



**Draft decision: VENCorp transmission  
determination 2008-14**

Pre-determination conference  
12 December 2007

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General Manager – Network Regulation South

# Process - submission to draft

<b>1 March 2007</b>	VENCorp submits proposal
<b>30 March 2007</b>	Determination of non-compliance and request for further information
<b>1 May 2007</b>	VENCorp submits revised proposal and public consultation commences
<b>10 May 2007</b>	Public forum held on initial proposal
<b>7 June 2007</b>	VENCorp submits its proposed pricing methodology
<b>13 June 2007</b>	Submissions on proposal close
<b>[21 June 2007]</b>	<b>2007 EAPR released]</b>
<b>22 June 2007</b>	AER publishes proposed NTSC
<b>19 July 2007</b>	VENCorp provides reconciliation of its initial proposal with the 2007 EAPR
<b>3 August 2007</b>	Submissions on NTSC close
<b>30 November 2007</b>	Draft decision released
<b>12 December 2007</b>	Pre-determination conference and commencement of public consultation on draft decision

# Components of transmission determination

A transmission determination has four elements:

- For prescribed services:
  - A **revenue determination** for the provider in respect of the provision by the provider of prescribed transmission services;
  - A determination that specifies the **pricing methodology** that applies to the provider
- For negotiated services:
  - A determination relating to the provider's **negotiating framework**
  - a determination that specifies the **negotiated transmission service criteria** that apply to the provider

## Victorian derogation – chapter 9

- Application of chapter 6A to VENCorp is **modified** by Victorian derogation in chapter 9
- AER must set VENCorp's MAAR:
  - on a full cost recovery, no operating surplus basis
  - so as not to exceed VENCorp statutory electricity transmission related costs
- Re-opener provision available to VENCorp if VENCorp's costs are likely to **exceed** its MAAR in any year (to ensure full cost recovery)

# Maximum allowable aggregate revenue (MAAR)

- Building blocks differ from other TNSPs:
  - Opex
    - corporate overhead

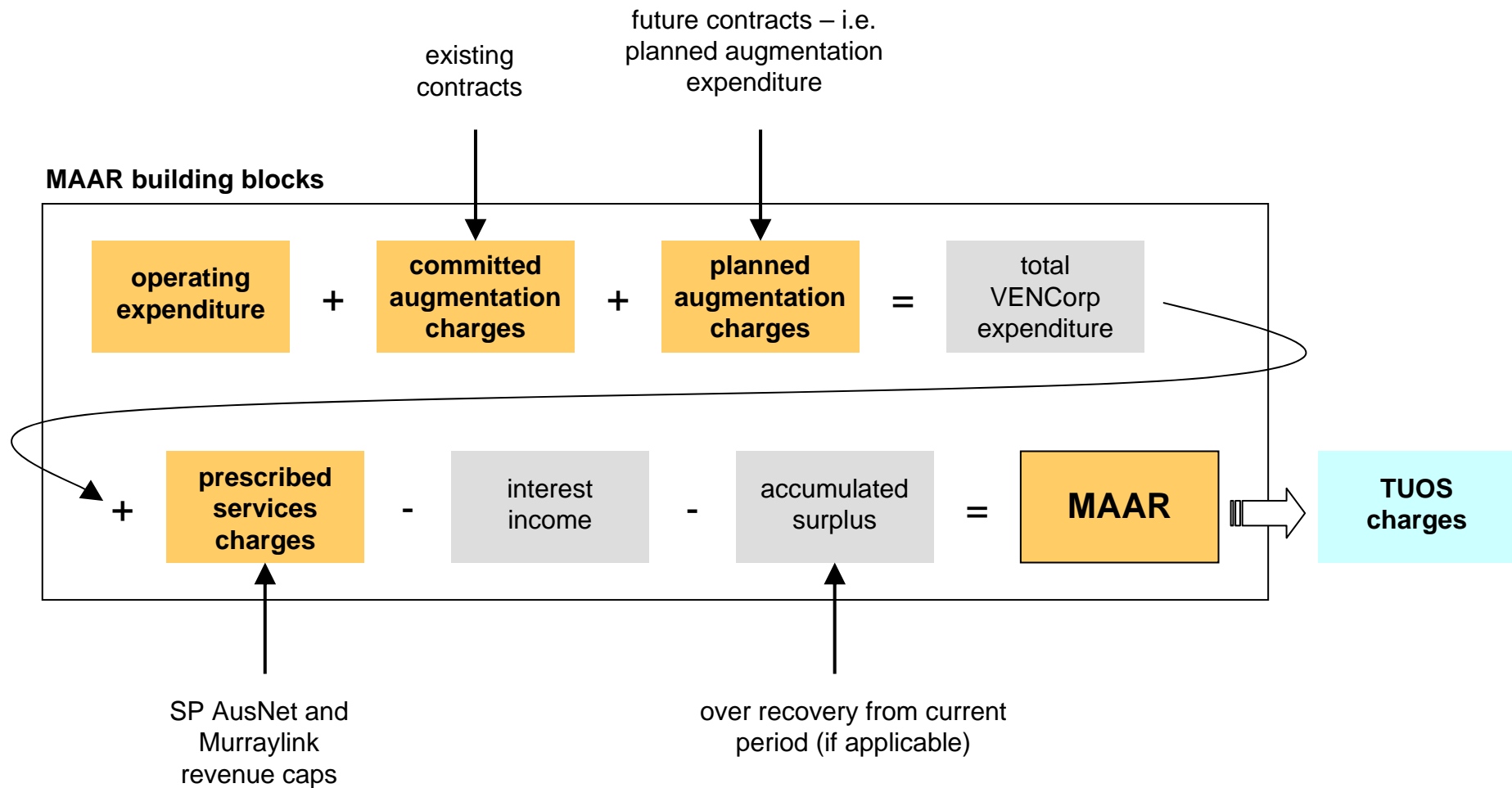
*plus*
  - Committed augmentation charges
    - expected contract charges from projects already commissioned

*plus*
  - Planned augmentation charges
    - expected contract charges for projects to be commissioned (or planned) during forthcoming regulatory period

*plus*
  - Prescribed services charges
    - expected charges for regulated services procured from SP AusNet and Murraylink (determined separately)

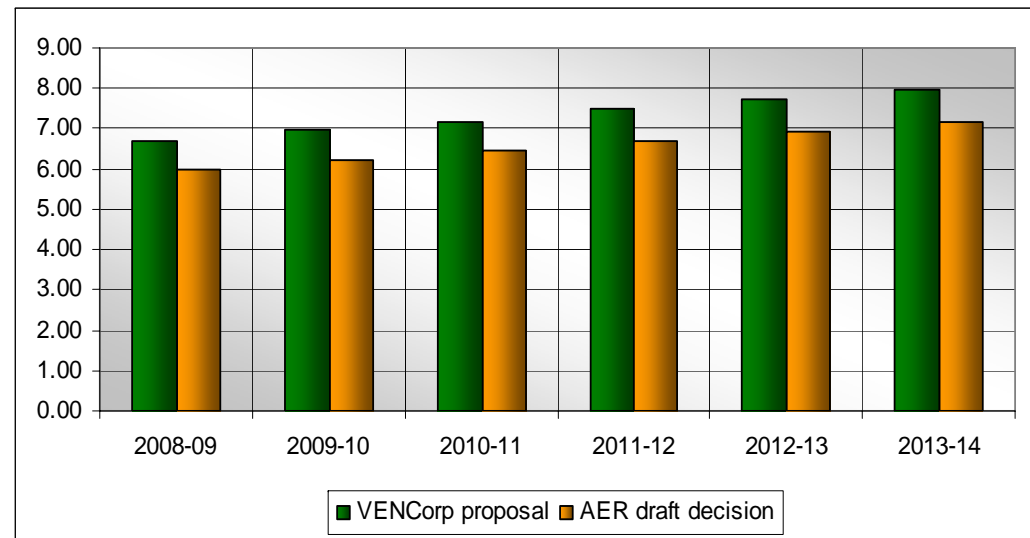
*equals*
  - MAAR

# Maximum allowable aggregate revenue (MAAR)



## Draft revenue determination – Opex

- VENCorp proposed total opex forecast of **\$44.00m** (nominal)
- AER's draft decision adjusted this forecast to **\$39.37m** (nominal) - \$4.63m reduction
- AER accepted VENCorp's base year (2006-07), but used actual, not budgeted expenditure.
- Also reversed effect of a non-cash expense item from the base year
- AER accepted VENCorp's cost escalators



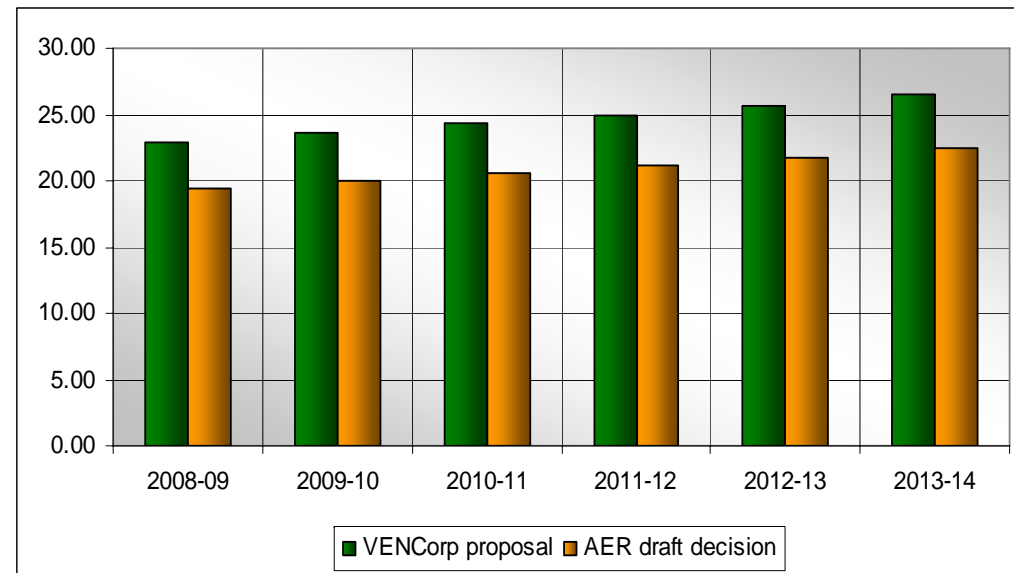
# Draft revenue determination – Committed augmentation charges

- Unlike other TNSPs, VENCorp does not own any transmission assets, but instead augments the network by procuring bulk transmission services under contract from SP AusNet
- VENCorp's committed augmentation charges are the charges payable under contracts already in existence at the commencement of the next regulatory period
- Forecast derived from the estimate of charges payable 2008-09 period, escalated by 3% per annum in each subsequent year of the regulatory period.

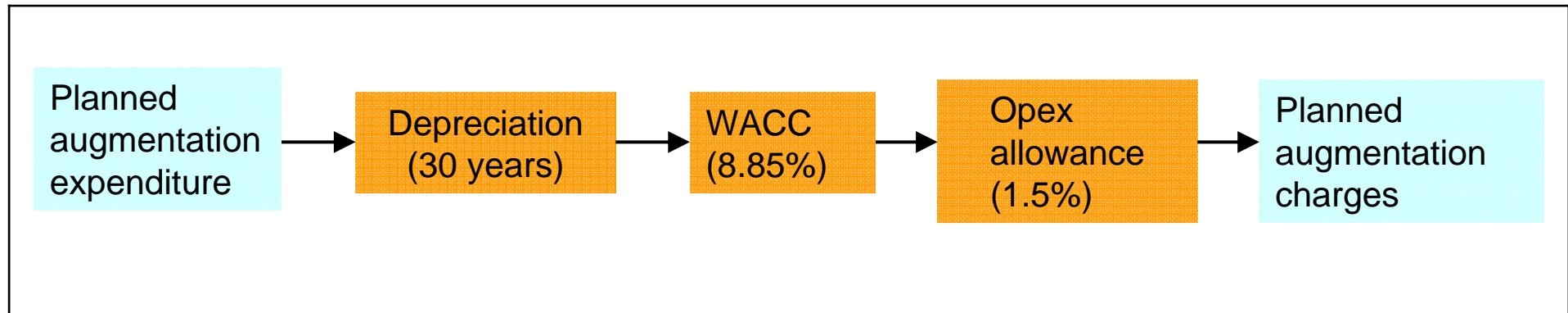


# Draft revenue determination – Committed augmentation charges

- VENCorp proposed a total of **\$148m** for committed augmentation charges.
- AER's draft decision approved a total of **\$125.16** for committed augmentation charges.
- AER's draft decision represents a reduction of \$22.84m to VENCorp's proposal to correct for material errors in calculations underlying VENCorp's forecast.



# Draft revenue determination – Forecast planned augmentation expenditure & charges

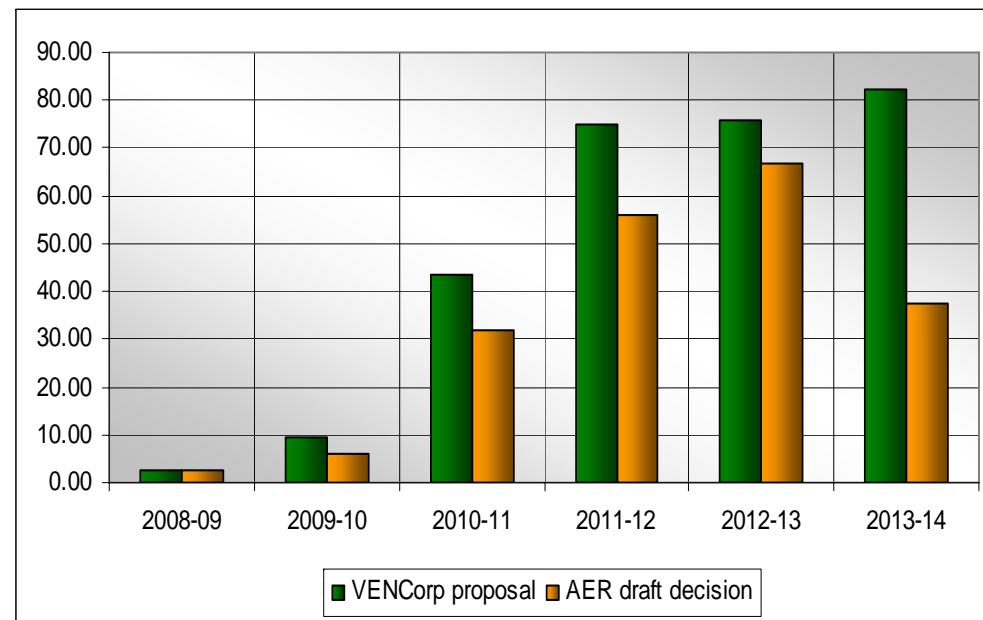


- Two stage process:
  1. An assessment of the underlying forecast planned augmentation *expenditure* and
  2. An assessment of VENCorp’s methodology to convert forecast expenditure into forecast *charges*.
- The forecast planned augmentation *charges* form the basis of the relevant building block component. VENCorp’s forecast augmentation *expenditure* does not appear in the MAAR.

# Draft revenue determination – forecast planned augmentation expenditure

- VENC Corp forecast **\$288.16m** of planned augmentation expenditure
- Draft decision approves forecast planned augmentation expenditure of **\$200.78m** (\$2007-08),
- Reduction of \$87.37m (30%) to VENC Corp's proposal.
- But 40% increase in equivalent expenditure from the current period to meet new constraints and cost pressures

AER's draft decision



# Forecast planned augmentation expenditure – AER adjustments

- *Application of appropriate cost estimates:* VENCorp's forecasts did not consider the timing of proposed projects and therefore did not reflect a realistic expectation of costs to meet the capex objectives: **-\$12.21m**
- *Detailed project reviews:* adjustments due to issues identified in detailed reviews including: forecast timing of projects not supported; unjustified need/driver for projects: **-\$50.75m**
- *Extrapolation of findings:* adjustments to other elements of forecast to implement findings of detailed review: **-\$24.42m**
- **Total AER reduction to planned augmentation = -\$87.38m**

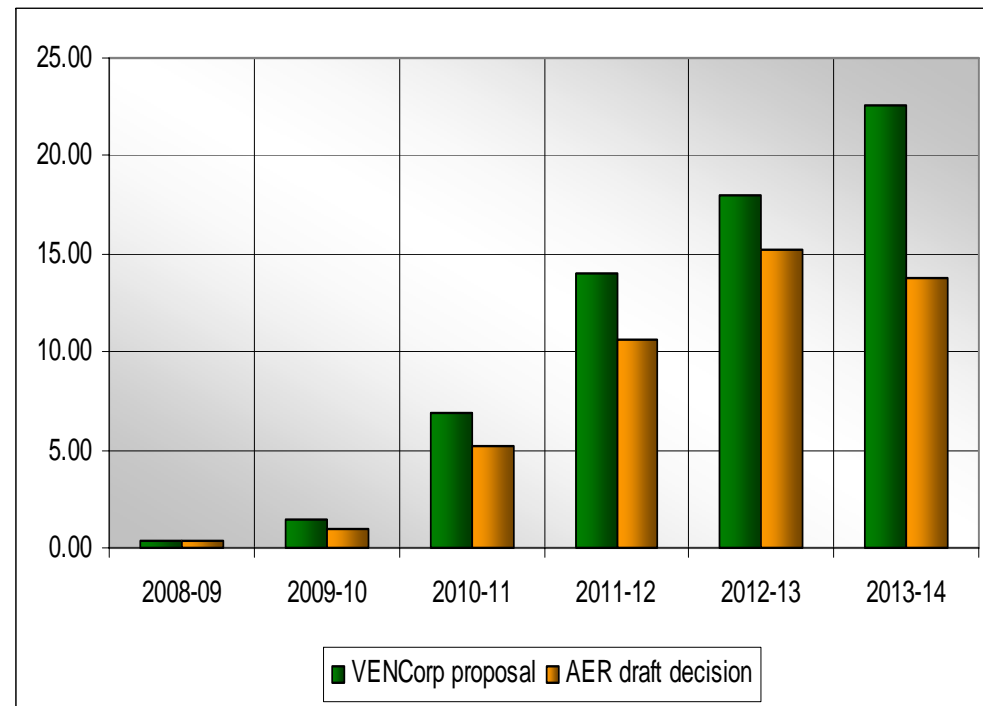
# Draft revenue determination – forecast planned augmentation charges

- VENCORP's planned augmentation charges are the charges payable under contracts expected to be entered into within the next regulatory period
- The forecast of *charges*, not *expenditure* forms the basis of the building block requirements.
- Forecast planned augmentation charges are derived from the forecast of planned augmentation expenditure through depreciation, WACC and opex assumptions from past contract experience
- The AER's draft decision accepts the methodology by which VENCORP calculated the forecast of planned augmentation charges
- AER reductions to proposed forecast result from lower forecast of underlying expenditure, and substitution of WACC value used in SP AusNet draft decision.

# Draft revenue determination – forecast planned augmentation charges

- VENCorp forecast **\$63.21m** of planned augmentation charges
- Draft decision approves forecast planned augmentation charges of **\$46.18m** (\$m, nominal)
- Reduction of \$17.03m (27%) to VENCorp's proposal.

AER's draft decision (\$m, 2007-08)



# Draft revenue determination – Prescribed services charges and other adjustments

- Prescribed services charges
  - Adjusted forecast to reflect AER's draft decision on SP AusNet's revenue cap
  - Adjusted forecast Murraylink charges, which were mistakenly based on revoked ML revenue cap
- Interest income
  - Accepted VENCorp's proposal to offset its MAAR by \$1m expected interest per annum
- AIS rebate allowance
  - VENCorp removed the AIS allowance from the prescribed services charges line of its revised proposal, after it realised SP AusNet had already asked for an allowance in its proposal.
  - However, VENCorp mistakenly did not remove the amount from the overall MAAR. The AER has corrected this.

# Draft revenue determination – Prescribed services charges and other adjustments

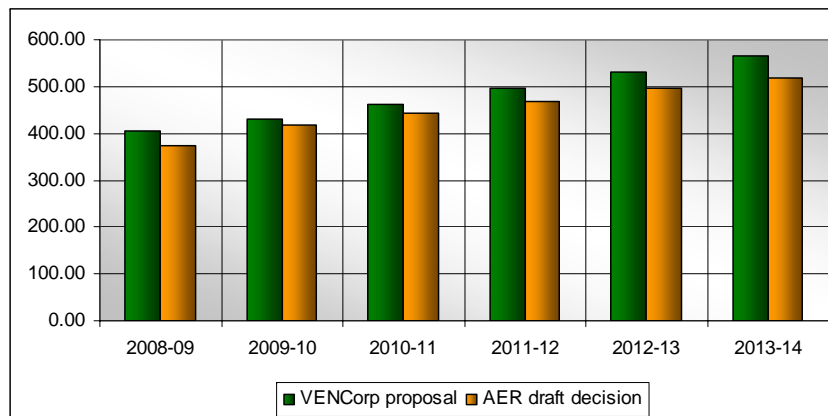
## Accumulated surplus

- Derogation requires the AER to apply any over recovery accumulated during the current period – this ensures VENCorp's MAAR is set on a full cost recovery but no operating surplus basis across regulatory periods
- VENCorp is expected to have an accumulated surplus of \$25.2m (nominal) at the end of the current regulatory period.
- AER has reduced the MAAR for the 1<sup>st</sup> year of forthcoming period by the full amount of the surplus – same process that VENCorp applies year on year during the period



# Draft revenue determination – MAAR

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	Total
Operating expenditure	5.99	6.20	6.43	6.67	6.91	7.17	39.37
Committed augmentation charges	19.35	19.93	20.53	21.14	21.78	22.43	125.16
Planned augmentation charges	0.37	1.01	5.16	10.67	15.25	13.72	46.18
<b>Total VENCORP expenditure</b>	<b>25.70</b>	<b>27.14</b>	<b>32.12</b>	<b>38.48</b>	<b>43.94</b>	<b>43.31</b>	<b>210.71</b>
Prescribed services charges	373.57	392.16	410.86	431.35	451.94	474.53	2 534.41
<i>minus</i> Interest income	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-6.00
<i>minus</i> Accumulated surplus	-25.19	-	-	-	-	-	-25.19
<b>MAAR</b>	<b>373.08</b>	<b>418.30</b>	<b>441.98</b>	<b>468.84</b>	<b>494.88</b>	<b>516.85</b>	<b>2 713.93</b>

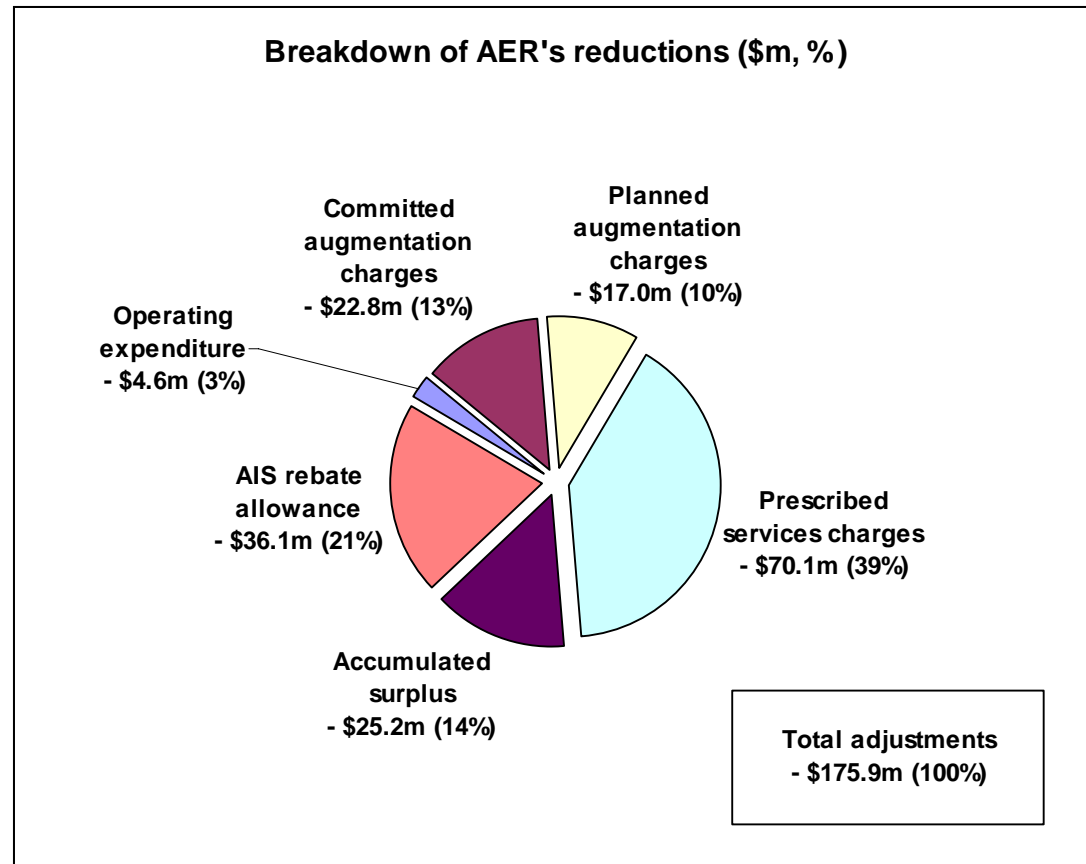


- VENCORP proposed a total MAAR of **\$2.890b** (nominal).
- AER's draft decision represents a reduction in MAAR of \$175.9m (6%) from VENCORP's proposal
- AER's draft decision approves total MAAR of **\$2.714b**

# Draft revenue determination – Breakdown of total adjustment (\$175.9m, 100%)

Adjustments to MAAR are a result of:

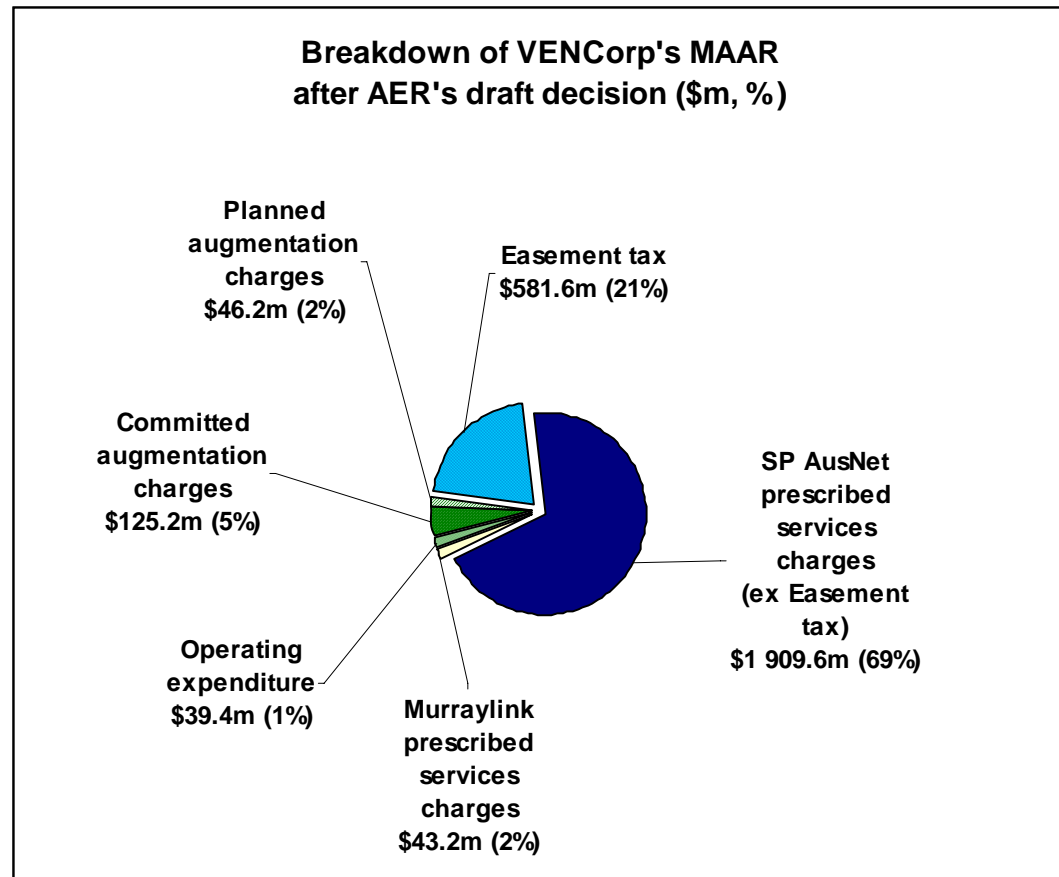
- SP AusNet draft decision (39% approx)
- Removing erroneously included rebate allowance (21%)
- Accumulated surplus (14%)
- AER's assessment of VENCorp's opex, committed charges and planned charges (26%)



# Draft revenue determination – Composition of MAAR

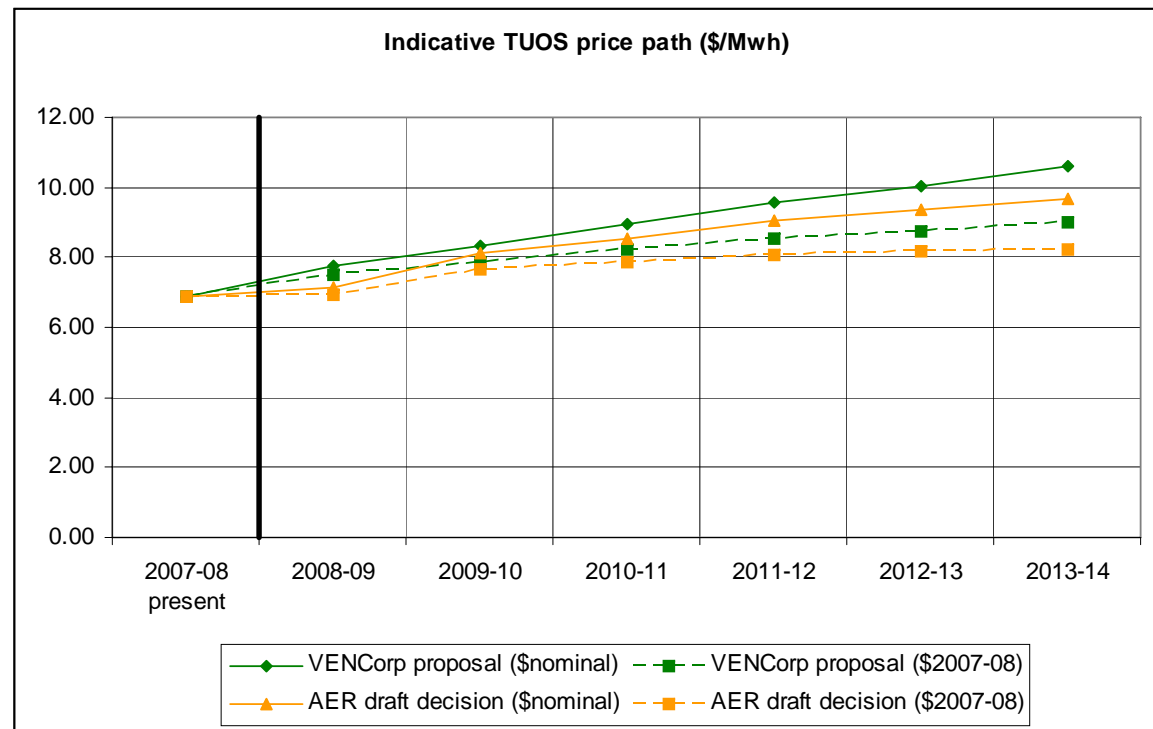
Largest components of MAAR are:

- SP AusNet charges (ex Easement tax) – 69%
- Easement tax – 21%
- Committed augmentation charges – 5%
- Planned augmentation charges, opex, Murraylink charges – less than or equal to 2% each



# Draft revenue determination – Indicative transmission price path

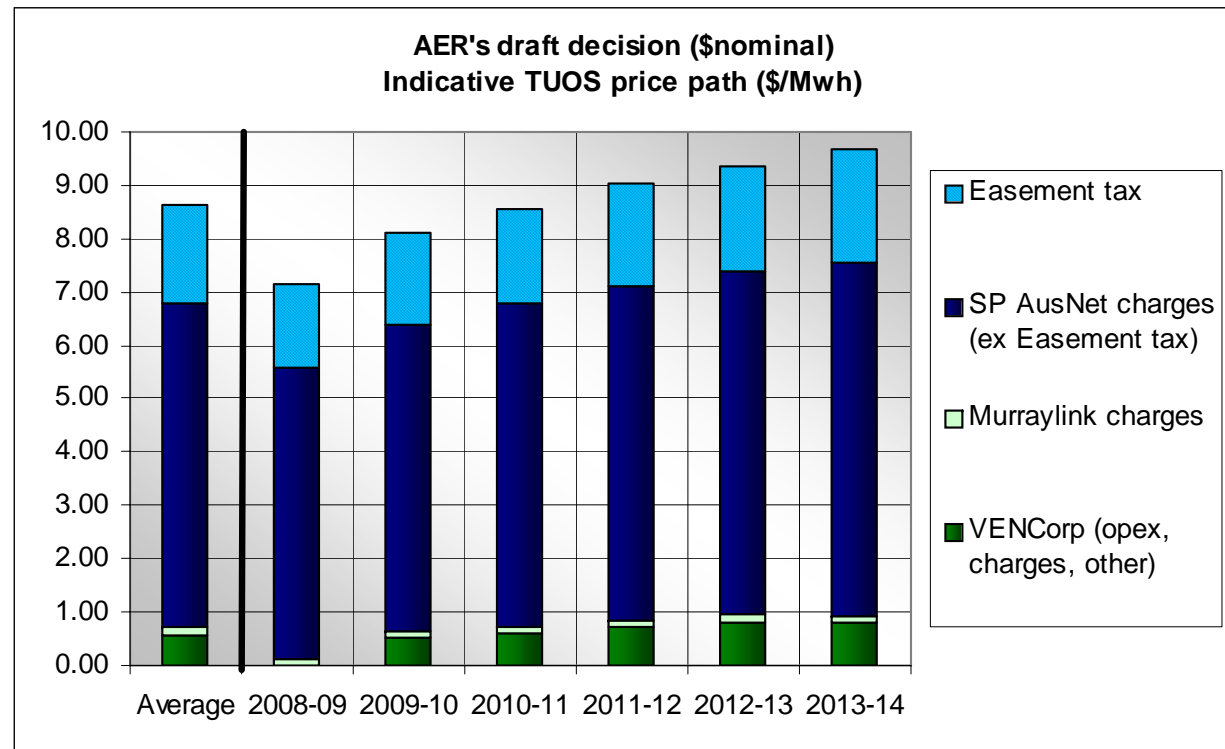
- Current price  
\$6.88/Mwh approx
- Effect of draft decision by 2013-14
  - \$9.68/Mwh (nominal)
  - \$8.20/Mwh (real \$2007-08)
- Average annual increase from present
  - VENCorp proposal
    - 7.5% nominal
    - 4.6% real
  - AER draft decision
    - 5.9% nominal
    - 3.1% real
- Assumes VENCorp demand forecasts (average 0.4% pa)
- Assumes no offsetting settlement residue received by VENCorp



# Draft revenue determination – Indicative price path

Under the draft decision:

- Effective pass-through of SP AusNet revenue cap accounts for most costs (\$6.61/Mwh average)
- Followed by easement tax (\$2.14/Mwh average)
- Other VENCORP costs small (\$0.79/Mwh average)
- Murraylink costs minimal (\$0.14/Mwh)

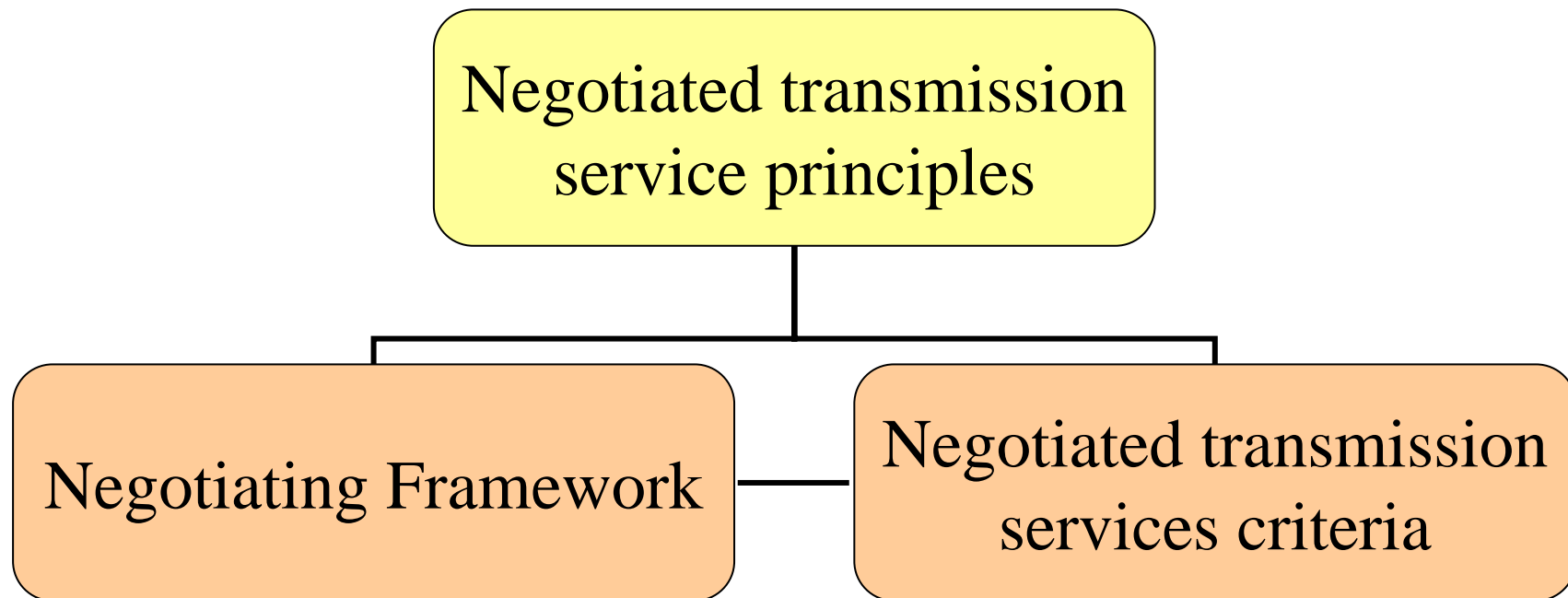


# Draft determination – Pricing methodology

- **Applies to prescribed transmission services only**
  - Allocates MAAR to service categories and connection points
  - Determines structure of prices for each category of service
- **The AER's agreed interim requirements:**
  - Developed in lieu of and prior to AER pricing guidelines
  - Required compliance with pricing principles in chapter 6A, otherwise compliance with Part C of old chapter 6
  - Allowed VENCorp to elect to have proposed methodology assessed under AER's guidelines once published (in October)
- **AER's draft decision:**
  - VENCorp developed proposed methodology under interim requirements
  - Subsequently elected to be assessed under new guidelines
  - AER required to reject methodology
  - Minor changes required (e.g. demonstration of compliance with guidelines rather than interim requirements)

# Negotiated services

- Designed to be light-handed - minimum prescription, reliance on commercial negotiation between able counter-parties
- Commercial arbitration available if necessary



# Draft determination – negotiating framework

- Sets out the procedure to be followed by VENCorp and a service applicant during negotiations for a negotiated transmission service.
- Framework must meet minimum requirements of cl.6A.9.5
- **AER's draft decision:** VENCorp's proposed negotiating framework is non-compliant in only one area:
  - purport to limit or alter the application of requirements in the NER.
- **Changes required** to VENCorp's proposal are limited to those necessary to achieve compliance.



# Draft determination – NTSC

- NTSC must be applied by VENCorp in negotiating terms and conditions of access for service applicants, and by a commercial arbitrator in the event of a dispute.
- The NTSC are determined by the AER:
  - They are the only component of the transmission determination that VENCorp is not required to propose
  - Must give effect to, and be consistent with, the negotiated transmission service principles
- NTSC for VENCorp are designed to give effect to the principles, but not extend or alter their effect.

# Process – next steps

- |                         |  |
|-------------------------|--|
| <b>14 December 2007</b> | VENCorp must resubmit pricing methodology                |
| <b>16 January 2008</b>  | VENCorp may submit revised proposal                      |
| <b>19 February 2008</b> | Submissions on draft decision and revised proposal close |
| <b>April 2008</b>       | AER final decision and transmission determination        |
| <b>1 July 2008</b>      | Transmission determination commences                     |

# Questions?