Draft Decision

Murraylink Transmission Determination 2023 to 2028

(1 July 2023 to 30 June 2028)

Attachment 9
Capital expenditure sharing scheme

September 2022

AUSTRALIAN ENERGY REGULATOR

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Note

This attachment forms part of the AER's draft decision on Murraylink's 2023–28 transmission determination. It should be read with all other parts of the draft decision.

The draft decision includes the following documents:

Overview

Attachment 1 – Maximum allowed revenue

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency benefit sharing scheme

Attachment 9 – Capital expenditure sharing scheme

Attachment 10 – Service target performance incentive scheme

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9 Capital expenditure sharing scheme

The capital expenditure sharing scheme (CESS) provides financial rewards to network service providers whose capital expenditure (capex) becomes more efficient and financial penalties for those that become less efficient. Consumers benefit from improved efficiency through lower regulated prices. We first applied the CESS to Murraylink in the 2018–23 regulatory control period.

This attachment sets out our decision for both the determination of the revenue impacts as a result of the CESS applying in the 2018–23 regulatory control period, and the application of the CESS for Murraylink in the 2023–28 regulatory control period.

The CESS approximates efficiency gains and efficiency losses by calculating the difference between forecast and actual capex. It shares these gains or losses between service providers and consumers. Under the CESS a service provider retains 30% of an under-spend or over-spend, while consumers retain 70% of the under-spend or over-spend. This means that for a one dollar saving in capex the service provider keeps 30 cents of the benefit while consumers keep 70 cents of the benefit.

The CESS works as follows:

1. We calculate the cumulative efficiency gains or losses for the current regulatory control period in net present value terms.
2. We apply a ratio of 30% to the cumulative under-spend or over-spend to work out the service provider's share of the under-spend or over-spend.
3. We calculate the CESS revenue increment/decrement taking into account the financing benefit, or cost, to the service provider of the under-spend or over-spend.[1] We can also make a further adjustment to account for deferral of capex and ex post exclusions of capex from the regulatory asset base (RAB).[2]
4. The CESS revenue increment/decrement is added or subtracted to the service provider's regulated revenue as a separate building block in the next regulatory control period.

9.1 Draft decision

9.1.1 Revenue impacts in the 2023–28 period from applying the CESS in the 2018–23 period

Our draft decision is to apply a CESS revenue increment amount of $0.47 million ($2022–23) from the application of the CESS in the 2018–23 regulatory control period.[3] CESS revenue increments arise as a result of an underspend in capex against the forecast for the relevant period (in this case, the 2018–23 period).

1 We calculate benefits as the benefits to the service provider of financing the under-spend since the amount of the under-spend can be put to some other income generating use during the period. Losses are similarly calculated as the financing cost to the service provider of the over-spend.

2 The capex incentive guideline outlines how we may exclude capex from the RAB. AER, Capex incentive guideline, November 2013, pp. 13–20.

3 NER, cl. 6A.14.1(5A).

Our draft decision on the revenue impact of the application of the CESS in the 2018–23 period is summarised in Table 9.1.

Table 9.1 AER's draft decision on Murraylink's CESS revenue increment ($million, 2022–23)

	2022–23	2023–24	2024–25	2025–26	2026–27	Total
Murraylink's proposal	0.07	0.07	0.07	0.07	0.07	0.35
AER draft decision	0.09	0.09	0.09	0.09	0.09	0.47

Source: Murraylink, Revenue Proposal 2023–27, Attachment 06 - Reset RIN - workbook 4 - CESS, 31 January 2022 and AER analysis.
Note: Numbers may not add up due to rounding.

Given the timing of this draft decision, we calculated the CESS revenue increments in Table 9.1 using estimates of Murraylink's capex for 2021–22 and 2022–23 regulatory years. The CESS revenue increment we calculated ($0.47 million) is different to the revenue increment that Murraylink proposed ($0.35 million) because we applied updated modelling inputs, including inflation and the rate of return.

9.1.2 Application of the CESS in the 2023–28 period

We will apply the CESS as set out in version 1 of the capital expenditure incentives guideline to Murraylink in the 2023–28 regulatory control period.[4] The guideline provides for the exclusion from the CESS of capex the service provider incurs in delivering a priority project approved under the network capability component of the service target performance incentive scheme (STPIS) for transmission network service providers.[5] This is consistent with the proposed approach we set out in our framework and approach paper.[6]

9.2 Murraylink's proposal

Murraylink proposed a $0.35 million ($2022–23) CESS revenue increment to its regulated revenue in the 2023–28 regulatory control period.[7]

9.3 Assessment approach

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

- the revenue impacts on Murraylink arising from applying the CESS in the 2018–23 regulatory control period
- whether or not to apply the CESS to Murraylink in the 2023–28 regulatory control period and how any applicable scheme will apply.[8]

4 AER, *Capital Expenditure Incentive Guideline*, November 2013, pp. 5–9.

5 AER, *Capital Expenditure Incentive Guideline*, November 2013, p. 6.

6 AER, *Framework and approach Murraylink 2023–28*, July 2021.

7 Murraylink, *Revenue Proposal 2023–27, Capital Expenditure Sharing Scheme Model,* 31 January 2022.

8 NER, cl. 6A.14.1(5A).

We must determine the appropriate revenue increments or decrements (if any) for each year of the 2023–28 period arising from the application of the CESS during the 2018–23 period.[9]

We must also determine how any applicable CESS is to apply to Murraylink in the 2023–28 period.[10] In deciding whether to apply a CESS to Murraylink for the 2023–28 period, and the nature and details of the scheme, we must:[11]

- make that decision in a manner that contributes to the capex incentive objective[12]
- take into account the CESS principles,[13] the capex objectives and, where relevant, the operating expenditure (opex) objectives,[14] the interaction with other incentive schemes,[15] and the circumstances of the service provider.[16]

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

9.3.1 Interrelationships

The approval of CESS revenue increment/decrement determines the associated CESS building block as part of Murraylink's overall forecast revenue requirement for the 2023–28 regulatory control period.

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

9.4 Reasons for draft decision

9.4.1 CESS revenue increments from application of the CESS in the 2018–23 regulatory control period

We consider Murraylink should receive a CESS revenue increment of $0.47 million ($2022–23) from the application of version 1 of the CESS during the 2018–23 regulatory control period. This means that Murraylink's allowed revenue in the 2023–28 regulatory control period is $0.47 million more than it would otherwise have been due to the application of the CESS to Murraylink in the 2018–23 regulatory control period.

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9 NER, cl. 6A.5.4(a)(5).

10 NER, cl. 6A.14.5(5A).

11 NER, cl. 6A.6.5A(e).

12 NER, cl. 6A.6.5A(e)(3); the capex incentive objective is set out in cl. 6A.5A (a).

13 NER, cl. 6A.6.5A(e)(4)(i); the CESS principles are set out in cl.6A.6.5A(c).

14 NER, cll. 6A.6.5A(e)(4)(i) and 6A.6.5A(d)(2); the capex objectives are set out in cl. 6A.6.7(a); the opex objectives are set out in cl. 6A.6.6(a).

15 NER, cll. 6A.6.5A(e)(4)(i) and 6A.6.5A(d)(1).

16 NER, cl. 6A.6.5A(e)(4)(ii).

The timing of our draft decision means that the 2021–22 and 2022–23 regulatory year incurred capex figures used to calculate the CESS revenue increments are estimates. Our capital expenditure incentive guideline provides for the calculation of CESS revenue amounts to use both actual and estimated capex for all years of the current period to determine the CESS revenues in the forecast period.

Given that the 2022–23 regulatory year capex will be an estimate at the time of our final decision we may need to make further adjustments to the revenue amount where actual underspending or overspending in the 2022–23 regulatory year is different to the estimate. These adjustments will be made when we undertake our revenue determination for the subsequent regulatory control period.

Our calculation of the CESS is in accordance with section 2.3 of version 1 of the capital expenditure incentive guideline.[17]

In the 2018–23 regulatory control period, Murraylink was subject to version 1 of the CESS. Under this scheme the CESS revenue increments are to be based on the difference between:

- approved forecast capex set out in our determination for Murraylink for the 2018–23 regulatory control period
- actual capex for the 2018–23 regulatory control period, after the removal of any excluded cost categories such as Network capability incentive parameter action plan (NCIPAP) capex and asset disposals.[18]

The formulas for calculating the revenue increments are set out in our determination CESS model.[19]

The CESS revenue increment we calculated ($0.47 million) is different to the revenue increment that Murraylink proposed ($0.35 million) because we have used:

- more recent inflation figures; and
- an updated weighted average cost of capital input information.

9.4.2 Application of the CESS in the 2023–28 regulatory control period

The reasons for our preference for a CESS are set out in our capital expenditure incentive guideline.[20] In developing the guideline we took into account the capex incentive objective, capex criteria, capex objectives and the national electricity objective (NEO).

We will apply version 1 of the CESS to Murraylink in the 2023–28 regulatory control period.[21] As we have set out in the framework and approach we consider the CESS is needed to provide Murraylink with a continuous incentive to pursue efficiency gains.

17 AER, *Capital Expenditure Incentive Guideline*, November 2013, p. 6.

18 An estimate of 2021-22 and 2022–23 capex has been used for the draft decision.

19 AER, *Murraylink draft decision 2023–28 CESS model*, September 2022.

20 AER, *Capital Expenditure Incentive Guideline*, November 2013.

21 AER, *Capital Expenditure Incentive Guideline*, November 2013.

Glossary

Term	Definition
AER	Australian Energy Regulator
Capex	Capital expenditure
CESS	Capital expenditure sharing scheme
EBSS	Efficiency benefit sharing scheme
NCIPAP	Network capability incentive parameter action plan
NEO	National Electricity Objective
NER	National Electricity Rules
Opex	Operating expenditure
RAB	Regulatory asset base
STPIS	Service target performance incentive scheme