



# **FINAL DECISION**

## **SA Power Networks Distribution Determination 2020 to 2025**

### **Attachment 14 Pass through events**

June 2020

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## Note

This attachment forms part of the AER's final decision on the distribution determination that will apply to SA Power Networks for the 2020–25 regulatory control period. It should be read with all other parts of the final decision.

The final decision includes the following attachments:

### Overview

Attachment 1 – Annual revenue requirement

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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## 14 Pass through events

The pass through mechanism of the National Electricity Rules (NER) recognises that a distributor can be exposed to risks beyond its control, which may have a material impact on its costs. A cost pass through enables a distributor to recover (or pass through) the costs of defined yet unpredictable, high cost events that are not built into our distribution determination. The NER includes the following prescribed pass through events for all distributors:<sup>1</sup>

- a regulatory change event
- a service standard event
- a tax change event
- a retailer insolvency event.

In addition to these prescribed events, other pass through events may be 'nominated' by a service provider for a regulatory control period.<sup>2</sup>

This attachment sets out our final decision on the nominated pass through events that will apply to SA Power Networks for the 2020–25 regulatory control period.

### 14.1 Final decision

Our final decision is that the following nominated pass through events will apply to SA Power Networks for the 2020–25 regulatory control period:

- insurance coverage event
- insurer credit risk event
- natural disaster event
- terrorism event.

These events are defined in Table 14.1. The reasons for our decision is set out in section 14.5.

We have also considered SA Power Networks 1 April 2020 proposal to modify the natural disaster event definition to capture pandemics or epidemics, including the COVID-19 pandemic. Our final decision is to not accept these amendments at this late stage in the process. Our reasons for this decision are set out in section 14.5.1.1.

Our final decision is to not include a nominated pass through event for corporate income tax for the 2020–25 regulatory control period as proposed by SA Power Networks in its revised proposal. Further, and consistent with our draft decision, our

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<sup>1</sup> NER, cl. 6.6.1(a1)(1)–(4). Each of these prescribed events is defined in Chapter 10 (Glossary) of the NER.

<sup>2</sup> NER, cl. 6.6.1(a1)(5).

final decision is to not include a major cyber event pass through event as a nominated pass through event. Our reasons are set out in section 14.5.1.1.

**Table 14.1 Approved cost pass through definitions**

Pass through event	Definition
Insurance coverage	<p>An insurance coverage event occurs if:</p> <ol style="list-style-type: none"> <li>1. SA Power Networks:               <ol style="list-style-type: none"> <li>a) makes a claim or claims and receives the benefit of a payment or payments under a relevant insurance policy or set of insurance policies; or</li> <li>b) would have been able to make a claim or claims under a relevant insurance policy or set of insurance policies but for changed circumstances; and</li> </ol> </li> <li>2. SA Power Networks incurs costs:               <ol style="list-style-type: none"> <li>a) beyond a relevant policy limit for that policy or set of insurance policies; or</li> <li>b) that are unrecoverable under that policy or set of insurance policies due to changed circumstances; and</li> </ol> </li> <li>3. The costs referred to in paragraph 2 above materially increase the costs to SA Power Networks in providing direct control services.</li> </ol> <p>For the purposes of this insurance coverage event:</p> <ul style="list-style-type: none"> <li>• 'changed circumstances' means movements in the relevant insurance liability market that are beyond the control of SA Power Networks, where those movements mean that it is no longer possible for SA Power Networks to take out an insurance policy or set of insurance policies at all or on reasonable commercial terms that include some or all of the costs referred to in paragraph 2 above within the scope of that insurance policy or set of insurance policies.</li> <li>• 'costs' means the costs that would have been recovered under the insurance policy or set of insurance policies had:               <ol style="list-style-type: none"> <li>i. the limit not been exhausted; or</li> <li>ii. those costs not been unrecoverable due to changed circumstances.</li> </ol> </li> <li>• A relevant insurance policy or set of insurance policies is an insurance policy or set of insurance policies held during the regulatory control period or a previous regulatory control period in which SA Power Networks was regulated; and</li> <li>• SA Power Networks will be deemed to have made a claim on a relevant insurance policy or set of insurance policies if the claim is made by a related party of SA Power Networks in relation to any aspect of SA Power Networks' network or business; and</li> <li>• SA Power Networks will be deemed to have been able to make a claim on a relevant insurance policy or set of insurance policies if, but for Changed Circumstances, the claim could have been made by a related party of SA Power Networks in relation to any aspect of SA Power Networks' network or business.</li> </ul> <p>Note for the avoidance of doubt, in assessing an insurance coverage event through application under rule 6.6.1(i), the AER will have regard to:</p> <ul style="list-style-type: none"> <li>• The relevant insurance policy or set of insurance policies for the event</li> <li>• The level of insurance that an efficient and prudent DNSP would obtain, or would have sought to obtain, in respect of the event; and</li> <li>• Any information provided by SA Power Networks to the AER about SA Power Networks' actions and processes.</li> </ul>

Pass through event	Definition
Insurer credit risk	<p>An insurer credit risk event occurs if:</p> <ul style="list-style-type: none"> <li>• An insurer of SA Power Networks becomes insolvent, and as a result, in respect of an existing or potential claim for a risk that was insured by the insolvent insurer, SA Power Networks: <ul style="list-style-type: none"> <li>○ 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</li> <li>○ incurs additional costs associated with funding an insurance claim, which would otherwise have been covered by the insolvent insurer.</li> </ul> </li> </ul> <p>Note: In assessing an insurer credit risk event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>• SA Power Networks' attempts to mitigate and prevent the event from occurring by reviewing and considering the insurers track record, size, credit rating and reputation, and</li> <li>• in the event that a claim would have been made after the insurer became insolvent, whether SA Power Networks had reasonable opportunity to insure the risk with a different insurer.</li> </ul>
Natural disaster	<p>Natural disaster event means any natural disaster including but not limited to cyclone, fire, flood or earthquake that occurs during the 2020–25 regulatory control period that increases the costs to SA Power Networks in providing direct control services, provided the fire, flood or other event was:</p> <ul style="list-style-type: none"> <li>• a consequence of an act or omission that was necessary for the service provider to comply with a regulatory obligation or requirement or with an applicable regulatory instrument; or</li> <li>• not a consequence of any other act or omission of the service provider.</li> </ul> <p>Note: In assessing a natural disaster event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>• whether SA Power Networks has insurance against the event,</li> <li>• the level of insurance that an efficient and prudent NSP would obtain in respect of the event.</li> </ul>
Terrorism	<p>Terrorism event means 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:</p> <ul style="list-style-type: none"> <li>• 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</li> <li>• increases the costs to SA Power Networks in providing direct control services.</li> </ul> <p>Note: In assessing a terrorism event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>• whether SA Power Networks has insurance against the event, and</li> <li>• the level of insurance that an efficient and prudent NSP would obtain in respect of the event</li> <li>• whether a declaration has been made by a relevant government authority that a terrorism event has occurred.</li> </ul>

## 14.2 SA Power Networks' revised proposal

In our draft decision we did not accept all the nominated pass through events proposed by SA Power Networks. Instead we substituted our own definitions of natural disaster event, insurance cap event, terrorism and insurer credit risk event to provide consistency between SA Power Networks and other service providers.<sup>3</sup> We did not accept SA Power Networks' initial proposal for a 'major cyber' event.<sup>4</sup>

In its revised proposal, SA Power Networks adopted some elements of our draft decision but not others. In particular, SA Power Networks:<sup>5</sup>

- proposed a number of amendments to the insurance cap event definition
- proposed two amendments to the natural disaster event definition
- proposed a new corporate tax change pass through event
- accepted the changes to the insurer credit risk and terrorism pass through events, and the AER's decision not to include a major cyber event.

Further to the above, SA Power Networks wrote to us on 1 April 2020 proposing a modified natural disaster event definition to capture pandemics or epidemics, including the potential impact of the COVID-19 virus.<sup>6</sup>

These are discussed further in section 14.5.1.1 below.

## 14.3 Assessment approach

The NER set out how we must assess nominated pass through events, and how we must assess an application from a service provider to pass through changes in costs where an event occurs.<sup>7</sup>

Our assessment approach is guided by the National Electricity Objective (NEO) and the Revenue and Pricing Principles (RPPs).<sup>8</sup> One of the RPPs is that the service provider should have a reasonable opportunity to recover at least the efficient costs of providing services and complying with regulatory obligations.<sup>9</sup> The NEO and the RPPs

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<sup>3</sup> E.g. AER, *Draft Decision, Ausgrid distribution determination 2019–24, Attachment 14 Pass through events*, November 2018, pp. 12–13; AER, *Draft Decision, Essential Energy distribution determination 2019–24, Attachment 14 Pass through events*, November 2018, pp. 11–13; AER, *Draft Decision, Ergon Energy distribution determination 2020–25, Attachment 14 Pass through events*, October 2019, pp. 11–13; AER, *Draft Decision, Energex distribution determination 2020–25, Attachment 14 Pass through events*, October 2019, pp. 11–13.

<sup>4</sup> AER, *Draft Decision, SA Power Networks' determination, Attachment 14*, October 2019.

<sup>5</sup> SA Power Networks, *2020–25 Revised Regulatory Proposal, Attachment 13, Pass throughs*, p. 6.

<sup>6</sup> SA Power Networks, *Letter – to AER re natural disaster pass through event*, 1 April 2020.

<sup>7</sup> NER, cl. 6.5.10(b), 6.6.1.

<sup>8</sup> NEL, ss. 7 and 7A.

<sup>9</sup> NEL, s. 7A(2).



also reflect the importance of incentives to promote economic efficiency,<sup>10</sup> and balance the risks of under and over investment.<sup>11</sup>

In the context of pass through events, we have particular regard to the impact on price, quality, reliability and security of supply that may arise as a result of any change in the efficient operation of, and ability and incentive of, a service provider to invest in its network. This is a similar approach to that taken by the Australian Energy Market Commission (AEMC) when considering pass through event rule changes.<sup>12</sup>

In determining whether we accept a nominated pass through event, we must take into account the 'nominated pass through event considerations' as defined, which are as follows:<sup>13</sup>

- whether the event proposed is an event covered by a category of pass through event specified in clause 6.6.1(a1)(1) to (4) (in the case of a distribution determination) or clause 6A.7.3(a1)(1) to (4) (in the case of a transmission determination);
- whether the nature or type of event can be clearly identified at the time the determination is made for the service provider;
- whether a prudent service provider could reasonably prevent an event of that nature or type from occurring or substantially mitigate the cost impact of such an event;
- whether the relevant service provider could insure against the event, having regard to:
  - the availability (including the extent of availability in terms of liability limits) of insurance against the event on reasonable commercial terms; or
  - whether the event can be self-insured on the basis that:
    - it is possible to calculate the self-insurance premium; and
    - the potential cost to the relevant service provider would not have a significant impact on the service provider's ability to provide network services; and
- any other matter the AER considers relevant and which the AER has notified network service providers is a nominated pass through event consideration.

The AEMC described the purpose of the nominated pass through event considerations as:

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<sup>10</sup> NEL, s. 7A(3).

<sup>11</sup> NEL, s. 7A(6).

<sup>12</sup> AEMC 2012, *Cost pass through arrangements for Network Service Providers, Rule Determination*, 2 August 2012, p. 6.

<sup>13</sup> NER, Chapter 10, definition of nominated pass through event considerations.

to incorporate and reflect the essential components of a cost pass through regime in the NER. It was intended that in order for appropriate incentives to be maintained, any nominated pass through event should only be accepted when event avoidance, mitigation, commercial insurance and self-insurance are unavailable.<sup>14</sup>

that a pass through event should only be accepted when it is the least inefficient option and event avoidance, mitigation, commercial insurance and self-insurance are found to be inappropriate. That is, it is included after ascertaining the most efficient allocation of risks between a service provider and end customers.<sup>15</sup>

This protects the incentive regime under the NER by limiting erosion of a service provider's incentives to use market based mechanisms to mitigate the cost impacts that would arise.<sup>16</sup> This promotes the efficient investment in, and efficient operation and use of, network services for the long term interests of consumers with respect to price.<sup>17</sup>

As a matter of good regulatory practice, we also take into account the desirability of consistency in our approach to assessing nominated pass through events across our electricity determinations and gas access arrangements.<sup>18</sup>

## 14.4 Interrelationships

As discussed in our draft decision, the pass through mechanism is not the only way service providers can manage their risks under a distribution or transmission determination. It is interrelated with other parts of this determination, in particular with SA Power Networks' forecast operating and capital expenditure and the rate of return included in our revenue determination. We must specify and take account of these interrelationships.<sup>19</sup> This requires us to balance the incentives in the various parts of our decision.

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<sup>14</sup> AEMC 2012, *Cost pass through arrangements for Network Service Providers, Rule Determination*, 2 August 2012, p. 19.

<sup>15</sup> AEMC 2012, *Cost pass through arrangements for Network Service Providers, Rule Determination*, 2 August 2012, p. 20.

<sup>16</sup> AEMC 2012, *Cost pass through arrangements for Network Service Providers, Rule Determination*, 2 August 2012, p. 8.

<sup>17</sup> AEMC 2012, *Cost pass through arrangements for Network Service Providers, Rule Determination*, 2 August 2012, p. 8.

<sup>18</sup> AEMC 2012, *Cost pass through arrangements for Network Service Providers, Rule Determination*, 2 August 2012, p. 18.

<sup>19</sup> NEL, s. 16(1)(c).

## 14.5 Reasons for final decision

### 14.5.1 Natural disaster

In our draft decision we made some minor amendments to provide greater consistency between SA Power Networks and other network service providers. We removed the term 'negligent' from the description of events that are outside the scope of the definition due to the acts or omissions of the service provider.

In its revised proposal, SA Power Networks' proposed two amendments to the natural disaster event, and associated definition, in the draft decision:

- the addition of the word 'unlawful' before the words '... acts or omissions of the service provider;' in the definition; and
- the removal of declarations by a relevant government authority that a natural disaster event has occurred (called the Declaration Consideration in this Attachment) from the specified list of matters that the AER will consider in assessing a natural disaster pass through event.<sup>20</sup>

The amended definition SA Power Networks proposed is as follows (with italicised text showing proposed additions, and strikethrough text showing proposed deletions):

Natural disaster event means any natural disaster including but not limited to cyclone, fire, flood or earthquake that occurs during the 2020–25 regulatory control period that increases the costs to SA Power Networks in providing direct control services, provided the fire, flood or other event was not a consequence of the *unlawful* acts or omissions of the service provider.

Note: In assessing a natural disaster event pass through application, the AER will have regard to, amongst other things:

- whether SA Power Networks has insurance against the event, and
- the level of insurance that an efficient and prudent NSP would obtain in respect of the event., and
- ~~whether a relevant government authority has made a declaration that a natural disaster has occurred.~~

In its revised proposal SA Power Networks stated that there may be situations where a natural disaster (such as a fire) arises as a consequence of it acting (or not being able to act) in accordance with the regulatory requirements governing its actions and omissions. In turn SA Power Network's compliance with these regulations could prevent it from meeting pass through requirements SA Power Networks submitted that it is both reasonable and necessary that the 'acts or omissions' of SA Power Networks that are excluded from triggering the pass through event be qualified so that such lawful acts (and omissions) do not unfairly disadvantage SA Power Networks. It

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<sup>20</sup> SA Power Networks, 2020–25 Revised Regulatory Proposal, Attachment 13, Pass through events, p. 19.

provided an example, in the context of vegetation clearance, to illustrate that there may be circumstances in which SA Power Networks is prohibited from clearing vegetation, even though contact between that vegetation and the distribution infrastructure could provide a source of ignition for a bushfire start.

While we recognise the specific scenario outlined by SA Power Networks, we do not consider adding the word 'unlawful' is the appropriate solution, as it would broaden the scope of the pass through event considerably. Our decision is to amend the definition in a more targeted way. . The amended drafting is set out below in italicised text.

Natural disaster event means any natural disaster including but not limited to cyclone, fire, flood or earthquake that occurs during the 2020–25 regulatory control period that increases the costs to SA Power Networks in providing direct control services, provided the fire, flood or other event was:

- *a consequence of an act or omission that was necessary for the service provider to comply with a regulatory obligation or requirement or with an applicable regulatory instrument; or*
- *not a consequence of any other act or omission of the service provider.*

We believe this change sufficiently covers the example illustrated by SA Power Networks and similar events.

We accept SA Power Networks' proposal to remove the reference to government declarations. This is consistent with recent decisions, including our Final Decision for TasNetworks Transmission and Distribution Determination 2019–24,<sup>21</sup> and our Final Decision for Evoenergy Distribution Determination 2019–24.<sup>22</sup> Removing this reference will not prevent the AER from having regard to whether a declaration has been made.

#### **14.5.1.1 Late submission relating to COVID-19 pandemic**

SA Power Networks wrote to us on 1 April 2020<sup>23</sup> making further submissions relating to the natural disaster pass through event. It sought additional amendments to the definition of this nominated pass through event to capture increased costs SA Power Networks may incur as a result of pandemics or epidemics. SA Power Networks made this late submission seeking to address concerns arising from the unfolding global COVID-19 pandemic.

In this submission SA Power Networks sought that the definition of the natural disaster event be amended such that it included the additional italicised words '*or other declared emergency including but not limited to cyclone, fire, flood, earthquake, epidemic or pandemic*', and that the words 'that occurs during the 2020–25 regulatory control period' be deleted. It also submitted that, despite its position in the revised

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<sup>21</sup> AER, *Overview | Final decision – TasNetworks transmission and distribution determination 2019–24*, p. 60

<sup>22</sup> AER, *Overview | Final decision – Evoenergy distribution determination 2019–24*, p. 47.

<sup>23</sup> SA Power Networks, *Letter – to AER re natural disaster pass through event*, 1 April 2020.

proposal, the AER should have regard to whether a government authority had made a declaration relating to a natural disaster, and that such declarations should include ‘a declaration of a public health emergency under, or pursuant to, the Public Health Act 2011 (SA)’.

We decided not to accept the amendments proposed to the definition of the natural disaster at this late stage in the process. Our reasons are set out below.

In making our decision we have had regard to the nominated pass through event considerations (see section 14.3). The pandemic amendments proposed by SA Power Networks are not covered by existing pass through events and a prudent service operator could not prevent a pandemic from occurring. However, there is still uncertainty around the cost impact of a pandemic and it is not clear whether those costs could be mitigated by a prudent service operator.

Even if SA Power Networks’ pandemic amendments satisfied the nominated pass-through event considerations (and the information we presently have does not allow us to be so satisfied), we decided not to allow it. We must have regard to the nominated pass-through event considerations. We are also required to determine this issue in a manner that we consider is most likely to contribute to the achievement of the NEO. As noted in section 14.3, in the context of pass through events, this means we give particular consideration to the impact of the proposal on price, quality, reliability and security of supply that may arise from changes in the efficient investment in, operation and use of electricity services in the long term interests of consumers.

We have concerns that the adoption of the proposal may have adverse effects that could impact future prices faced by consumers. For example, the proposed amendments are for increases in costs (e.g. opex or capex), however, there could also be cost savings as a result of a pandemic (e.g. with delayed capex) that would not be captured by the pass through. Accepting a pass-through that is not well specified comes with the risk of unbalanced treatment of the effects of a pandemic.

Further, we have concerns related to the appropriateness of the amendments as a response specifically to the COVID-19 pandemic. For example:

- it is not clear that modifying the natural disaster definition is the appropriate way to address this event given their differences, including that the current COVID-19 pandemic has a broader economic effect.
- it is also not clear that the effects of COVID-19 should all be dealt with in the same way.
- we have concerns related to the effects of amending the definition of ‘natural disaster’ pass through. For example, restricting the pass through to events occurring during the 2020–25 regulatory control period may have other impacts for natural disasters that have already occurred.

We have not been able to adequately explore these issues in the limited time since SA Power Networks proposed the amendment to the definition. Given this, we considered that we could not be satisfied that adoption of the proposal would promote the NEO.

A further reason why we decided not to allow the pass through was our view that we could not adequately consult affected stakeholders, including with consumers who may be impacted in the future. While this decision was delayed, we do not consider this provided sufficient time to examine the issues and consult adequately with stakeholders given the novel, and not insignificant, nature of the proposed amendments and the complex issues raised. As noted in the Overview, we also considered that delaying the determinations further to allow more time for the effects of COVID-19 to be assessed is not the appropriate response when balancing the importance of finalising the arrangements for 1 July 2020.

The COVID-19 pandemic potentially affects all of the network businesses we regulate, and all of their customers. In making our decision about SA Power Network's proposal we considered that consistency in approach across all regulated businesses means that any impacts of the COVID-19 pandemic are likely to be more appropriately considered across the industry as a whole through a rule change.

Going forward, if it becomes clear that that the impacts of COVID-19 are substantial, then a rule change would need to be considered to enable us to re-open existing revenue determinations.

## 14.5.2 Insurance cap

In our draft decision we made minor amendments to the insurance cap pass through event to provide greater consistency between SA Power Networks and other network service providers.

SA Power Networks' revised proposal included a number of new changes to the insurance cap pass through definition that were not part of its initial proposal and were therefore not considered in the draft decision. These can be grouped into three categories:

- changes to reflect SA Power Networks' use of multiple insurance policies
- changes to take into account potential insurance coverage gaps in the future arising from changing insurance liability market conditions
- inclusion of a reference to the outcome of a new annual consultative process about the efficiency and prudence of SA Power Networks' insurance procurement. The consultative process would be a matter we take into account in assessing an insurance cap pass through event application.

Our assessment and decision in relation to these proposed changes is set out below.

SA Power Networks, and other network operators sometimes have more than one policy, particularly for bushfire insurance. We consider it appropriate to amend this pass through event to reflect the use of multiple insurance policies. Our amended wording is slightly more generic (and therefore more flexible) than that proposed by SA Power Networks, in that we have made reference to a 'set of insurance policies' instead of 'program of policies'. We consider this change reflects insurance market conditions are changing following significant bushfire events in Australia and overseas. The changes are making bushfire coverage more expensive and difficult to procure.

Gaps in a network operator's insurance coverage may occur if SA Power Networks is unable to find suitable insurance providers to fill withdrawn capacity or cannot economically justify higher premiums.

We have refined the pass through definition to allow for unfavourable changes to SA Power Networks' insurance policy, but only under what we have defined as 'changed circumstances'. Our definition of 'changed circumstances' is as follows:

'changed circumstances' means movements in the relevant insurance liability market that are beyond the control of SA Power Networks, where those movements mean that it is no longer possible for SA Power Networks to take out an insurance policy or set of insurance policies at all or on reasonable commercial terms that include some or all of the costs referred to in paragraph 2 above within the scope of that insurance policy or set of insurance policies.

Our final decision recognises the possibility of future coverage gaps, negative impact on deductible schedules or reinstatement rights as raised by SA Power Networks, but also seeks to preserve appropriate pass through event incentives under a normal operating environment.

In addition, our final decision also updates the name of the pass through event. This name change - from 'insurance cap event' to 'insurance coverage event' recognises that in the future potential insurance gaps may not only relate to any insurance caps.

In relation to the annual consultative process proposed by SA Power Networks, SA Power Networks has effectively asked the AER to establish a process under which we would review consistency of SA Power Networks' insurance decisions with 'the level and scope of insurance cover that an efficient and prudent DNSP would obtain in respect of the event'.<sup>24</sup>

We have not included this proposed change in our final decision. The NER only allows us to make a decision about whether to amend a service provider's maximum allowed revenue under a revenue determination once the relevant event has occurred.<sup>25</sup> These decisions are highly specific to the facts and circumstances of each individual event, and it is therefore not appropriate for the AER to form any ex-ante or pre-emptive views.

However, we consider it reasonable to provide SA Power Networks and the broader industry with greater clarity and guidance around the matters we are likely to have regard to in assessing any insurance cap pass through event that occurs. We propose to release a consultation paper to begin this process shortly.

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<sup>24</sup> SA Power Networks, 2020–25 Revised Regulatory Proposal, Attachment 13, Pass throughs, p. 15.

<sup>25</sup> NER 6.6.1(d) and 6A.7.3(d).



### 14.5.3 Corporate income tax

SA Power Networks' revised proposal included a new pass through event for changes in corporate income tax. This would include a change in the tax rate itself as well as in the application, or the way, corporate income tax is calculated.

Our decision is to not accept the proposed corporate income tax event, on that basis that the NER specifically excludes changes in (corporate) income tax from the definition of “tax change event”. Allowing changes in income tax to be a pass through event under the more general category of “nominated pass through events” would be inconsistent with this specific exclusion from a prescribed pass through event, and would mean that it has no effect.

Further, pass through events in our regulatory framework serve as a compromise between pure revenue caps and cost plus regulation. The framework is intended to provide incentives for businesses to increase efficiency within a regulatory control period. At the next reset we would review the way we forecast the tax allowance to reflect any changes in corporate income tax treatment.

In relation to the treatment of past immediate expensing, we consider that SA Power Networks' customers should not be potentially exposed to paying higher prices in the future due to SA Power Networks' treatment of immediate expensing in the past. We believe this is consistent with our final decision on immediate expensing<sup>26</sup> in relation to the tax base and the review of the regulatory tax approach.<sup>27</sup>

### 14.5.4 Insurer credit risk, terrorism and major cyber event

SA Power Networks' revised proposal accepted our draft decisions and minor amendments in relation to the insurer credit risk and terrorism nominated pass through events. As a result, we have included these in our final decision with no changes.

SA Power Networks also accepted our draft decision to not accept a major cyber event as a nominated pass through event. As a result, we have not included this in our final decision.

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<sup>26</sup> AER, *Final Decision, SA Power Networks 2020–25, Attachment 7 Corporate income tax*, May 2018.

<sup>27</sup> AER, *Final Report, Review of regulatory tax approach*, December 2018.



## Shortened forms

Shortened form	Extended form
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Distributor	distribution network service provider
NEL	National Electricity Law
NEO	National Electricity Objective
NER	National Electricity Rules
NSP	network service provider
RBA	Reserve Bank of Australia
RPP	revenue and pricing principles

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