AUSTRALIAN ENERGY REGULATOR

Final decision: TasNetworks Electricity distribution determination 2017–19

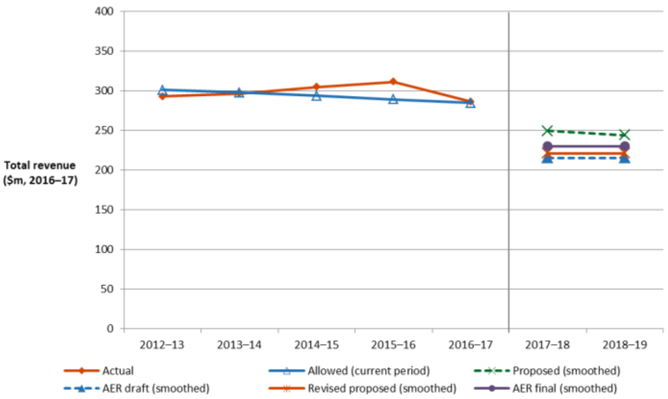
Overview

The Australian Energy Regulator (AER) regulates the revenues of TasNetworks by setting the annual revenue it may recover from its customers.

Our final decision allows TasNetworks to recover $477.3 million ($nominal) from its customers over two years commencing 1 July 2017. This results in average annual revenues over the 2017–19 regulatory period of $230.1 million ($2016–17), compared to $293.1 million ($2016–17) over the previous (2012–17) regulatory period.

The figure below shows the difference between TasNetworks' proposed revenue, and what we have allowed for each year of the regulatory period.

TasNetworks' past and proposed total revenue and AER final decision revenue allowance ($million, 2016–17)



TasNetworks consulted with its customers and proposed substantial savings in operating its distribution network. As a consequence, in our final decision we have been able to accept most of TasNetworks' regulatory proposal, including its capital and operating expenditure forecasts. We also accepted the methodology proposed by TasNetworks to calculate its rate of return, which we have updated to reflect current market conditions.

Our final decision allows TasNetworks to recover more revenue than in its revised proposal and our draft decision, due to an increase in the allowed rate of return. This increase is reflective of a rise in government bond rates since TasNetworks submitted its revised proposal and ensures that the rate of return reflects prevailing market conditions.

Estimated impact on customer bills

The revenue we determine affects the distribution component of a customer's electricity bill. Distribution charges may make up approximately 41 per cent of the bill for a typical Tasmanian residential customer.

As a result of the reductions proposed in our final decision, we expect that the distribution component of the average annual residential electricity bill in 2018–19 would reduce by about $110 below the 2016–17 level. We also expect the distribution component of the average annual small business electricity bill in 2018–19 would reduce by about $184 below the 2016–17 level.

Other components of customer bills include the cost of generation, transmission, and retailer costs. The AER regulates the transmission and distribution components only, it does not influence the cost of generation or set retail prices.

Key elements of our decision

We based our assessment of TasNetworks' proposed revenue on a number of components. These include expenditures to maintain and operate the network, and the return to shareholders on their investment. Together, these determine the revenue that TasNetworks may recover from its customers.

Two components of our final decision drive most of the difference between the revenue that TasNetworks was allowed to recover in the 2012–17 regulatory period, and the level of revenue approved for the 2017–19 regulatory period: rate of return, and operating expenditure (opex).

We discuss each of these below.

Rate of return

Significant investment is required to build a transmission network. The return TasNetworks must pay lenders and investors is referred to as the rate of return. Even a small difference in the rate of return can have a big impact on revenues.

Our final decision sets the allowed rate of return (or 'cost of capital') at 6.02 per cent for 2017–18. This is a significant decrease compared to the rate of return approved in our previous (April 2012) final decision for TasNetworks (formerly Aurora Distribution) of 8.28 per cent.

We set out our approach to determining the rate of return in the Rate of Return Guideline (Guideline) we published in December 2013. In its proposal, TasNetworks proposed to use the methodology set out in our Guideline. We have accepted the approach proposed by TasNetworks for calculating the rate of return.

This approach requires us to consider prevailing market conditions. The investment environment has improved since our previous decision, which was made during the period of uncertainty surrounding the global financial crisis. This improved investment environment translates to lower financing costs necessary to attract efficient investment.

The lower rate of return in this final decision will reduce TasNetworks' average annual revenue requirement compared to the previous regulatory control period.

Operating expenditure

Opex includes forecast operating, maintenance and other non–capital costs incurred in the provision of network services. It includes labour costs and other non-capital costs that TasNetworks is likely to require during the 2017–19 regulatory period for the efficient operation of it network.

TasNetworks proposed a lower opex forecast for the 2017–19 regulatory period compared with what it was allowed to recover during the 2012–17 regualtory period. This decrease reflects efficiency gains made over the 2012–17 regulatory period. These efficiency gains are largely the result of the synergies associated with the merger of TasNetworks' transmission and distribution networks in 2014.

Our final decision accepts TasNetworks' proposed opex forecast. This lower opex forecast will reduce TasNetworks' average annual revenue requirement compared to the previous regulatory control period.

For more information

More information on TasNetworks' proposal, and our final decision can be found on our website: [www.aer.gov.au.](http://www.aer.gov.au)