In the regulatory process, stronger consumer engagement can help us test service providers' expenditure proposals, and can raise alternative views on matters such as service priorities, capex and opex proposals and tariff structures.

Our impression is that Evoenergy's consumer engagement processes, including its increased efforts to engage with consumers prior to submission of its initial regulatory proposal in January 2018, have improved significantly in recent years.

According to Evoenergy, its engagement program for its 2019–24 regulatory proposal was developed in 2016 and:[25]

> "…has guided activities that provided stakeholders from a range of consumer groups input to Evoenergy's electricity network five-year plan."

This engagement has been instrumental in identifying the key themes that have informed its 2019–24 initial and revised regulatory proposals. Summary tables throughout Evoenergy's initial proposal set out how, in each element of that proposal, Evoenergy sought to work with and respond to the key themes identified through its engagement.

In developing its 2019–24 initial and revised regulatory proposals, Evoenergy's consumer engagement has utilised a variety of engagement techniques and mediums, including:

- issues and discussion papers
- consumer forums
- consumer surveys
- bi-monthly engagement with the Evoenergy ECRC[26]
- 'deep dive' workshops with consumers and other key stakeholders.

Evoenergy's consumer engagement in the preparation of its 2019–24 initial and revised regulatory proposals has generally been well received by stakeholders, but there is room for ongoing improvement, particularly in terms of embedding consumer engagement into business-as-usual operations.

As our CCP10 observed:

> "…Evoenergy has been proactive in seeking consumer input to the key aspects of their regulatory proposal, in seeking to resolve the outstanding matters from 2014–19 and has demonstrated significant goodwill with both consumers and the Regulator and the processes culminated in their Revised Revenue Proposal."[27]

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25 Evoenergy, *Attachment 2 Consumer engagement-January 2018_Public*, pp. 2–1.

26 Membership of the Evoenergy Energy Consumer Reference Council (ECRC) includes: an independent Chair, ACT Council of Social Service (ACTCOSS), Council of the Ageing (COTA), Gungahlin Community Council, Tuggeranong Community Council, Canberra Business Chamber, SEE-Change Inc., Property Council of Australia (ACT), Master Builders Association of the ACT (MBA), Engineers Australia, Australian National University (ANU), and Canberra Urban and Regional Futures (CURF).

27 CCP, *CCP10 Response to the Evoenergy Revised Regulatory Proposal 2019-24 and AER draft determination*, January 2019, p. 23.

> "When considering our initial three questions for assessing consumer engagement, we observed that Evoenergy has become more confident in trying a range of consumer engagement approaches, they recognise the value of hearing what consumers say and have heard a considerable amount of what consumers told them. However, their practice in applying consumer engagement into the day-to-day operation of the business is still work in progress."[28]

Overall, CCP10 considered Evoenergy's revised proposal as a missed opportunity to fully reflect the feedback it had received from the AER and CCP10:[29]

> "The AER also encouraged Evoenergy to respond to the concerns that were raised in the Draft Decision, prompting us to encourage Evoenergy to 'tell the narrative'…
>
> Despite strong engagement with CCP10, its ECRC and other stakeholders before lodging the Revised Proposal – strong consumer engagement is not reflected in those plans.
>
> The Revised Proposal is not capable of acceptance…
>
> At its recent best, Evoenergy's consumer engagement has been of a high standard and the ECRC provides a very sound base for ongoing engagement."

Evoenergy's ECRC was supportive of Evoenergy's consumer engagement approach:[30]

> "Commencing with ECRC meeting 13 in August 2016, through to meeting 26 in December 2018, the 2019–24 determination has been a key topic at virtually all ECRC meetings, with extensive briefings and updates by Evoenergy management and ample opportunity for our community representatives to ask questions of the organisation and to provide feedback on their proposal…
>
> We are of the view that Evoenergy has made great progress in their genuine commitment to consumer engagement in the past four years and their acceptance of feedback from our ECRC members has been extremely encouraging. We believe the ECRC is a very representative body on behalf of ACT energy consumers and our members are generally very supportive of Evoenergy's revised regulatory proposal for the 2019–24 period."

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28 CCP, *CCP10 Response to the Evoenergy Revised Regulatory Proposal 2019-24 and AER draft determination*, January 2019, pp. 27–28.

29 CCP, *CCP10 Response to the Evoenergy Revised Regulatory Proposal 2019-24 and AER draft determination*, January 2019, p. 46.

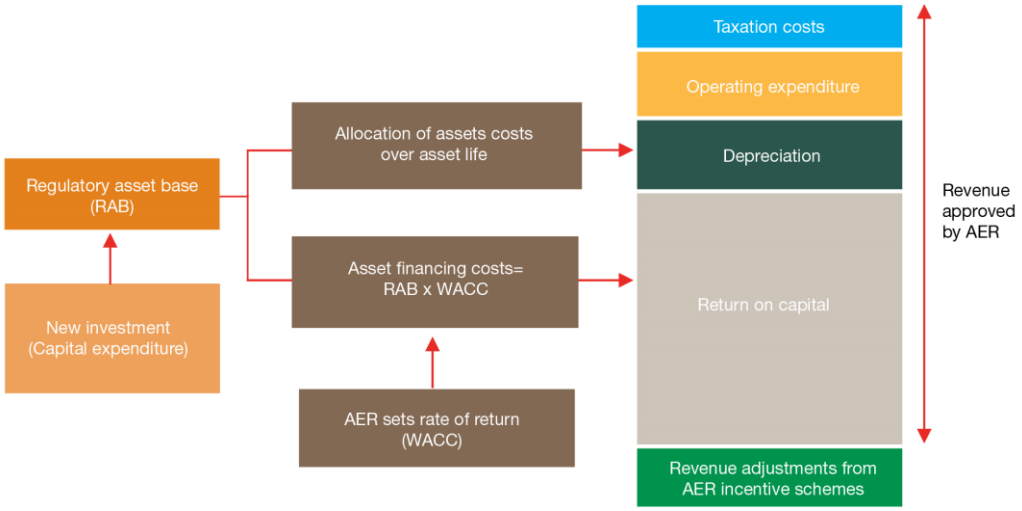
30 Evoenergy ECRC, *Public Submissions – Evoenergy 2019–24 Draft Electricity Determination*, January 2019, pp. 2-3.

2 Key components of our final decision on revenue

The total revenue Evoenergy has proposed reflects its forecast of the efficient cost of providing network services over the 2019–24 regulatory control period. Evoenergy's revised proposal, and our assessment of it under the NEL and NER, are based on a 'building block' approach to determining a total revenue allowance which looks at five cost components (see Figure 5):

- return on the RAB (or return on capital, to compensate investors for the opportunity cost of funds invested in the business)
- depreciation of the RAB (or return of capital, to return the initial investment to investors over time)
    - The forecast capex approved in our decisions affects the projected size of the RAB and therefore the revenue generated from the return on capital and depreciation building blocks.
- forecast opex (the operating, maintenance and other non-capital expenses incurred in the provision of network services)
- revenue adjustments (including revenue increments/decrements resulting from the application of incentive schemes)
- estimated cost of corporate income tax.

Figure 5 The building block model to forecast network revenues



Source: AER 2018 State of the Energy Market report.

We use an incentive approach where, once regulated revenues are set for a five-year period, networks who keep actual costs below the regulatory forecast of costs retain part of the benefit. This benchmark incentive framework is a foundation of our regulatory approach and promotes the delivery of the NEO. Service providers have an incentive to become more efficient over time, as they retain part of the financial benefit

from improved efficiency. Consumers also benefit when efficient costs are revealed and a lower cost benchmark is set in subsequent regulatory periods.

In the sections below, we discuss the key components of our final decision on Evoenergy's revenue for the 2019–24 period in turn.

2.1 Regulatory asset base

The regulatory asset base (RAB) is the value of assets used by Evoenergy to provide regulated distribution and transmission network services. The value of the RAB substantially impacts Evoenergy's revenue requirement and the price consumers ultimately pay. This makes it a key issue for many stakeholders. Other things being equal, a higher RAB would increase both the return on capital and regulatory depreciation (return of capital) components of the revenue determination.

As part of our decision on Evoenergy's revenue for 2019–24, we make a decision on Evoenergy's opening RAB as at 1 July 2019 for its distribution and transmission (dual function assets) networks.[31] We use the RAB at the start of each regulatory year to determine the return on capital and regulatory depreciation (return of capital) building block allowances.

For our 2019–24 final decision, we have determined:

- opening RAB values of $796.0 million and $177.3 million ($ nominal) as at 1 July 2019 for Evoenergy's distribution and transmission networks, respectively.
- forecast closing RAB values of $892.5 million and $173.0 million ($ nominal) as at 30 June 2024 for Evoenergy's distribution and transmission networks, respectively.

We accept Evoenergy's revised proposed opening RABs, subject to the following revisions:

- update the 2018–19 inflation rate with the actual consumer price index (CPI) input for indexation in the RAB roll forward
- update the 2017–18 capex and disposals for amended asset allocations.

The key differences between the forecast RAB outcome in our final decision and Evoenergy's revised proposal are:

- our related final decisions on:
    - opening RAB values as at 1 July 2019, as discussed above
    - forecast capex for the 2019–24 period (section 2.4)
    - forecast regulatory depreciation for the 2019–24 period (section 2.3)

[31] NER, cl. 6.12.1(6). Evoenergy's dual function assets are high-voltage assets which support the broader NSW transmission network owned and operated by TransGrid. We apply transmission pricing to these assets.

- updates to the estimation of inflation to reflect the most recent data from the Reserve Bank of Australia (RBA). Our final decision applies a lower inflation rate of 2.42 per cent compared to 2.45 per cent in Evoenergy's revised proposal (section 2.2).

Table 2 and Table 3 set out our final decision on the forecast RAB values for Evoenergy over the 2019–24 regulatory control period. Further details on Evoenergy's RAB can be found in Attachment 2.

Table 2 AER's final decision on Evoenergy's RAB for the 2019–24 regulatory control period – distribution ($ million, nominal)

	2019–20	2020–21	2021–22	2022–23	2023–24
Opening RAB	**796.0**	**816.2**	**830.3**	**861.3**	**880.7**
Capital expenditure[a]	56.1	52.8	73.0	65.2	60.6
Inflation indexation on opening RAB	19.3	19.8	20.1	20.9	21.4
Less: straight-line depreciation	55.2	58.5	62.1	66.7	70.1
Closing RAB	**816.2**	**830.3**	**861.3**	**880.7**	**892.5**

Source: AER analysis.

(a) Net of forecast disposals and capital contributions. In accordance with the timing assumptions of the PTRM, the capex includes a half-year weighted average cost of capital (WACC) allowance to compensate for the six month period before capex is added to the RAB for revenue modelling.

Table 3 AER's final decision on Evoenergy's RAB for the 2019–24 regulatory control period – transmission ($ million, nominal)

	2019–20	2020–21	2021–22	2022–23	2023–24
Opening RAB	**177.3**	**174.3**	**178.0**	**177.6**	**175.3**
Capital expenditure[a]	3.5	10.9	7.4	6.4	7.0
Inflation indexation on opening RAB	4.3	4.2	4.3	4.3	4.3
Less: straight-line depreciation	10.9	11.4	12.2	13.0	13.6
Closing RAB	**174.3**	**178.0**	**177.6**	**175.3**	**173.0**

Source: AER analysis.

(a) Net of forecast disposals and capital contributions. In accordance with the timing assumptions of the PTRM, the capex includes a half-year weighted average cost of capital (WACC) allowance to compensate for the six month period before capex is added to the RAB for revenue modelling.

2.2 Rate of return and value of imputation credits

The return each business is to receive on its RAB (the 'return on capital') continues to be a key driver of proposed revenues. We calculate the regulated return on capital by applying a rate of return to the value of the RAB.

We estimate the rate of return by combining the returns of the two sources of funds for investment: equity and debt. The allowed rate of return provides the business with a return on capital to service the interest on its loans and give a return on equity to investors.

An accurate estimate of the rate of return is necessary to promote efficient prices in the long-term interests of consumers. If the rate of return is set too low, the network business may not be able to attract sufficient funds to be able to make the required investments in the network and reliability may decline. Conversely, if the rate of return is set too high, the network business may seek to spend too much and consumers will pay inefficiently high tariffs.

In December 2018, the NEL and NGL were amended to require us to make a binding rate of return instrument. As a binding instrument, it sets out the methodology for calculating the rate of return. The method must be capable of automatic application to all regulated network service providers without the exercise of discretion. The 2018 Rate of Return Instrument (2018 Instrument) specifies the return on debt as a formula, being the trailing average portfolio approach, and requires a business that is not already using a trailing average to transition to it over a 10-year period that is in the future.

As required under the NER, we have applied the 2018 Instrument and estimate an allowed rate of return of 5.53 per cent (nominal vanilla).[32] Submissions to this process and also separate but concurrent regulatory processes support the immediate full application of the binding 2018 Instrument to all resets.[33]

Our calculated rate of return, in Table 4, will apply to the first year of the 2019–24 regulatory control period. A different rate of return will apply for the remaining regulatory years of the period. This is because we will update the return on debt

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[32] See https://www.aer.gov.au/networks-pipelines/guidelines-schemes-models-reviews/rate-of-return-guideline-2018/final-decision. The legislative amendments to replace the (previous) non-binding Rate of Return Guidelines with a binding legislative instrument were passed by the South Australian Parliament in December 2018. See, Statutes Amendment (National Energy Laws) (Binding Rate of Return Instrument) Act 2018 (SA). NGL, Chapter 2, Part 1, division 1A; NEL, Part 3, division 1B.

[33] For example, see: EUAA, *Submission to NSW DNSP's 2019-24 revenue reset*, January 2019, p. 5; Origin, *Letter to the AER: AER draft decision for NSW electricity distributors 2019-24*, 5 February 2019, p. 1; PIAC, *Submission to the AER's draft determinations and the NSW DNSPs' 2019-24 revised proposals*, 7 February 2019, p. 9; ECA, *Submission to the AER's draft decision on the Endeavour Energy 2019 to 2024 distribution determination*, 15 February 2019, p. 2; CCP10, *Response to the Ausgrid revised regulatory proposal 2019-24 and AER draft determination*, January 2019, p. 48; and CCP10, *Response to the Evoenergy revised regulatory proposal 2019-24 and AER draft determination*, January 2019, pp. 43–44.

component of the rate of return each year in accordance with the 2018 Instrument to use a 10-year trailing average portfolio return on debt that is rolled-forward each year. Our final decision is to accept Evoenergy's return on equity and debt averaging periods because they satisfied the 2018 Instrument.[34]

Table 4 Final decision on Evoenergy's rate of return (% nominal)

	AER draft decision (2019–24)	Evoenergy revised proposal (2019–24)	AER final decision (2019–24)	Allowed return over regulatory control period
Nominal risk free rate	2.66% [a]	2.66% [b]	1.96% [c]	
Market risk premium	6%	6.5%	6.1%	
Equity beta	0.6	0.7	0.6	
Return on equity (nominal post–tax)	6.3%	7.2%	5.6%	Constant (%)
Return on debt (nominal pre–tax)	5.46%	5.46%	5.47%[d]	Updated annually
Gearing	60%	60%	60%	Constant (60%)
Nominal vanilla WACC	5.80%	6.16%	5.53%	Updated annually for return on debt
Forecast inflation	2.45%	2.45%	2.42%	Constant (%)

Source: AER analysis.

[a] Calculated using a placeholder averaging period of 20 business days ending 31 July 2018.

[b] Calculated using a placeholder averaging period of 20 business days ending 31 July 2018.

[c] Final decision to accept proposed period of 20 consecutive business days ending 29 March 2019.

[d] Final decision is to accept the proposed debt averaging periods and return on debt updated for the latest averaging period. Our decision reflects a trailing average return on debt which assumes that the annual return on debt (for the remaining years in the 2019-24 period) is the annual return on debt estimated for 2019–20. However, as noted above and in the 2018 Instrument, we will update the remaining years' trailing average return on debt each year using the averaging periods specified in this decision.

We have reviewed Evoenergy's revised rate of return proposal and found that it was not consistent with our 2018 Instrument because it proposed equity parameters from the 2013 rate of return guidelines (2013 Guidelines). That is, it proposed a market risk

[34] AER, *Rate of return instrument*, December 2018, clauses 7–8, 23–25; Evoenergy, *Regulatory Proposal for ACT electricity distribution Network 2019-24 - Appendix 8.1*, 31 January 2018. Evoenergy's proposed risk free rate averaging period for the upcoming regulatory period, as set out in the proposal dated 31 January 2018. As the 31 March 2019 is a Sunday, we consider that, practically, this entails the closest business day preceding this end date (29 March 2019). The averaging period meets the conditions set out in clauses 7 and 8 of the Rate of Return Instrument.

premium of 6.5 per cent and equity beta of 0.7.[35] However, we note that Evoenergy's revised proposal was submitted prior to legislative changes which installed a binding rate of return instrument and the release of the 2018 Instrument. Evoenergy has since recognised that we would apply the 2018 Instrument to its 2019–24 distribution determination,[36] which entails a market risk premium of 6.1 per cent and equity beta of 0.6.[37] These values are a product of our extensive consultation and analysis during the 2018 rate of return review process.

Debt and equity raising costs

In addition to compensating for the required rate of return on debt and equity, we provide an allowance for the transaction costs associated with raising debt and equity. We include debt raising costs in the opex forecast because these are regular and ongoing costs. We include equity raising costs in the capex forecast because these costs are only incurred once and would be associated with funding the particular capital investments.

Our final decision forecasts for equity and debt raising costs are included in capex and opex Attachments 5 and 6, respectively. We set equity raising costs of $0.1 million ($2018–19) for Evoenergy's prescribed transmission services and zero for its standard control services. As we have rejected Evoenergy's revised opex proposal, we have estimated debt raising costs using our benchmark approach which Evoenergy has adopted in its proposal (see Table 5).[38]

Table 5 AER's final decision on debt raising costs ($ million, 2018-19)

	2019–20	2020–21	2021–22	2022–23	2023–24	Total
Transmission	0.1	0.1	0.1	0.1	0.1	0.4
Distribution	0.4	0.4	0.4	0.4	0.4	2.0

Source: AER analysis.

Note: Columns may not add to total due to rounding for presentation in table.

[35] Evoenergy, *Revised regulatory proposal ACT electricity distribution network 2019–24*, November 2018, p. 63.

[36] Evoenergy, *Rate of return guideline 2018,* 18 February 2019.

[37] AER, *Rate of return instrument*, December 2018, clause 4(b) and (c). The legislative amendments to replace the (previous) non-binding Rate of Return Guidelines with a binding legislative instrument were passed by the South Australian Parliament in December 2018. See, Statutes Amendment (National Energy Laws) (Binding Rate of Return Instrument) Act 2018 (SA). NGL, Chapter 2, Part 1, division 1A; NEL, Part 3, division 1B.

[38] Evoenergy adopted our benchmark approach in its revised proposal. See: Evoenergy, *regulatory proposal for the ACT electricity distribution network 2019–24 Attachment 8: rate of return, imputation credits and forecast inflation*, January 2018, p. 20. Also see our opex attachment for our final opex decision.

Imputation credits

Our final decision applies a gamma of 0.585 as per the binding 2018 Instrument.[39] This was the result of extensive analysis and consultation conducted as part of the 2018 rate of return review.[40] Evoenergy's revised proposal adopted a gamma of 0.4.[41] However, subsequent to the lodgement of its revised proposal, Evoenergy submitted that it recognises that we would apply the 2018 Instrument for its 2019–24 distribution determination.[42]

2.3 Regulatory depreciation (return of capital)

Regulatory depreciation is the allowance provided so capital investors recover their investment over the economic life of the asset (return of capital). Evoenergy invests capital in large assets to provide electricity network services to its customers. The costs of these assets are recovered over the assets' useful lives, many of which can be 50 or more years. This means only a small part of the cost of such assets are recovered from customers upfront or in any year. The greater proportion is recovered over time through the depreciation allowance. The regulatory depreciation allowance is the net total of the straight-line depreciation less the inflation indexation adjustment of the RAB.

Our final decision on Evoenergy's revenue for 2019–24 includes a regulatory depreciation allowance of $250.7 million ($ nominal).[43] This is $0.8 million (0.3 per cent) higher than Evoenergy's revised proposal.

We have adopted the same approach to depreciation as Evoenergy, including the revised proposed asset lives which determine how quickly an asset class is depreciated (removed from the RAB). However, we have changed the standard asset life for the 'Equity raising costs' asset class.

The difference between our final decision depreciation allowance and Evoenergy's revised proposal also reflects other related parts of our final revenue decision, including our final decisions on:

- the opening RAB values at 1 July 2019, as discussed in section 2.1
- the expected inflation rate, which is lower than used by Evoenergy in its proposal

The effect of these changes to the opening RAB is to slightly increase the depreciation allowance relative to Evoenergy's revised proposal. The depreciation allowance included in our final decision on Evoenergy's revenue is 24.7 per cent higher ($2018–

39 AER, *Rate of return instrument*, December 2018, clause 27.

40 AER, *Rate of return instrument explanatory statement*, December 2018, pp. 307–382.

41 Evoenergy, *Revised regulatory proposal ACT electricity distribution network 2019–24*, November 2018, p. 63.

42 Evoenergy, *Rate of return guideline 2018,* 18 February 2019.

43 This comprises $211.1 million for Evoenergy's distribution network and $39.6 million for its transmission network.

19) than the allowance for the 2014–19 period.[44] One reason for this increase is the continued depreciation over the 2019–24 period of short-lived assets invested in during the 2014–19 period.

Table 6 and Table 7 set out our final decision on the forecast regulatory depreciation allowance for Evoenergy's 2019–24 regulatory control period for its distribution and transmission networks, respectively. Further detail on Evoenergy's regulatory depreciation is set out in Attachment 4.

Table 6 AER's final decision on Evoenergy's forecast regulatory depreciation allowance for the 2019–24 regulatory control period – distribution ($ million, nominal)

	2019–20	2020–21	2021–22	2022–21	2021–24	Total
Straight-line depreciation	55.2	58.5	62.1	66.7	70.1	312.6
Less: inflation indexation on opening RAB	19.3	19.8	20.1	20.9	21.4	101.5
Regulatory depreciation	**35.9**	**38.7**	**42.0**	**45.8**	**48.7**	**211.1**

Source: AER analysis.

Table 7 AER's final decision on Evoenergy's forecast regulatory depreciation allowance for the 2019–24 regulatory control period – transmission ($ million, nominal)

	2019–20	2020–21	2021–22	2022–21	2021–24	Total
Straight-line depreciation	10.9	11.4	12.2	13.0	13.6	61.0
Less: inflation indexation on opening RAB	4.3	4.2	4.3	4.3	4.3	21.4
Regulatory depreciation	**6.6**	**7.2**	**7.9**	**8.7**	**9.3**	**39.6**

Source: AER analysis.

2.4 Capital expenditure

Capital expenditure (capex) — the capital costs and expenditure incurred in the provision of network services — mostly relates to assets with long lives, the costs of which are recovered over several regulatory control periods.

Capex is added to Evoenergy's RAB, which is used to determine the return on capital and return of capital (regulatory depreciation) building block allowances. All else being equal, higher forecast capex will lead to a higher projected RAB value and higher return on capital and regulatory depreciation allowances.

[44] https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/evoenergy-actewagl-distribution-determination-2014-19-remittal/final-decision

Our final decision addresses a modelling error in Evoenergy's capex forecast, but otherwise includes its corrected total forecast capex of $314.3 million ($2018–19) for the 2019–24 regulatory control period.[45]

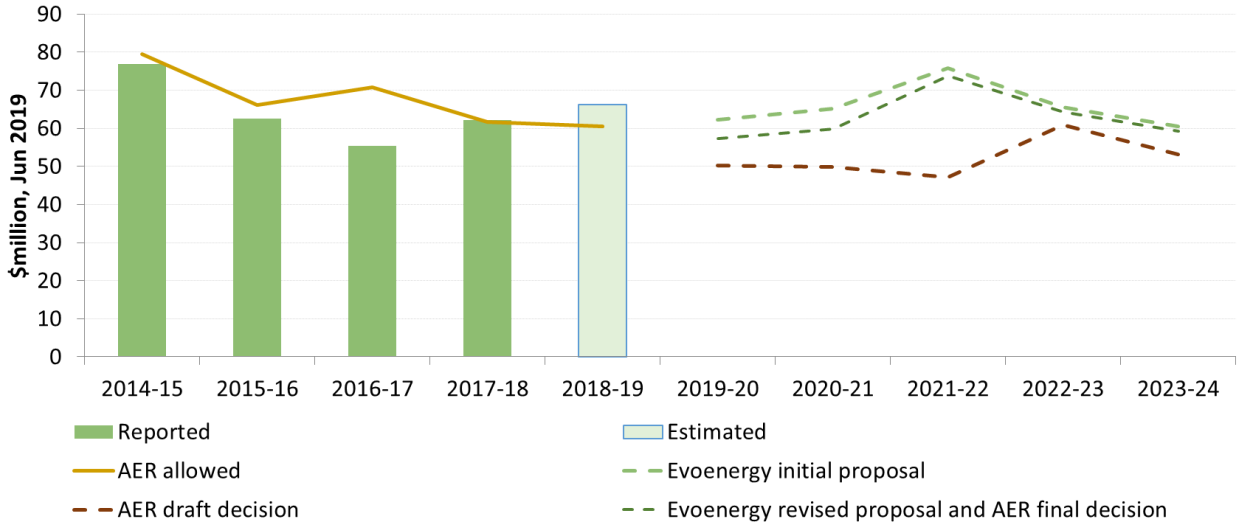
Our final decision accepts Evoenergy's revised total net capex forecast $314.3 million ($2018–19) for the 2019–24 regulatory control period. This forecast is $8.9 million (2.8 per cent) lower than its actual and estimated net capex over the 2014–19 period.

Evoenergy's revised total net capex forecast is $15.2 million (4.6 per cent) lower than its initial total net capex forecast of $329.5 million ($2018–19).

We are satisfied that Evoenergy's revised total net capex forecast reasonably reflects the capex criteria and is consistent with the efficient costs that a prudent operator would incur in the 2019–24 regulatory control period.

Figure 6 outlines Evoenergy's historical capex trend, its 2019–24 initial and revised forecasts, and our 2019–24 draft and final decisions (the final decision being consistent with the revised proposal).

Figure 6 Evoenergy's capex over time ($ million, 2018-19)



Source: AER analysis.

Note: Net capex.

Table 8 sets out the capex amounts by driver that Evoenergy has justified would reasonably reflect the capex criteria.

[45] In its November 2018 revised proposal, Evoenergy presented a total capex forecast of $316.5 million. We subsequently identified that Evoenergy's revised connections capex forecast did not account for an earlier revision that it provided in April 2018. The final decision modifies Evoenergy's revised connections proposal based on the earlier revision.

Table 8 Assessment of required capex by driver for the 2019–24 regulatory control period ($ million, 2018-19)

Category	2019–20	2020–21	2021–22	2022–23	2023–24	Total
Augmentation	9.6	12.5	13.9	6.7	6.0	48.7
Reliability	1.2	1.2	1.2	1.2	1.3	6.2
Connections	22.9	30.6	17.5	17.7	17.2	105.9
Replacement	17.3	17.6	16.4	17.2	23.3	91.8
Non-network	8.4	6.6	17.6	16.6	6.7	56.0
Capitalised overheads	13.0	14.9	14.4	12.3	11.8	66.4
Gross capex	**72.4**	**83.5**	**81.0**	**71.8**	**66.3**	**375.0**
Less capital contributions	-14.9	-23.6	-7.0	-7.2	-6.9	-59.6
Less disposals	-0.2	-0.1	-0.1	-0.4	-0.2	-1.2
Net capex	**57.3**	**59.8**	**73.8**	**64.2**	**59.2**	**314.3**

Source: AER analysis.

Notes: Capital contributions in this table include an overheads component.
Numbers may not add up due to rounding.
Net capex = gross capex *less* capital contributions *less* disposals

2.5 Operating expenditure

Operating expenditure (opex) refers to the operating, maintenance and other non-capital expenses incurred in the provision of network services. Forecast opex for standard control services (SCS) is one of the building blocks we use to determine a service provider's annual total revenue requirement.

Our final decision on Evoenergy's revenue includes $295.8 million ($2018–19) in total forecast opex for the 2019–24 regulatory control period. This is $6.2 million (2.1 per cent) lower than Evoenergy's revised opex forecast of $302.0 million ($2018–19) which we do not accept.

Table 9 shows our final decision compared to Evoenergy's revised opex forecast.

Table 9 AER final decision on total opex ($ million, 2018–19)

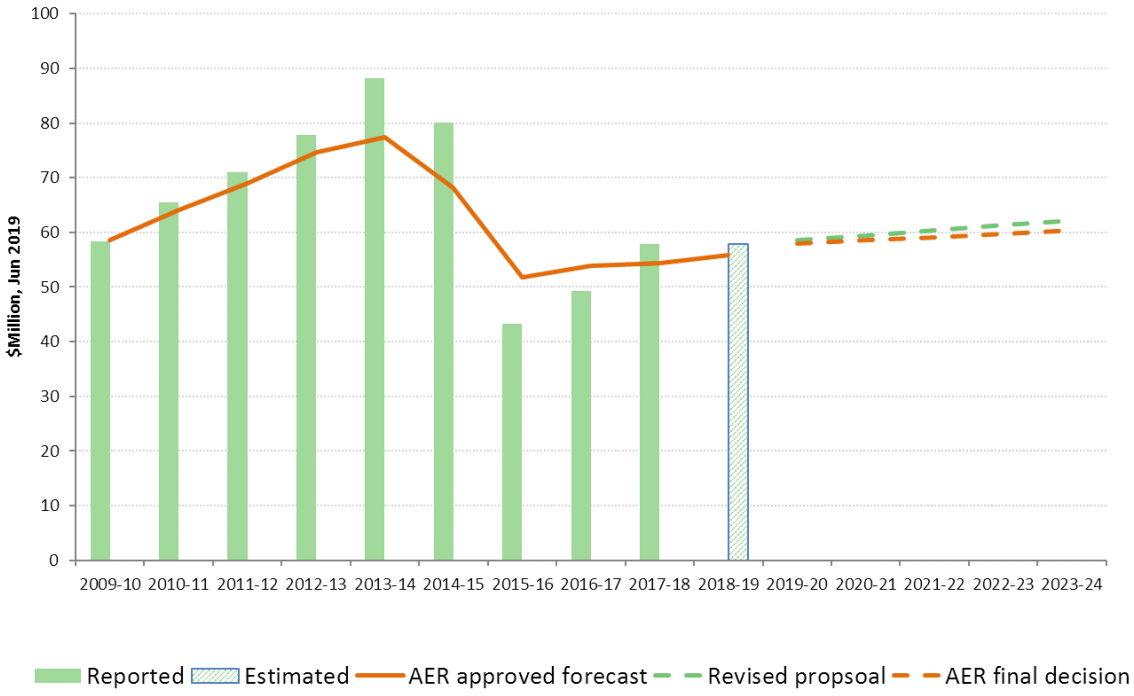
	2019–20	2020–21	2021–22	2022–23	2023–24	Total
Evoenergy's revised proposal	58.7	59.5	60.4	61.3	62.2	302.0
AER final decision	57.9	58.6	59.2	59.8	60.3	295.8
Difference	-0.7	-0.9	-1.2	-1.5	-1.9	-6.2

Source: Evoenergy, *Revised revenue proposal*, *PTRM*, November 2018; AER analysis

Note: Includes debt-raising costs. Numbers may not add up to total due to rounding.

Figure 7 shows our opex final decision compared to Evoenergy's revised opex forecast and its reported opex over the last two regulatory control periods.

Figure 7 AER final decision on total forecast opex ($ million, 2018–19)



Source: Evoenergy, *Annual reporting regulatory information notices*; Evoenergy, *Revenue proposal 2019-24, Workbook 1 Regulatory determination*; AER analysis.

Note: Includes debt-raising costs.

Evoenergy's revised opex forecast adopts many aspects of the approach we used in our draft decision, and is 1.7 per cent higher than our draft decision. The key differences between Evoenergy's revised opex forecast and our draft decision are:

- the update of the 2017–18 base year opex and adjustments with actual cost data. This is 2.6 per cent higher than Evoenergy's January 2018 initial proposal (which we accepted in our draft decision) due to updated information of its actual opex in 2017–18.
- the updates of Evoenergy's output growth forecast based on the latest available information, including the output growth weights, Evoenergy's customer number forecast and energy throughput forecast.

Our final decision to not accept Evoenergy's revised total opex proposal of $302.0 million ($2018–19) reflects the material difference between the revised proposal and our alternative estimate of $295.8 million ($2018–19). Therefore, we are not satisfied that Evoenergy's revised opex forecast reasonably reflects of the opex criteria.

The primary difference between Evoenergy's revised proposal and our alternative estimate is due to our inclusion of a productivity growth forecast of 0.5 per cent per year in our alternative estimate, as compared to the zero per cent per year Evoenergy has included in its revised proposal. This reflects the opex productivity growth that can be achieved by a prudent electricity distributor acting efficiently under business-as-usual conditions.

As foreshadowed in our draft decision, we undertook an industry wide consultation on our approach to forecasting opex productivity growth. Evoenergy made a submission to our opex productivity growth forecast review. We concluded our review in March 2019 and took into account Evoenergy's submission. Our opex productivity growth forecast of 0.5 per cent per year reflects the outcome of this review.

In formulating our alternative opex estimate, we have also:

- updated Evoenergy's revised base opex to reflect the RBA's most recent inflation forecast. This reduces our opex forecast compared to Evoenergy's revised opex forecast.
- updated our labour price growth forecast according to Deloitte Access Economics' wage price index forecast updated in February 2019, which we averaged with Evoenergy's forecast prepared by BIS Oxford Economics. This increases our opex forecast compared to Evoenergy's revised opex forecast.
- updated our output growth forecast, using an average of the output weights from the four benchmarking models presented in our 2017 annual benchmarking report (consistent with our draft decision) for the period 2006–17. This is broadly consistent with Evoenergy's revised opex forecast.

We have considered the issues raised in stakeholder submissions about opex in establishing our alternative estimate, including the submissions Evoenergy had made during and after our opex productivity growth forecast review process. We have set out the reasons for our final decision on opex in greater detail in Attachment 6. Our opex model, which calculates our alternative estimate of opex, is available on our website.

2.6 Corporate income tax

The 'building block' approach to the calculation of revenue includes an allowance for the estimated cost of corporate income tax payable by Evoenergy. Our final decision is to include a corporate income tax allowance of $12.6 million ($ nominal) in Evoenergy's revenue for 2019–24.[46] This represents a reduction of $28.8 million (or 69.5 per cent) on Evoenergy's revised proposal.

The key reasons for this reduction are:

- we amended the PTRM to implement the findings in our final report on the review of the regulatory tax approach (the tax review), which concluded after the

[46] This comprises $8.0 million for Evoenergy's distribution network and $4.7 million for its transmission network.

submission of Evoenergy's revised proposal. Specifically, for this final decision, we have recognised immediately expensed capex for the calculation of tax depreciation. We also applied the diminishing value (DV) method for tax depreciation to all new depreciable assets except for forecast capex associated with equity raising costs. These changes have reduced the revised proposed corporate income tax allowance by about $15.3 million (or 36.9 per cent).[47]

- we reduced Evoenergy's revised proposed return on equity (section 2.2). Our final decision on the forecast return on equity affects the amount of estimated taxable income. Therefore, it has contributed to the reduction on the revised proposed corporate income tax allowance by about $7.1 million (or 17.1 per cent).[48]
- we increased the value of imputation credits (gamma) to 0.585 as per the binding 2018 Instrument from Evoenergy's revised proposal of 0.4 (section 2.2). This has reduced the revised proposed corporate income tax allowance by about $6.9 million (or 16.6 per cent).[49]

For this final decision, we accepted Evoenergy's approach for establishing the opening tax asset base (TAB). We also accepted the revised proposed total opening TAB as at 1 July 2019 of $907.3 million ($ nominal).[50] We updated the revised proposed opening TAB values for a number of asset classes to reflect our amendments to Evoenergy's actual capex value for 2017–18 in the roll forward model. While these amendments affect the opening TAB values at the asset class level, they do not result in a material change to the total opening TAB values.

As a consequence of amending the actual capex value for 2017–18, we have updated Evoenergy's remaining tax asset lives as at 1 July 2019. We accept Evoenergy's revised proposed standard tax asset lives, which are consistent with our draft decision, subject to a change for the 'Buildings' asset class.

Our final decision on the regulatory depreciation (section 2.3) and forecast capex (section 2.4 and Attachment 5) affect the calculation of the estimated taxable income, which in turn impacts the corporate income tax allowance.

Table 10 and Table 11 set out our final decision on the estimated cost of corporate income tax allowance for Evoenergy over the 2019–24 regulatory control period for its distribution and transmission networks, respectively.

Further detail on our final decision regarding corporate income tax is set out in Attachment 7.

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47 This reflects reductions of $14.3 million (or 44.7 per cent) and $1.0 million (or 10.5 per cent) for Evoenergy's distribution and transmission networks, respectively.

48 This reflects reductions of $5.9 million (or 18.3 per cent) and $1.2 million (or 12.9 per cent) for Evoenergy's distribution and transmission networks, respectively.

49 This reflects reductions of $4.3 million (or 13.5 per cent) and $2.5 million (or 26.8 per cent) for Evoenergy's distribution and transmission networks, respectively.

50 This comprises $744.0 million for Evoenergy's distribution network and $163.3 million for its transmission network.

Table 10 AER's final decision on Evoenergy's cost of corporate income tax allowance for the 2019–24 regulatory control period – distribution ($ million, nominal)

	2019–20	2020–21	2021–22	2022–23	2023–24	Total
Tax payable	4.2	4.5	3.7	3.5	3.3	19.2
Less: value of imputation credits	2.5	2.6	2.2	2.0	1.9	11.2
Net corporate income tax allowance	**1.8**	**1.9**	**1.5**	**1.4**	**1.4**	**8.0**

Source: AER analysis.

Table 11 AER's final decision on Evoenergy's cost of corporate income tax allowance for the 2019–24 regulatory control period – transmission ($ million, nominal)

	2019–20	2020–21	2021–22	2022–23	2023–24	Total
Tax payable	3.5	6.2	0.5	0.5	0.6	11.3
Less: value of imputation credits	2.1	3.6	0.3	0.3	0.4	6.6
Net corporate income tax allowance	**1.5**	**2.6**	**0.2**	**0.2**	**0.3**	**4.7**

Source: AER analysis.

2.7 Revenue adjustments

Our final decision on Evoenergy's total revenue also includes a number of adjustments:

- Capital expenditure sharing scheme (CESS) — Evoenergy has not accrued rewards under the CESS, which we applied in the current 2014–19 regulatory control period to incentivise Evoenergy to undertake efficient capex throughout the period. The CESS rewards efficiency gains and penalises efficiency losses, each measured by reference to the difference between forecast and actual capex. In the 2014–19 period, Evoenergy over-spent against our capex forecast. Our final decision is to apply a CESS revenue decrement amount of $1.1 million.
- Demand management innovation allowance mechanism (DMIAM) — A DMIAM allowance of $1.63 million ($2018–19) has been applied to Evoenergy over the 2019–24 regulatory control period.[51] The DMIAM aims to encourage distribution businesses to find investments that are lower cost alternatives to investing in network solutions.

[51] As a result of corrections to the DMIAM calculation, this is slightly higher than in Evoenergy's revised proposal.

- Remittal — A net revenue reduction of $0.9 million ($2018–19) has been applied to Evoenergy, in accordance with what we determined will be returned to customers under our 2014–19 remade final remade for Evoenergy.[52] This amount reflects the difference between our 2014–19 remade final decision and the revenue expected to be recovered by Evoenergy under the interim price undertakings that have applied over the 2014–19 period. This adjustment was included in Evoenergy's revised proposal.

[52] NER, cl. 8A.15.

3 Incentive schemes

Incentive schemes are a component of incentive based regulation and complement our approach to assessing efficient costs. These schemes provide important balancing incentives under the revenue determination to encourage Evoenergy to pursue expenditure efficiencies and demand side alternatives to capex and opex, while maintaining the reliability and overall performance of its network.

The incentive schemes that might apply to an electricity network as part of our decision are the:

- opex efficiency benefit sharing scheme (EBSS)
- capital expenditure sharing scheme (CESS)
- service target performance incentive scheme (STPIS)
- demand management incentive scheme (DMIS) and demand management innovation allowance mechanism (DMIAM).

Once we make our decision on Evoenergy's revenue cap, it has an incentive to provide services at the lowest possible cost, because its returns are determined by its actual costs of providing services. Our incentive schemes encourage network businesses to make efficient decisions. They give network businesses an incentive to pursue efficiency improvements in opex and capex, and to share them with consumers.

Our final decision is that each of the EBSS, CESS, STPIS, DMIS and DMIAM will apply to Evoenergy for the 2019–24 regulatory control period. Evoenergy's performance under these schemes in the 2019–24 regulatory control period will be reflected in its annual pricing proposals throughout that period and its revenue proposal for the subsequent, 2024–29 regulatory control period.

Our final decision on the incentive schemes are outlined below.

3.1 Efficiency benefit sharing scheme

The EBSS is intended to provide a continuous incentive for distributors to pursue efficiency improvements in opex, and provide for a fair sharing of these between distributors and network users. Consumers benefit from improved efficiencies through lower regulated prices.

Our final decision is to maintain our draft decision and reinstate the EBSS for Evoenergy in the 2019–24 regulatory control period.[53] We will apply version two of our EBSS to Evoenergy in the 2019–24 period, with a carryover period of five years.

[53] AER, *Draft decision – Evoenergy distribution determination 2019–24, Attachment 8: Efficiency benefit sharing scheme*, September 2018.

Consistent with version two of the EBSS, we will make the following adjustments when we calculate the efficiency gains and losses that will be carried over into the next regulatory control period:

- exclude debt-raising costs, because these are not forecast on a revealed cost basis
- adjust forecast opex to add (subtract) any approved revenue increments (decrements) made after the initial regulatory determination, such as approved pass through amounts
- adjust actual opex to remove DMIA opex
- adjust actual opex to add capitalised opex that has been excluded from the RAB[54]
- exclude costs for any services that will not be classified as standard control services (SCS) in the 2024–29 regulatory control period.

In its revised proposal, Evoenergy accepted our draft decision on the EBSS in entirety, including our proposed carryover period and adjustments to forecast or actual opex when calculating EBSS carryover amounts.

Our reasons and approach are set out in our draft decision in detail.

3.2 Capital expenditure sharing scheme

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

As noted earlier, in the 2014–19 regulatory control period, Evoenergy over-spent against our capex forecast. Our final decision is to apply a CESS revenue decrement amount of $1.1 million from the application of the CESS in the 2014–19 period.

We will also apply the CESS as set out in version 1 of the Capital Expenditure Incentives Guideline to Evoenergy in the 2019–24 regulatory control period.

Further detail on our final decision regarding the CESS is set out in Attachment 9.

3.3 Service target performance incentive scheme

The STPIS is intended to balance a business' incentive to reduce expenditure with the need to maintain or improve service quality. The scheme achieves this by providing financial incentives to distributors to maintain and improve service performance where customers are willing to pay for these improvements.

[54] NER, cl. 6.5.8(c)(4) requires us to have regard to any incentives the service provider may have to capitalise expenditure.

Distributors can only retain their rewards for sustained and continuous improvements to the reliability of supply to customers. Once improvements are made, the benchmark performance targets will be tightened in future years.

Our final decision is to apply the service standards component (the s-factor) of our national STPIS, STPIS version 2.0 (November 2018)[55], to Evoenergy for the 2019–24 regulatory control period. We will not apply the guaranteed service level component to Evoenergy as the existing jurisdictional arrangements will continue to apply.

Attachment 10 sets out our decision on Evoenergy's STPIS for 2019–24.

3.4 Demand management incentive scheme

On 13 December 2017, we published a new DMIS[56] and DMIAM.[57] These schemes replace the current DMIS and DMIA in the 2019–24 regulatory control period for all electricity distributors.

In our draft decision, our decision was to apply the new DMIS and DMIAM to Evoenergy for the 2019–24 regulatory control period, without any modification.[58] Evoenergy's revised proposal accepted our draft decision.[59]

We received no submissions on Evoenergy's proposed implementation of the new DMIS and DMIAM.

The DMIS contains three elements:[60]

- a cost uplift on expected costs of efficient demand management projects
- a net benefit constraint, to ensure the incentive payment for any project cannot be higher than that project's expected net benefit
- an overall incentive constraint, which limits the total incentive in any year to one per cent of the distributor's allowed revenue for that year.

The cost multiplier (uplift) applicable to any eligible project will be the cost multiplier specified in the version of the DMIS that is in effect under clause 6.6.3 of the NER at the time the eligible project becomes a committed project.[61]

The DMIAM comprises:[62]

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55 AER, *Electricity distribution network service providers—service target performance incentive scheme*, *Version 2.0*, November 2018. (AER, *STPIS*, November 2018).

56 AER, *Demand management incentive scheme, Electricity distribution network service providers*, December 2017.

57 AER, *Demand management innovation allowance mechanism*, *Electricity distribution network service providers*, December 2017.

58 AER, *Draft decision, Evoenergy distribution determination 2019-24, Attachment 11, Demand management incentive scheme*, September 2018.

59 Evoenergy, *Revised Regulatory Proposal, ACT electricity distribution network 2019-24*, November 2018, p. 85.

60 AER, *Demand management incentive scheme*, *Electricity distribution network service providers*, December 2017.

61 AER, *Demand management incentive scheme*, *Electricity distribution network service providers*, December 2017, clause 2.1(2).

- a fixed allowance of $200,000 ($2016–17) plus 0.075 per cent of the annual revenue requirement for each regulatory year, as set out in our PTRM for Evoenergy
- project eligibility requirements
- compliance reporting requirements.

Our calculation of Evoenergy's DMIAM funding over the 2019–24 regulatory control period is shown in Table 12. As noted earlier, the total DMIAM funding is $1.63 million ($2018–19) over the period. This calculation is based on the smoothed annual revenue requirement as set out in the PTRM for Evoenergy in our 2019–24 final decision.

Table 12 AER's final decision on the DMIA for Evoenergy ($ million, 2018–19)

	2019–20	2020–21	2021–22	2022–23	2023–24	Total
DMIA	0.32	0.33	0.33	0.33	0.33	1.63

Source: AER analysis.

[62] AER, *Demand management innovation allowance mechanism*, *Electricity distribution network service providers*, December 2017.

4 Tariff structure statement

Evoenergy's 2019–24 revised proposal includes the second iteration of its tariff structure statement (TSS). Its current TSS applies to 30 June 2019.

A TSS applies to a distributor's tariffs for the duration of the regulatory control period. It describes a distributor's tariff classes and structures, the distributor's policies and procedures for assigning and reassigning customers to tariffs, the charging parameters for each tariff, and a description of the approach the distributor takes to setting tariffs in pricing proposals.[63] It is accompanied by an indicative pricing schedule.[64] A TSS provides consumers and retailers with certainty and transparency in relation to how and when network prices will change.

Evoenergy accepted our draft decision on its TSS and, in doing so, incorporated our proposed revisions.[65] Our final decision is consistent with our draft decision and Evoenergy's revised proposal.[66]

We note some stakeholders raised concerns about aspects of the revised TSS. We set out our consideration of these issues below, along with our consideration of Evoenergy's approach to estimating long run marginal cost.

Data sampling period required to manage customer transition

Consistent with our draft decision, Evoenergy's revised proposal amended its tariff assignment policy for reassigning customers to cost reflective network tariffs to include a 12-month data sampling period between the trigger event occurring and tariff reassignment for customers where reassignment results from an end-of-life meter replacement.[67]

Retailer, ActewAGL, submitted that the amendment to Evoenergy's tariff reassignment trigger will impede customers' ability to benefit from having a smart meter as well as increasing complexity for customers and adding to implementation costs for retailers.[68]

While we acknowledge there is not universal support for the data sampling period, we remain of the view that a 12-month data sampling period is appropriate. Comparing the implementation costs with the advantages of managing transitional impacts is difficult as it is hard to quantify benefits. However, we consider that:

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63 NER, cl. 6.18.1A(a).

64 NER, cl. 6.18.1A(e).

65 Evoenergy, *Revised regulatory proposal, ACT electricity distribution network 2019–24,* November 2018 p.96–97

66 AER, *Draft Decision Evoenergy distribution determination 2019–24, Attachment 18 Tariff Structure Statement*, September 2018

67 AER, *Draft Decision Evoenergy distribution determination 2019–24, Attachment 18 Tariff Structure Statement*, September 2018

68 ActewAGL, *Submission on Evoenergy 2019–24*, 11 January 2019

- even without a data sampling period, it is likely retailers will still face implementation costs (for example, needing to update existing billing systems)
- the 12-month data sampling period provides a mechanism to mitigate transitional impacts to manage the potential risk of customer concern, without which tariff reform could be set back further.

We consider this will ease implementation issues and allow a better understanding for 'passive' customers.[69] These customers are currently not actively engaging with their electricity supplier, with circumstances beyond their control driving their tariff reassignment. We are satisfied that this measure better informs these customers on how they can mitigate the impact of changes in tariffs through their usage decisions.[70]

Customer impacts accounted for in tariff design

Evoenergy's default cost reflective tariff consists of a seasonal peak demand charge, a flat energy charge and a fixed daily charge. This is consistent with the structure applying at the conclusion of the current 2014–19 regulatory control period.[71] Stakeholders raised concerns that there had been customer dissatisfaction with demand tariffs.

We requested Evoenergy to describe any community or retailer feedback it has received since transitioning its customers onto these cost reflective tariffs.[72] In its response, Evoenergy noted that it has so far assigned 8,000 residential and 1,000 commercial customers to its demand tariffs. In doing so, Evoenergy engaged specialist assistance in designing customer communications, which led it to refresh its website, produce a customer fact-sheet and material for its call centre staff.[73] This approach has led to very few negative responses to the new demand tariffs. As of 31 January 2019, Evoenergy's contact centre has no record of any customer complaints regarding demand tariffs. Evoenergy did note that three letters directed to retailer, ActewAGL, regarding retail demand tariffs were published in local media.[74]

We are satisfied that any concerns with demand tariffs are isolated and do not apply to network tariffs, but rather to retailers passing these through. We commend the approach Evoenergy is taking to communicating changes to underlying network tariffs to customers.

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69 'Passive' customers being those who have not initiated a change to their circumstances, rather than those who have had their meter replaced with a smart meter as their existing meter reaches end-of-life.

70 NER 6.18.5(h).

71 Evoenergy (ActewAGL Distribution Network), *Revised Tariff Structure Statement,* 4 October 2016, p.22.

72 AER, *Information request #051*, 1 February 2019.

73 AER, *Information request #051*, 1 February 2019.

74 Evoenergy, *Response to AER Information Request #051*, 8 February 2019.

Long run marginal cost

We are satisfied Evoenergy's approach to estimating long run marginal cost (LRMC) contributes to compliance with the distribution pricing principles or to the achievement of the network pricing objective. Evoenergy did not amend its method for estimating LRMC in its revised proposal.[75] Our assessment of, and reasons for, accepting Evoenergy's estimation method are therefore unchanged from our draft decision.[76]

Although the LRMC estimation method is consistent with Evoenergy's initial regulatory proposal, its revised proposal:

- updated the models for forecasting energy sales, customer numbers and peak demand to account for new data up to September 2018[77]
- corrected the adjustment for power factor.[78]

Table 13 presents the revised LRMC estimates for each tariff class and shows significant reductions compared to the initial proposal. This is due to a combination of lower capex forecasts and higher demand forecasts in the forecast horizon.

Table 13 LRMC estimate for each tariff class ($/kW per annum, $2018–19)

Tariff Class	Evoenergy corrected initial proposal	Evoenergy revised proposal	Difference (per cent)
LV Residential	216	111	-48
LV Commercial	117	53	-55
HV	26	13	-50

Note: The corrected initial proposal LRMC estimates applied the power factor correctly.

Source: Evoenergy, *Response to AER information request IR31 Public*, 6 July 2018; Evoenergy, *Appendix 1.1: Revised tariff structure statement: Explanatory statement*, November 2018, p. 104.

The trend for decreasing capex in the LRMC input is due to two reasons:

- firstly, corporate overheads that are unaffected by an increment in demand in those areas of forecast demand growth were included in the initial proposal, but not the revised proposal

[75] Evoenergy, *Appendix 1.1: Revised tariff structure statement: Explanatory statement*, November 2018, pp. 101–104.

[76] AER, *Draft decision: Evoenergy distribution determination 2019 to 2024: Attachment 18: Tariff structure statement*, September 2018, pp. 22-24.

[77] Evoenergy, *Revised Regulatory Proposal*, November 2018, p. 3

[78] As mentioned in the AER's Draft Decision, Evoenergy corrected the LRMC estimates in response to an AER information request: Evoenergy, *AER Query 31 Response Public*, 6 July 2018. Due to this correction, the LRMC estimates are different to the published LRMC estimates in Evoenergy, *Attachment 17 Proposed Tariff Structure Statement*, January 2018.

- secondly, the timing changes for capital projects between the initial proposal and the revised proposal have impacted the LRMC capex input.[79]

The forecast incremental demand has increased largely due to the additional year of data used for sampling and changes to town planning. Recent updates to the ACT Government's planning and land release program have resulted in an increasing number of requests for customer connections.[80]

We consider the adjustments Evoenergy has made to the inputs in its LRMC estimation method are reasonable.

[79] Evoenergy, *Response to AER information request IR046*, 15 January 2019; Evoenergy, *Response to follow up questions to AER information request IR046*, 23 January 2019.

[80] Evoenergy, *Response to follow up questions to AER information request IR046*, 23 January 2019.

5 Other price terms and conditions

In this section, we consider the other aspects of our determination. These may be described as the terms and conditions of our determination that cover how Evoenergy must set its prices. These include the classification of services, the conditions under which we may grant Evoenergy additional revenues to cover unforeseen circumstances and the framework for Evoenergy's negotiated services, customer connections and transmission pricing.

5.1 Classification of services

Service classification determines the nature of economic regulation, if any, that is applicable to specific distribution services. Classification is important to customers as it determines which network services are included in basic electricity charges, the basis on which additional services are sold, and which services we will not regulate. Our decision reflects our assessment of a number of factors, including existing and potential competition to supply these services.

We set out our proposed approach to the classification of distribution services for Evoenergy in our Framework and Approach (F&A).[81] Our final decision is to retain the classification structure consistent with our F&A[82] and draft decision. Our draft decision included the addition of 'enhanced connection services' as an alternative control service (ACS). Our final decision is to retain this service in the classified services list as set out in Attachment 12. Evoenergy accepted our draft decision as being in accordance with its regulatory proposal.[83]

5.2 Pass through events

Consistent with our draft decision, we accept Evoenergy's four nominated pass through events ('terrorism', 'natural disaster', 'insurance cap' and 'insurer's credit risk') for the purpose of rule 6.6.1(a1)(5).

The approved definitions of these events are set out in Table 14.

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81 AER, *Final framework and approach for ActewAGL – Regulatory control period commencing 1 July 2019*, July 2017.

82 AER, *Final framework and approach for NSW electricity distributor – Regulatory control period commencing 1 July 2019*, July 2017. NER, cl. 6.12.3(b) – The classification of distribution services must be as set out in the relevant framework and approach paper unless we consider that a material change of circumstances justifies departing from that proposed classification.

83 Evoenergy, *Revised regulatory proposal – main document – November 2018*, p. 102.

Table 14 Approved nominated pass through events

Pass through event	Definition
Terrorism Event	A terrorism event occurs if: • An act (including, but not limited to, the use of force or violence or the threat of force or violence) of any person or group of persons (whether acting alone or on behalf of or in connection with any organisation or government), which from its nature or context is done for, or in connection with, political, religious, ideological, ethnic or similar purposes or reasons (including the intention to influence or intimidate any government and/or put the public, or any section of the public, in fear) and which increases the costs to Evoenergy in providing Direct Control Services. Note: In assessing a terrorism event pass through application, the AER will have regard to, among other things: • whether Evoenergy has insurance against the event; • the level of insurance that an efficient and prudent NSP would obtain in respect of the event; and • whether a declaration has been made by a relevant government authority that an act of terrorism has occurred.
Natural Disaster Event	Natural disaster event means any natural disaster including but not limited to fire, flood or earthquake that occurs during the 2019–24 regulatory control period that increases the costs to Evoenergy in providing Direct Control Services, provided the fire, flood or other event was not a consequence of the acts or omissions of the service provider. Note: In assessing a natural disaster event pass through application, the AER will have regard to, among other things: • whether Evoenergy has insurance against the event; and • the level of insurance that an efficient and prudent NSP would obtain in respect of the event.
Insurance Cap Event	An insurance cap event occurs if: • Evoenergy makes a claim or claims and receives the benefit of a payment or payments under a relevant insurance policy; • Evoenergy incurs costs beyond the policy limit of the relevant insurance policy at the time of the event that gives rise to the relevant claim; and • the costs beyond the relevant policy limit increase the costs to Evoenergy in providing Direct Control Services. For this insurance cap event: • a relevant insurance policy is an insurance policy held during the 2019–24 regulatory control period or a previous regulatory control period in which Evoenergy was regulated; and • Evoenergy will be deemed to have made a claim on a relevant insurance policy if the claim is made by a related body corporate of Evoenergy in relation to any aspects of Evoenergy's Direct Control Services. Note: In making a determination on an insurance cap event, the AER will have regard to, among other things: • the insurance policy for the event; and • the level of insurance that an efficient and prudent NSP would obtain in respect of the event.

Pass through event	Definition

Insurer's Credit Risk Event	An insurer's credit risk event occurs if:
	• A nominated insurer of Evoenergy becomes insolvent, and as a result, in respect of an existing, or potential, claim for a risk that was insured by the insolvent insurer, Evoenergy:
	  ○ is subject to a higher or lower claim limit or a higher or lower deductible than would have otherwise applied under the insolvent insurer's policy; or
	  ○ incurs additional costs associated with self-funding an insurance claim, which would otherwise have been covered by the insolvent insurer.
	Note: In assessing an insurer's credit risk event pass through application, the AER will have regard to, among other things:
	• Evoenergy's attempts to mitigate and prevent the event from occurring by reviewing and considering the insurer's track record, size, credit rating and reputation; and
	• in the event that a claim would have been made after the insurance provider became insolvent, whether Evoenergy had reasonable opportunity to insure the risk with a different provider.

5.3 Negotiating framework and criteria

In our draft decision, we approved Evoenergy's proposed distribution negotiating framework for the 2019–24 regulatory control period.[84] Evoenergy's revised proposal accepted our draft decision.[85]

Our final decision is to approve Evoenergy's negotiating framework. The distribution negotiating framework that will apply to Evoenergy for the period of this determination is set out in Attachment A.

We are also required to make a decision on the negotiated distribution service criteria (NDSC) for the distributor.[86] Our final decision is to retain the NDSC that we published for Evoenergy in February 2018[87] for the 2019–24 regulatory control period. The NDSC give effect to the negotiated distribution services principles.[88]

5.4 Connection policy

Our draft decision modified Evoenergy's proposed connection policy that it submitted in its initial regulatory proposal.[89]

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84 AER, *Draft Decision, Evoenergy distribution determination 2019 to 2024*, September 2018, Attachment 16, p.16–1.

85 Evoenergy, *Evoenergy Revised Regulatory Proposal Main Document 2019–2024*, 29 November 2018, p. 105.

86 NER, cl. 6.12.1(16).

87 AER, *Draft Decision, Evoenergy distribution determination 2019 to 2024*, September 2018, Attachment 16, p.16–1.

88 NER, cl. 6.7.1.

89 AER, *Draft Decision Evoenergy Distribution Determination 2019 to 2024, Attachment 17 Connection policy*, September 2018.

In its revised proposal, Evoenergy accepted our draft decision but proposed further refinements.[90] These minor changes are:

- to clarify that if a customer pays for connection that is above the least cost technically acceptable solution, the payment may include the cost of operation and maintenance (in addition to the additional construction cost)
- to clarify that for high-demand or high-consumption commercial connections, high-voltage connection is preferred by Evoenergy but is not mandatory (that is, the customer can select low-voltage connection)
- a change in terminology for new residential estates from 'typical estate' to 'Category 1 estate' (in relation to capital contributions by real estate developers)
- to expand and improve the description of a pioneer scheme.

We consider these proposed changes are reasonable.

We did not receive any submission on the draft decision and Evoenergy's revised proposal that addressed Evoenergy's connection policy.

Our final decision is to approve the connection policy submitted by Evoenergy in its revised proposal in November 2018.[91]

5.5 Pricing methodology

The role of Evoenergy's pricing methodology is to answer the question 'who should pay how much' in order for Evoenergy to recover its costs relating to its provision of transmission services.[92] The pricing methodology must provide a 'formula, process or approach' that when applied:[93]

- allocates the aggregate annual revenue requirement to the categories of prescribed transmission services that a network business provides and to the connection points of network users[94]
- determines the structure of prices that a network business may charge for each category of prescribed transmission services.[95]

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90 Evoenergy, *Revised regulatory proposal for the ACT electricity distribution network 2019–24, Attachment 2: Connection policy,* November 2018.

91 Evoenergy, *Revised regulatory proposal for the ACT electricity distribution network 2019–24, Attachment 2: Connection policy,* November 2018. See https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/evoenergy-actewagl-determination-2019-24/revised-proposal.

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

93 NER, cl. 6A.24.1(b).

94 NER, cl. 6A.24.1(b)(1).

95 NER, cl. 6A.24.1(b)(4).

Evoenergy must submit a transmission pricing methodology for our approval because its network includes high-voltage transmission assets, which are subject to the pricing arrangements for transmission standard control services (SCS).[96]

In our draft decision, we approved Evoenergy's proposed pricing methodology for the 2019–24 regulatory control period, subject to several amendments.[97] We also asked Evoenergy to update several references to the NER.[98]

Evoenergy accepted our draft decision and re-submitted its pricing proposal with the requested amendments.[99]

Our final decision is to approve Evoenergy's pricing methodology. Evoenergy's pricing methodology relates to transmission SCS only.

Our draft decision also noted that Evoenergy would update its pricing methodology in its revised proposal. The update would account for our 2014–19 remade final decision (remittal) for Evoenergy for the 2014–19 regulatory control period, which we had not published at the time Evoenergy submitted its initial regulatory proposal for 2019–24.[100] However, matters related to our remade final decision will be dealt with through the PTRM and the control mechanism for transmission SCS (see Attachment 13).[101]

The pricing methodology that will apply to Evoenergy for the period of this determination is set out in Attachment B.

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96 NER, cl. 6A.24.1(b)(2).

97 AER, *Draft Decision, Evoenergy distribution determination 2019 to 2024*, December 2018, Attachment 19, p. 5.

98 AER, *Evoenergy - information request #054 - Revised proposal - Pricing methodology - PUBLIC*, 4 March 2019; AER, *Follow up: Evoenergy - information request #054 - Revised proposal - Pricing methodology - PUBLIC*, 22 March 2019.

99 Evoenergy, *RE: Evoenergy - information request #054 - Revised proposal - Pricing methodology - PUBLIC*, 12 March 2019.

100 AER, *Draft Decision, Evoenergy distribution determination 2019 to 2024*, December 2018, Attachment 19, pp. 5–6.

101 Evoenergy, *Letter to AER: Prescribed (transmission) service pricing 2019/20 and 2020/21*, 5 December 2018.

A The National Electricity Objective

The National Electricity Law (NEL) requires us to make our decision in a manner that contributes, or is likely to contribute, to achieving the National Electricity Objective (NEO).[102] The focus of the NEO is on promoting efficient investment in, and operation and use of, electricity services (rather than assets) in the long-term interests of consumers.[103] This is not delivered by any one of the NEO's factors in isolation, but rather by balancing them in reaching a regulatory decision.[104]

In general, we consider that the long-term interests of consumers are best served where consumers receive a reasonable level of safe and reliable service that they value at least cost in the long run.[105] A decision that places too much emphasis on short term considerations may not lead to the best overall outcomes for consumers once the longer term implications of that decision are taken into account. [106]

There may be a range of economically efficient decisions that we could make in a revenue determination, each with different implications for the long-term interests of consumers.[107] A particular economically efficient outcome may nevertheless not be in the long-term interests of consumers, depending on how prices are structured and risks allocated within the market.[108] There are also a range of outcomes that are unlikely to advance the NEO, or advance the NEO to the degree than others would. For example, we consider that:

- the long-term interests of consumers would not be advanced if we encourage over-investment which results in prices so high that consumers are unwilling or unable to efficiently use the network.[109] This could have significant longer term pricing implications for those consumers who continue to use network services.
- equally, the long-term interests of consumers would not be advanced if allowed revenues result in prices so low that investors do not invest to sufficiently maintain the appropriate quality and level of service, and where customers are making more use of the network than is sustainable.[110] This could create longer term problems in the network, and could have adverse consequences for safety, security and reliability of the network.

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102 NEL, section 16(1).

103 This is also the view of the AEMC. See, for example, AEMC, *'Applying the Energy Objectives: A guide for stakeholders'*, 1 December 2016, p. 5.

104 Hansard, SA House of Assembly, 26 September 2013, p. 7173. See also AEMC, *'Applying the Energy Objectives: A guide for stakeholders'*, 1 December 2016, pp. 7–8.

105 Hansard, SA House of Assembly, 9 February 2005, p. 1452.

106 See, for example, AEMC, *'Applying the Energy Objectives: A guide for stakeholders'*, 1 December 2016, pp. 6–7.

107 Re Michael: Ex parte Epic Energy [2002] WASCA 231 at [143].

108 See, for example, AEMC, *'Applying the Energy Objectives: A guide for stakeholders'*, 1 December 2016, p. 5.

109 NEL, s. 7A(7).

110 NEL, s. 7A(6).

The legislative framework recognises the complexity of this task by providing us with significant discretion in many aspects of the decision-making process to make judgements on these matters.

A.1 Achieving the NEO to the greatest degree

Electricity determinations are complex decisions. In most cases, the provisions of the National Electricity Rules (NER) do not point to a single answer, either for our decision as a whole or in respect of particular components. They require us to exercise our regulatory judgement. For example, chapters 6 and 6A of the NER requires us to prepare forecasts, which are predictions about unknown future circumstances. Very often, there will be more than one plausible forecast,[111] and much debate amongst stakeholders about relevant costs. For certain components of our decision there may therefore be several plausible answers or several plausible point estimates.

When the constituent components of our decision are considered together, this means there will almost always be several potential, overall decisions. More than one of these may contribute to the achievement of the NEO. In these cases, our role is to make an overall decision that we are satisfied contributes to the achievement of the NEO to the greatest degree.[112]

We approach this from a practical perspective, accepting that it is not possible to consider every permutation specifically. Where there are choices to be made among several plausible alternatives, we have selected what we are satisfied would result in an overall decision that contributes to the achievement of the NEO to the greatest degree.

A.2 Interrelationships between constituent components

Examining constituent components in isolation ignores the importance of the interrelationships between components of the overall decision, and would not contribute to the achievement of the NEO. We have considered these interrelationships in our analysis of the constituent components of our final decision in the relevant attachments. Examples include:

- underlying drivers and context which are likely to affect many constituent components of our decision. For example, forecast demand affects the efficient levels of capex and opex in the regulatory control period.
- direct mathematical links between different components of a decision. For example, the level of gamma has an impact on the appropriate tax allowance; the benchmark

111 AEMC, *Rule Determination: National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006*, 16 November 2006, p. 52.

112 NEL, s. 16(1)(d).

efficient entity's debt to equity ratio has a direct effect on the cost of equity, the cost of debt, and the overall vanilla rate of return.

- trade-offs between different components of revenue. For example, undertaking a particular capex project may affect the need for opex or vice versa.

B Constituent components

This Overview and the accompanying attachments, including where appropriate attachments to our draft decision, set out our final decision on Evoenergy's distribution determination for the 2019–24 regulatory control period. Our final decision includes the following constituent components:[113]

Constituent component
In accordance with clause 6.12.1(1) of the NER, the AER's final decision is that the classification of services set out in Attachment 12 will apply to Evoenergy for the 2019–24 regulatory control period.
In accordance with clause 6.12.1(2)(i) of the NER, the AER's final decision is not to approve the annual revenue requirement set out in Evoenergy's building block proposal. Our final decision on Evoenergy's annual revenue requirement for each year of the 2019–24 regulatory control period is set out in Attachment 1 of this final decision.
In accordance with clause 6.12.1(2)(ii) of the NER, the AER's final decision is to approve Evoenergy's proposal that the regulatory control period will commence on 1 July 2019. Also in accordance with clause 6.12.1(2)(ii) of the NER, the AER's final decision is to approve Evoenergy's proposal that the length of the regulatory control period will be 5 years from 1 July 2019 to 30 June 2024.
In accordance with clause 6.12.1(3)(i) and acting in accordance with clause 6.5.7(c) of the NER, the AER's final decision is to accept Evoenergy's proposed total net capital expenditure forecast of $314.3 million ($2018–19). This is set out in Attachment 5 of this final decision.
In accordance with clause 6.12.1(4)(ii) and acting in accordance with clause 6.5.6(d) of the NER, the AER's final decision is not to accept Evoenergy's proposed total forecast operating expenditure inclusive of debt raising costs and exclusive of the demand management innovation allowance mechanism (DMIAM) of $302.0 million ($2018–19). Our final decision therefore includes a substitute estimate of Evoenergy's total forecast opex for the 2019–24 regulatory control period of $295.8 million ($2018–19) including debt raising costs and exclusive of DMIAM. This is set out in Attachment 6 of this final decision.
In accordance with clause 6.12.1(5) of the NER and the 2018 Rate of Return Instrument, the AER's final decision is that the allowed rate of return for the 2019–20 regulatory year is 5.53 per cent (nominal vanilla), as set out in section 2.2 of this final decision Overview, and that the rate of return for the remaining regulatory years 2020–24 will be updated annually because our decision is to apply a trailing average portfolio approach to estimating debt which incorporates annual updating of the allowed return on debt.
In accordance with clause 6.12.1(5A) of the NER and the 2018 Rate of Return Instrument, the AER's final decision on the value of imputation credits as referred to in clause 6.5.3 is to adopt

[113] NEL, s. 16(1)(c).

Constituent component
a value of 0.585. This is set out in section 2.2 of this final decision Overview.
In accordance with clause 6.12.1(6) of the NER, the AER's final decision on Evoenergy's regulatory asset base (RAB) as at 1 July 2019 in accordance with clause 6.5.1 and schedule 6.2 is $796.0 million and $177.3 million ($ nominal) for its distribution and transmission networks, respectively. This is set out in Attachment 2 of this final decision.
In accordance with clause 6.12.1(7) and clause 6.5.3 of the NER, the AER estimates Evoenergy's cost of corporate income tax is $12.6 million ($ nominal). This is set out in Attachment 7 of this final decision.
In accordance with clause 6.12.1(8) of the NER, the AER's final decision is to not approve the depreciation schedules submitted by Evoenergy. Our final decision substitutes alternative depreciation schedules in accordance with clause 6.5.5(b). This is set out in Attachment 4 of this final decision.
In accordance with clause 6.12.1(9) of the NER, the AER makes the following final decisions on how any applicable efficiency benefit sharing scheme (EBSS), capital expenditure sharing scheme (CESS), service target performance incentive scheme (STPIS), demand management incentive scheme (DMIS) or small-scale incentive scheme is to apply: • We will apply version two of the EBSS to Evoenergy in the 2019–24 regulatory control period. This is set out in section 3.1 of this final decision Overview. • We will apply the CESS as set out in version 1 of the Capital Expenditure Incentives Guideline to Evoenergy in the 2019–24 regulatory control period. This is set out in Attachment 9 of this final decision. • We will apply our STPIS to Evoenergy for the 2019–24 regulatory control period. This is set out in Attachment 10 of this final decision. • We will apply the DMIS and DMIAM to Evoenergy for the 2019–24 regulatory control period. This is set out in section 3.4 of this final decision Overview.
In accordance with clause 6.12.1(10) of the NER, the AER's final decision is that all appropriate amounts, values and inputs are as set out in this final decision including attachments.
In accordance with clause 6.12.1(11) of the NER and our framework and approach paper, the AER's final decision on the form of control mechanisms (including the X-factor) for standard control services is a revenue cap. The revenue cap for Evoenergy for any given regulatory year is the total annual revenue calculated using the formula in Attachment 13 plus any adjustment required to move the distribution use of system (DUoS) unders and overs account to zero. This is set out in Attachment 13 of this final decision.
In accordance with clause 6.12.1(12) of the NER and our framework and approach paper, the AER's final decision on the form of the control mechanism for alternative control services is to apply price caps for all services. This is set out in Attachment 13 of this final decision.
In accordance with clause 6.12.1(13) of the NER, to demonstrate compliance with its distribution determination, the AER's final decision is that Evoenergy must maintain a DUoS unders and overs account. It must provide information on this account to us in its annual pricing

Constituent component
proposal. This is set out in Attachment 13 of this final decision.
In accordance with clause 6.12.1(14) of the NER, the AER's final decision is to apply the following nominated pass through events for the 2019–24 regulatory control period in accordance with clause 6.5.10: • Terrorism event • Natural Disaster event • Insurance Cap event • Insurer's Credit Risk event These events have the definitions set out in section 5.2 of this final decision Overview.
In accordance with clause 6.12.1(14A) of the NER, the AER's final decision is to approve the tariff structure statement (TSS) proposed by Evoenergy. This is set out in section 4 of this final decision Overview.
In accordance with clause 6.12.1(15) of the NER, the AER's final decision is that the negotiating framework as proposed by Evoenergy will apply for the 2019–24 regulatory control period. This is set out in in section 5.3 of this final decision Overview.
In accordance with clause 6.12.1(16) of the NER, the AER's final decision is to apply the negotiated distribution services criteria published in February 2018 to Evoenergy. This is set out in section 5.3 of this final decision Overview.
In accordance with clause 6.12.1(17) of the NER, the AER's final decision on the policies and procedures for assigning retail customers to tariff classes, or reassigning retail customers from one tariff class to another (including any applicable restrictions), for Evoenergy is set out in Attachment 13 of this final decision.
In accordance with clause 6.12.1(17A) of the NER, the AER's final decision is to approve Evoenergy's proposed pricing methodology for transmission standard control services. This is set out in section 5.5 of this final decision Overview.
In accordance with clause 6.12.1(18) of the NER, the AER's final decision is that the depreciation approach based on forecast capex (forecast depreciation) is to be used to establish the RAB at the commencement of Evoenergy's regulatory control period as at 1 July 2024. This is set out in Attachment 2 of this final decision.
In accordance with clause 6.12.1(19) of the NER, the AER's final decision on how Evoenergy is to report to the AER on its recovery of designated pricing proposal charges is to set this out in its annual pricing proposal for each regulatory year of the 2019–24 regulatory control period. The method to account for the under and over recovery of designated pricing proposal charges is set out in Attachment 13 of this final decision.
In accordance with clause 6.12.1(20), the AER's final decision is to require Evoenergy to maintain a jurisdictional scheme unders and overs account. It must provide information on this account to us in its annual pricing proposal as set out in Attachment 13 of this final decision.
In accordance with clause 6.12.1(21) of the NER, the AER's final decision is to apply

Constituent component
Evoenergy's proposed connection policy. This is set out in section 5.4 of this final decision Overview.

C List of submissions

We received 6 submissions in response to our draft decision and Evoenergy's revised revenue proposal. These are listed below.

Submission from	Date received
ActewAGL	14 January 2019
ACT Technical Regulator	15 January 2019
Consumer Challenge Panel (CCP10)	15 January 2019
Electrical Trades Union of Australia (ETU)	11 January 2019
Evoenergy Energy Consumer Reference Council (ECRC)	4 January 2019
Pre Power One Co-op	10 January 2019