

**Determination  
Network support pass  
through applications for  
the 2019–20 and 2020–21  
regulatory years  
TransGrid**

**December 2021**

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# Contents

- Overview ..... 1**
- 1 Determination ..... 2**
- 2 TransGrid’s applications ..... 3**
  - 2.1 Background ..... 3
  - 2.2 Regulatory requirements ..... 3
  - 2.3 Guidelines for transmission network support pass through applications ..... 4
  - 2.4 TransGrid’s proposed pass through amounts ..... 4
- 3 AER assessment ..... 6**
  - 3.1 Negative network support events ..... 6
  - 3.2 Relevant factors ..... 6
  - 3.3 Calculation of the pass through events ..... 6
  - 3.4 Timing matters ..... 9
- Glossary ..... 10**

## Overview

On 22 September 2021, TransGrid submitted two applications to the Australian Energy Regulator (AER) to pass through costs relating to network support. One application was for the 2019–20 regulatory year and the other for the 2020–21 regulatory year.

TransGrid is a provider of electricity transmission network services in New South Wales.

Network support refers to non-network solutions used by transmission network service providers (TNSPs) as a cost effective substitute for network augmentation. Potential non-network solutions include local generation, co-generation, demand side response and services from a Market Network Service Provider. Generally, network support is seen as desirable where it can cost effectively substitute for network build and is promoted by allowing TNSPs to pass through network support payments which are different to those forecast and are beyond the TNSPs' control<sup>1</sup>. In addition, unlike other pass throughs, network support pass through events are not subject to any materiality test under the regulatory regime, which is intended to further promote such measures.

We have assessed both of TransGrid's pass through applications in accordance with the National Electricity Rules (NER) and our procedural guideline for preparing a transmission network support pass through application.<sup>2</sup>

We determine that:

- A negative network support event has occurred for TransGrid in both the 2019–20 and 2020–21 regulatory years.
- In relation to the 2019–20 regulatory year, the negative network support pass through amount is \$1,621,707
- In relation to the 2020–21 regulatory year, the negative network support pass through amount is \$5,348,008.

The cumulative negative network support pass through amount of \$6,969,715 (\$nominal, 2022–23) will be subtracted from allowed revenues for the next regulatory year (2022–23) and result in slightly lower transmission charges (other things constant).

<sup>1</sup> See, NER, Chapter 10 (definition of 'network support payment').

<sup>2</sup> AER, Procedural guideline for preparing a transmission network support pass through application, June 2011.

# 1 Determination

We consider that a negative network support event has occurred in both the 2019–20 and 2020–21 regulatory years<sup>3</sup> and approve negative network support pass through amounts of \$1,621,707 (\$nominal, 2022–23) and \$5,348,008 (\$nominal, 2022–23) for each year respectively. This is due to network support costs being lower in 2019–20 and 2020–21 than the allowance forecast for such costs in TransGrid's revenue determination. The approved network support pass through amounts will be adjusted in TransGrid's maximum allowed revenue for the 2022–23 regulatory year in accordance with the procedures set out in TransGrid's 2018–23 revenue determination.

The NER require us to determine the amount that should be passed through to customers.<sup>4</sup> We base our decision on an assessment of the factors set out in clause 6A.7.2(i) of the NER. On 22 September 2021, TransGrid proposed negative network support pass through amounts of \$1,585,450 (\$nominal, 2022–23) and \$5,372,970 (\$nominal, 2022–23) for the 2019–20 and 2020–21 regulatory years respectively, to be recovered from its transmission network users in 2022–23.

We have verified the actual network support costs TransGrid incurred through its 2019–20 and 2020–21 Regulatory Financial Reports (provided in response to our Regulatory Information Notices). Additionally, we have adjusted Transgrid's proposed network support pass through amounts through the use of updated consumer price index (CPI) figures and this resulted in a slightly different pass through amounts, compared to TransGrid's proposal.

<sup>3</sup> A negative change event is defined in the NER as a pass through event which entails the transmission network service provider incurring materially lower costs in providing prescribed transmission services than it would have incurred but for that event. See NER, chapter 10 Glossary.

<sup>4</sup> NER, cl. 6A.7.2(f).

## 2 TransGrid's applications

TransGrid submitted its network support pass through applications on 22 September 2021. Both applications are available on our website.<sup>5</sup>

### 2.1 Background

Revenue determinations for TNSPs include forecast allowances for network support payments.

A network support event occurs when the actual amount of network support payments differs from the forecast amount allowed in the determination. Differences generally arise because the amount of network support required by a TNSP in a regulatory year is dependent on factors that are outside the control of the TNSP, such as weather conditions, demand levels and electricity usage patterns. The difference between the forecast cost of network support and the actual cost of network support is passed through to users in higher (or lower) charges for the use of the TNSP's transmission services.

### 2.2 Regulatory requirements

Clause 6A.7.2 of the NER provides that a TNSP may apply to the AER for a determination on a positive or negative network support event following a regulatory year.

A positive or negative network support event entails a TNSP making higher or lower network support payments in the preceding regulatory year than the amount of network support payments (if any) that is provided for in the annual building block revenue requirements for the TNSP for that regulatory year.

Where a positive or negative network support event occurs, the AER must determine a network support pass through amount.<sup>6</sup>

Clause 6A.7.2(i) of the NER lists the relevant factors that the AER must consider when making a determination on a positive or negative network support event:

- (1) the matters and proposals set out in any statement given to the AER by the Transmission Network Service Provider under paragraph (c);
- (2) in the case of a positive network support event, the increase in costs in the provision of prescribed transmission services that the provider has incurred in the preceding regulatory year as a result of the positive network support event;
- (3) in the case of a positive network support event, the efficiency of the provider's decisions and actions in relation to the risk of the event, including whether the provider has failed to take any action that could reasonably be taken to reduce the magnitude of the positive network support event and whether the provider has taken or omitted to take any action where such action or omission has increased the magnitude of the amount in respect of that event;
- (4) the time cost of money based on the allowed rate of return for the provider for the relevant regulatory control period;

<sup>5</sup> <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/cost-pass-throughs>.

<sup>6</sup> NER, cl. 6A.7.2(d) and 6A.7.2(f).

- (5) the need to ensure that the provider only recovers any actual increment in costs under this paragraph (i) to the extent that such increment is solely as a consequence of a network support event; and
- (6) any other factors the AER considers relevant.

The NER does not require that any materiality threshold be applied to network support pass throughs as opposed to other or most pass through events. The reason for this is to encourage the use of non-network solutions.

## 2.3 Guidelines for transmission network support pass through applications

We released a guideline detailing our approach to assessing network support cost pass throughs in June 2011 (guideline).<sup>7</sup> The guideline was prepared in order to assist TNSPs in preparing their network support pass through applications. The guideline increases the transparency of the process applying to network support pass through arrangements.

The guideline provides information regarding what steps we will take in assessing an application for a network support cost pass through, and what information is required from TNSPs for the process. The basic steps to assessing an application are:

- Assessing whether a network support event has occurred
- Verifying the network support payments
- Checking the calculations for the pass through amount, including steps taken to compensate the TNSP or its users for the time cost of money
- Assessing the efficiency of a network support provider's decisions and actions in relation to the risk of an event.

For further detail, the guideline can be found at <http://www.aer.gov.au/node/972>.

We have considered TransGrid's applications for the network support pass throughs in accordance with the NER and the guideline, and our reasoning is set out below.

## 2.4 TransGrid's proposed pass through amounts

On 22 September 2021, TransGrid applied to the AER for negative network support pass throughs of \$1,585,450 (\$nominal, 2022–23) for the 2019–20 regulatory year and \$5,372,970 (\$nominal, 2022–23) for the 2020–21 regulatory year. This reflects TransGrid's calculation of the differences between the allowance TransGrid received for network support payments as part of its revenue determination and what TransGrid actually spent on network support in the relevant periods. TransGrid's revenue determination for the 2018–23 regulatory control period included an allowance for \$2,552,342 (\$2017–18) for the 2019–20 regulatory year and \$5,834,271 (\$2017–18) for the 2020–21 regulatory year.<sup>8</sup>

Both pass throughs relate to network support services incurred in relation to TransGrid's Powering Sydney's Future (PSF) project. The network support allowance approved in TransGrid's 2018–23 determination was intended to enable TransGrid to use non-network

<sup>7</sup> AER, *Procedural guideline for preparing a transmission network support pass through application*, June 2011.

<sup>8</sup> AER, *TransGrid, Post Tax Revenue Model. 2021-22 return on debt update*, January 2021; AER analysis.

solutions to manage the risk of supply outages in the inner Sydney and CBD area, before the new 330kV cable becomes operational in 2022–23.

TransGrid stated in its applications the variation between the actual and the forecasted amounts could be contributed to the following factors:

- In the 2019–20 regulatory year<sup>9</sup>:
  - The magnitude of the demand management contracted for was 15 MW less than the amount that was proposed in the RIT-T Project Assessment Conclusions Report (PACR) for PSF; and
  - One of the three contracted parties being unable to fulfil 10 MW of their contract capacity for one month, resulting no payments being made to them during this period of unavailability.
- In the 2020–21 regulatory year<sup>10</sup>:
  - COVID-19 and the changes to office-based work patterns. This resulted in a marked reduction in Inner Sydney demand as people worked from home, which removed the need to procure higher levels of demand management; and
  - One of the three contracted parties being unable to fulfil their contracted capacity resulting in no payments being made to them.

<sup>9</sup> TransGrid, *Network Support Pass Through Application 2020–21*, September 2021, p.8.

<sup>10</sup> TransGrid, *Network Support Pass Through Application 2020–21*, September 2021, p.3, p.4.



## 3 AER assessment

### 3.1 Negative network support events

The NER defines network support event as follows<sup>11</sup>:

#### **Network support event**

If, at the end of a regulatory year of a regulatory control period, the amount of network support payments made by a Transmission Network Service Provider for that previous regulatory year is higher or lower than the amount of network support payments (if any) that is provided for in the annual building block revenue requirement for the Transmission Network Service Provider for that regulatory year, this constitutes a network support event.

We determine that a negative network support event has occurred in both the 2019–20 and 2020–21 regulatory years because the network support payments made by TransGrid in 2019–20 (\$1,245,290, \$2019–20) and 2020–21 (\$1,194,829, \$2020–21) were both lower than the amount of the corresponding network support payments provided for in TransGrid's 2018–23 determination (\$2,645,693, \$2019–20) and (\$6,099,702, \$2020–21).

### 3.2 Relevant factors

As aforementioned, clause 6A.7.2(i) of the NER sets out a number of factors that we must take into account when determining the approved pass through amount following a network support event.

We have given regard to the appropriate factors:

- We have considered the matters and proposals set out by TransGrid
- We have calculated the decrease in costs TransGrid has incurred as a result of the negative network support events
- We are satisfied that TransGrid's decisions and actions in relation to the risk of the events were efficient
- We have taken into account the time cost of money to calculate the appropriate pass through amount
- We are satisfied that the costs TransGrid will recover under this determination are solely a consequence of the aforementioned network support events
- We do not consider any other factors to be relevant.

### 3.3 Calculation of the pass through events

In its applications submitted to the AER on 22 September 2021, we consider that TransGrid has incorrectly calculated the negative network support pass through amounts.

Our 2018–23 revenue determination for TransGrid made an allowance for \$2,552,342 (\$2017–18) for the 2019–20 regulatory year and \$5,834,271 (\$2017–18) for the 2020–21 regulatory year.

<sup>11</sup> NER, chapter 10 Glossary.

We determine that negative network support events have occurred in both regulatory years and the appropriate negative network support pass through amounts are \$1,621,707 (\$nominal, 2022–23) for the 2019–20 regulatory year and \$5,348,008 (\$nominal, 2022–23) for the 2020–21 regulatory year. These amounts will be subtracted from allowed revenues during the next regulatory year (2022–23) and result in lower transmission charges (other things constant).

### 3.3.1 Calculation of the pass through amount for 2019–20

To calculate the negative network support pass through amount for the 2019–20 network support event, we have used the network support cost amount of \$1,233,986 (\$nominal, 2019–20) reported in TransGrid's 2019–20 Regulatory Financial Report, provided as part of its response to our Regulatory Information Notice. This amount matches the network support cost amount in its application<sup>12</sup>.

In its application, TransGrid used the ratio of June 2020 to December 2019 when it escalated the network support cost amount of \$1,233,986 (\$nominal, 2019–20) to the end of the regulatory year. In our calculation, we have used the percentage change in the December 2018 to December 2019 quarters' CPI figures in the escalation of the network support cost amount to the end of the 2019–20 regulatory year. The December quarters' CPI figures were utilised, as December is the mid point of the regulatory year, so transactions occurring throughout the regulatory year are assumed to occur in the middle for simplicity. The network support cost amount we have used is \$1,245,290 (\$2019–20).

The same approaches as described above were taken by both TransGrid and the AER when the forecasted operating allowance for network support payments was escalated to the end of the 2019–20 regulatory year. TransGrid used the ratio of June 2020 to June 2018 in its escalation, which produced a figure of \$2,583,964 (\$2019–20). In our calculation, we used the percentage change in the December quarters' CPI figures for each year since end of the last regulatory period (June 2018), which produced a figure of \$2,645,693 (\$2019–20).

We are satisfied that TransGrid has reasonably incurred actual network support costs of \$1,245,290 (\$2019–20) compared to the applicable regulatory allowance of \$2,645,693 (\$2019–20). The variation in the expenditure meets the definition of a network support event in the NER. The contract for these network services was awarded on the basis of a competitive request for tender process<sup>13</sup> and we consider this an appropriate method for maintaining costs at an efficient level.<sup>14</sup>

To account for the time cost of money, WACC escalations are applied over the lag period between when the difference is calculated and when the network support costs are applied to the TNSP's allowed revenues. In its calculation of the 2019–20 network support event pass through amount, TransGrid used the following figures to account for the time cost of money:

<sup>12</sup> TransGrid, *Network Support Pass Through Application 2020–21*, September 2021, p.7.

<sup>13</sup> TransGrid, *Network Support Pass Through Application 2020–21*, September 2021, p.5.

<sup>14</sup> NER, cl. 6A.7.2(c)(3)(i).

- The 2020–21 nominal WACC of 6.21 per cent over one year, to account for the time between June 2020 (when the difference was calculated) and June 2021
- The 2021–22 nominal WACC of 5.94 per cent over one year, to account for the time between June 2021 and June 2022
- A further 2022–23 nominal WACC of 5.94 per cent for half a year, to account for the time between June 2022 and December 2022 (the period where the network support pass through is reflected in the its allowed revenue).<sup>15</sup>

In total, this method was used to account for the time cost of money across the two and a half year lag period between June 2020 and December 2022 and was consistent with the standard approach outlined in our guidelines. Our calculations followed this same approach.

Consequently, we determine that a negative network support event has occurred in the 2019–20 regulatory year and the appropriate negative network support pass through amount is \$1,621,707 (\$nominal, 2022–23). This amount will be subtracted from allowed revenues for the next regulatory year (2022–23).

### 3.3.2 Calculation of the pass through amount for 2020–21

To calculate the negative network support pass through amount for the 2020–21 network support event, we have used the network support cost amount of \$1,189,721 (\$nominal, 2020–21) reported in TransGrid's 2020–21 Regulatory Financial Report, provided as part of its response to our Regulatory Information Notice. This amount matches the network support cost amount in its application<sup>16</sup>.

In its application, TransGrid used the ratio of June 2021 to December 2020 CPI figures when it escalated the network support cost amount of \$1,189,721 (\$nominal, 2020–21) to the end of the 2020–21 regulatory year. In our calculation, we have used the percentage change in the December 2019 to December 2020 quarters' CPI figures in the escalation of the actual network support cost amount to the end of the 2020–21 regulatory year. The December quarters' CPI figures were utilised, as December is the mid point of the regulatory year, so transactions occurring throughout the regulatory year are assumed to occur in the middle for simplicity. The actual network support cost amount we have used is \$1,194,829 (\$2020–21).

The same approaches as described above were taken by both TransGrid and the AER when the forecasted operating allowance for network support payments was escalated to the end of the 2020–21 regulatory year. TransGrid used the ratio of June 2021 to June 2018 in its escalation, which produced a figure of \$6,133,729 (\$2020–21). In our calculation, we used the percentage change in the December quarters' CPI figures for each year since end of the last regulatory period (June 2018), which produced a figure of \$6,099,702 (\$2020–21).

We are satisfied that TransGrid has reasonably incurred actual network support costs of \$1,194,829 (\$2020–21) compared to the applicable regulatory allowance of \$6,099,702 (\$2020–21). The variation in the expenditure meets the definition of a network support event in the NER.

<sup>15</sup> AER, *TransGrid, Post Tax Revenue Model. 2021-22 return on debt update*, January 2021; AER analysis.

<sup>16</sup> TransGrid, *Network Support Pass Through Application 2020-21*, September 2021, p.3.

In its calculation of the 2020–21 network support event pass through amount, TransGrid used the following figures to account for the time cost of money:

- The 2021–22 nominal WACC of 5.94 per cent over one year, to account for the time between June 2021 (when the difference was calculated) and June 2022.
- A further 2022–23 nominal WACC of 5.94 per cent for half a year, to account for the time between June 2022 and December 2022 (the period where the network support pass through is reflected in the its allowed revenue).

This method was used to account for the time cost of money across the one and a half year lag period between June 2021 and December 2022 and was consistent with the standard approach outlined in our guidelines. Our calculations followed this same approach.

Consequently, we determine that a negative network support event has occurred in the 2020–21 regulatory year and the appropriate negative network support pass through amount is \$5,348,008 (\$nominal, 2022–23). This amount will be subtracted from allowed revenues for the next regulatory year (2022–23).

### 3.4 Timing matters

The NER provide that if a negative network support pass through event occurs (whether or not the occurrence of that event is notified by the provider to the AER within 60 business days of the end of the relevant regulatory year), the AER must conduct an assessment of the cost pass through application.<sup>17</sup> We must then make a determination within 60 business days of the business' application to us.<sup>18</sup>

The relevant regulatory years ended on 30 June 2020 and 30 June 2021. TransGrid submitted its cost pass through applications on 22 September 2021. As both applications were for negative network support events, we were required to assess and make a determination on both applications.

<sup>17</sup> NER, cl. 6A7.2(f).

<sup>18</sup> NER, cl. 6A7.2(e).

## Glossary

Term	Definition
AER	Australian Energy Regulator
CPI	Consumer price index
EOI	Expression of Interest
Guideline	Procedural guideline for preparing a transmission network support pass through application
NER	National Electricity Rules
TNSP	Transmission network service provider
WACC	Weighted average cost of capital

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