AUSTRALIAN ENERGY REGULATOR

Level 17, Casselden
2 Lonsdale Street
Melbourne Vic 3000

28 May 2021

Mr Steve Masters
Chief Executive Officer
ElectraNet

By email: [redacted]

Dear Mr Masters

Re: Contingent project application for Project EnergyConnect

I am writing in response to your letter of 9 April 2021 providing further information supporting ElectraNet's 30 September 2020 contingent project application for Project EnergyConnect.

As you know, the AER's role is to determine the forecast prudent and efficient capital expenditure and operating expenditure required to deliver the project, and the incremental revenues ElectraNet can recover from customers. However, we must only do so when the need and timing of the project is certain.

I am pleased to inform you that the AER has considered ElectraNet's application, and the additional supporting information provided, and has made a determination in accordance with clause 6A.8.2 of the National Electricity Rules (NER).

We are satisfied that ElectraNet's Board has now committed to proceed with the project. Our determination means that ElectraNet is now entitled to begin to recover the prudent and efficient costs of delivering the project in the 2018–23 regulatory control period.

The AER has determined that ElectraNet is allowed to recover $10.2 million in additional revenue from customers in 2022-23, the final year of the current regulatory control period. We estimate that the impact of delivering the project is that the average residential electricity bill in South Australia will increase by $6 in 2022-23. This will increase to $17 per year over the next five year regulatory period.

This increase in allowed revenues reflects our determination on the prudent and efficient costs of delivering the project. ElectraNet's application proposed $468.6 million in capital expenditure to deliver the project. Our determination is that $457.4 million is a reasonable estimate of the total costs required to deliver the project efficiently.

We have also made a determination on TransGrid's forecast expenditure and incremental revenue reasonably required to deliver the New South Wales component of the project.

We acknowledge that this decision is a significant milestone for ElectraNet, TransGrid and Project EnergyConnect and recognise ElectraNet's continued engagement with us throughout the process, which has allowed us to make a fully informed decision. The attachment to this letter provides a summary of our decision, and we intend to publish the full determination and post-tax revenue model on our website shortly. This letter will be published on our website on 31 May 2021.

Please contact me should you have any questions.

Yours sincerely

[redacted]

Clare Savage
Chair
Australian Energy Regulator

Cc: Mr Paul Italiano - TransGrid

Attachment — Summary of AER determination on Project EnergyConnect

Requirements for the AER to make a determination

The AER may only determine the forecast expenditure and incremental revenue required to deliver this project if the following three conditions are met:

- The successful completion of the *South Australian Energy Transformation* Regulatory Investment Test for Transmission (RIT-T) that identifies Project EnergyConnect as the preferred investment option that delivers positive net economic benefits.
- Determination by the AER that the proposed investment satisfies the requirements of the Regulatory Investment Test for Transmission.
- ElectraNet Board commitment to proceed with the project subject to the AER amending the revenue determination pursuant to the NER.

We are satisfied that all three conditions have been met and as such ElectraNet is entitled to recover revenues from consumers to deliver the project.

The process undertaken by ElectraNet, described below, has satisfied the first condition to trigger the contingent project.

In February 2019, ElectraNet completed the *South Australia Energy Transformation* RIT-T demonstrating that a new SA-NSW interconnector was the preferred option that maximised net economic benefits.

On 24 January 2020, we determined that this preferred option identified by ElectraNet satisfies the requirements of the regulatory investment test for transmission, as set out in the NER, satisfying the second condition to trigger the contingent project.

Under the NER, ElectraNet is required to re-apply the regulatory investment test process if, in its reasonable opinion, the project is no longer the preferred option that maximises the net economic benefits.

In September 2020, ElectraNet published an updated cost benefit analysis that accounted for updated project cost estimates as well as inputs and assumptions from the Australian Energy Market Operator’s 2020 Integrated System Plan. This updated analysis indicated that the net benefits of the project are likely to be positive and that the project remains the preferred option. Therefore, ElectraNet concluded that there is no need to reapply the regulatory investment test for this project.

On 28 September, we advised ElectraNet that its updated cost benefit analysis provided a not unreasonable basis for its opinion that the project remains the preferred option.

On 31 March 2021, ElectraNet published a review of whether recent market developments could result in a material change of circumstances that may lead to the project no longer being the preferred option. ElectraNet's assessment concluded that the announcements were likely to have an overall positive impact on the modelled net benefits of the project. This was supported by further analysis undertaken by AEMO.

On 30 March 2021, the ElectraNet Board made a resolution committing to the project, satisfying the third and final condition to trigger the contingent project.

Project commencement and completion dates

We are required to determine the likely project commencement and completion dates. Based on the information provided by ElectraNet, we are satisfied that the project has commenced and the South Australian component is likely to be completed by March 2023. This is within the current 2018-23 regulatory control period.

Forecast expenditure

Table 1 sets out our determination on the forecast capex and opex reasonably required by ElectraNet to deliver the project. These forecasts are reflected in the maximum revenue ElectraNet is allowed to recover from customers for the current regulatory control period.

Table 1 Forecast capital and operating expenditure (million, $2017-18)

	2018-19	2019-20	2020-21	2021-22	2022-23	Total
Forecast capex	5.0	4.1	30.2	171.4	246.7	457.4
Forecast opex	0.0	0.0	0.0	0.1	0.3	0.5

Source: AER analysis

Our assessment found that the majority of ElectraNet's forecast capex for the project reasonably reflects the costs required to deliver the project efficiently. However, our determination differs from ElectraNet in relation to the quantification of project risks and the opportunities available to further reduce project costs as it finalises its design process.

This final decision reflects the assessment we have undertaken since 30 September 2020, informed by submissions from stakeholders and ElectraNet's engagement with us over the process. This has included responding to our information requests and providing further information in response to the preliminary assessment we published in December 2020. This process has ensured we have been able to make a fully informed decision.

Forecast maximum allowable revenues and customer bill impact

Table sets out our determination of the amount of incremental revenue ElectraNet is allowed to recover from customers over the current regulatory control period to undertake the project. These revenues reflect our standard annual building block revenue approach, in accordance with clause 6A.8.2(h) of the NER, consistent with ElectraNet's application.

The amount of incremental revenue required by ElectraNet in 2022-23 as a result of undertaking the project is $10.2 million, an increase in annual allowed revenue of 2.9 per cent. As a result of recovering these revenues, we estimate that the transmission component of the average residential electricity bill in South Australia will increase by $6 in 2022-23. This will increase to $17 per year for the 2023-28 regulatory control period.[1]

Table 2 Annual allowed revenues ($m, nominal)

	2018-19	2019-20	2020-21	2021-22	2022-23	Total
Annual building block revenue requirement (unsmoothed)	0.0	0.2	0.4	1.5	7.8	10.0
Annual expected maximum allowable revenue (smoothed)	0.0	0.0	0.0	0.0	10.2	10.2
Increase to annual expected revenue (%)	0.0%	0.0%	0.0%	0.0%	2.9%	0.6%

Source: AER analysis

[1] For the New South Wales component of the project, we estimate the incremental revenue required by TransGrid in 2022-23 as a result of undertaking the project is $61.5 million, resulting in the transmission component of the average residential electricity bill in NSW increasing by $11. This would increase to $22 per year for the 2023-28 regulatory control period.