Combined Proposal 2024-2029

Attachment 2
Annual revenue requirement

Outline: This attachment to TasNetworks' Combined Proposal sets out how the annual revenue requirement provisions of the National Electricity Rules will apply during the 2024-2029 regulatory control period.

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Note

This attachment forms part of TasNetworks' Combined Proposal for the 2024-2029 regulatory control period and should be read in conjunction with the other parts of the proposal. TasNetworks' Combined Proposal is made up of the documents and attachments listed below, as well as the supporting documents that are listed in Attachment 23.

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	Combined Proposal overview
Attachment 1	Customer and stakeholder engagement summary
Attachment 2	**Annual revenue requirement**
Attachment 3	Regulatory asset base
Attachment 4	Rate of return
Attachment 5	Regulatory depreciation
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2 Annual revenue requirement

2.1 Overview

The forecast total revenue requirement for our transmission network for the 2024-2029 regulatory control period is $784.1 million ($2023-24). This is around 4.8 per cent lower than our total revenue requirement for the 2019-2024 regulatory control period. This total revenue reduction results in a forecast decrease in the average transmission price in the first year of the next regulatory control period of 1.0 per cent.

The forecast total revenue requirement for our distribution network for the 2024-2029 regulatory control period is $1,549.2 million ($2023-24). This is around 8.3 per cent higher than our total revenue requirement for the 2019-2024 regulatory control period resulting in an increase in the indicative distribution network charge in the first year of the next regulatory control period of around 5.9 per cent.[1]

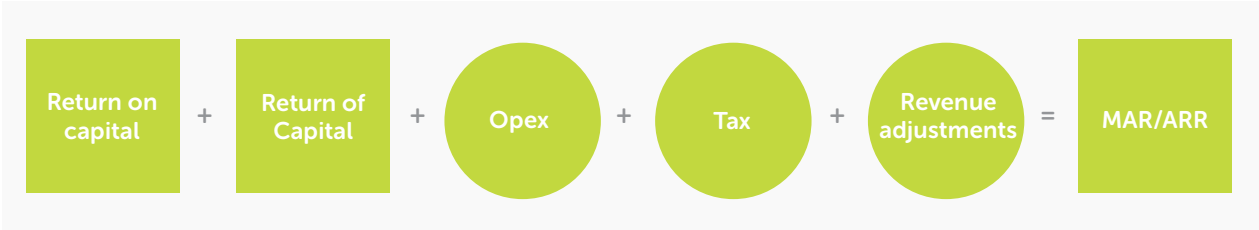
In accordance with the feedback we have received from our customers and stakeholders, we have taken a disciplined approach to our capital and operating expenditure by constraining the total revenue required to maintain safe, reliable and affordable network services.

2.2 Rule requirements

Our total revenue requirements for our transmission and distribution networks are based on the Australian Energy Regulator's (**AER's**) post-tax building block approach and comply with clauses 6.4.3 and 6A.5.4 of the National Electricity Rules (**NER**), the Post Tax Revenue Model (**PTRM**) and the Roll Forward Model (**RFM**). The revenue building block components are shown in Figure 1.

1 for a typical Residential customer

Figure 1. Revenue Building Blocks



TasNetworks' forecast total revenue requirement comprises unsmoothed annual revenue requirement (**ARR**) or maximum allowed revenue (**MAR**) for each year of the 2024-2029 regulatory control period, which are calculated as the sum of the above building block components for each of our networks. Clause 6A.6.8 of the NER requires that these unsmoothed revenue requirements must be smoothed with an X-factor, such that the smoothed ARR / MAR is equal to the net present value (**NPV**) of the annual unsmoothed ARR / MAR, while ensuring that the smoothed and unsmoothed ARR / MAR for the last regulatory year are as close as reasonably possible.

In addition to the above building blocks, clause 6A.7.2 of the NER requires that any changes in transmission network support costs that occur during a regulatory control period be subject to a pass-through application. The application will seek to vary the MAR for each year based on the difference between forecast and actual network support expenditure.

Furthermore, clauses 6A.7.3 and 6.6.1 of the NER allow the pass through of other approved transmission and distribution costs (refer to Attachment 17 Pass through events).

Finally, clause 6A.8 (transmission) and 6.6A (distribution) of the NER allows the AER to amend TasNetworks revenue allowance for costs associated with contingent projects that are triggered during a regulatory control period (refer to Attachment 7 Contingent projects).

2.3 Forecast revenue

Figure 2 shows a $39.4 million reduction in real terms and a flatter annual profile between TasNetworks' total annual revenue forecasts for our transmission network for the 2024-2029 regulatory control period compared to the 2019-2024 regulatory control period.

Figure 2. Forecast Transmission Revenue ($ million, 2023-24)

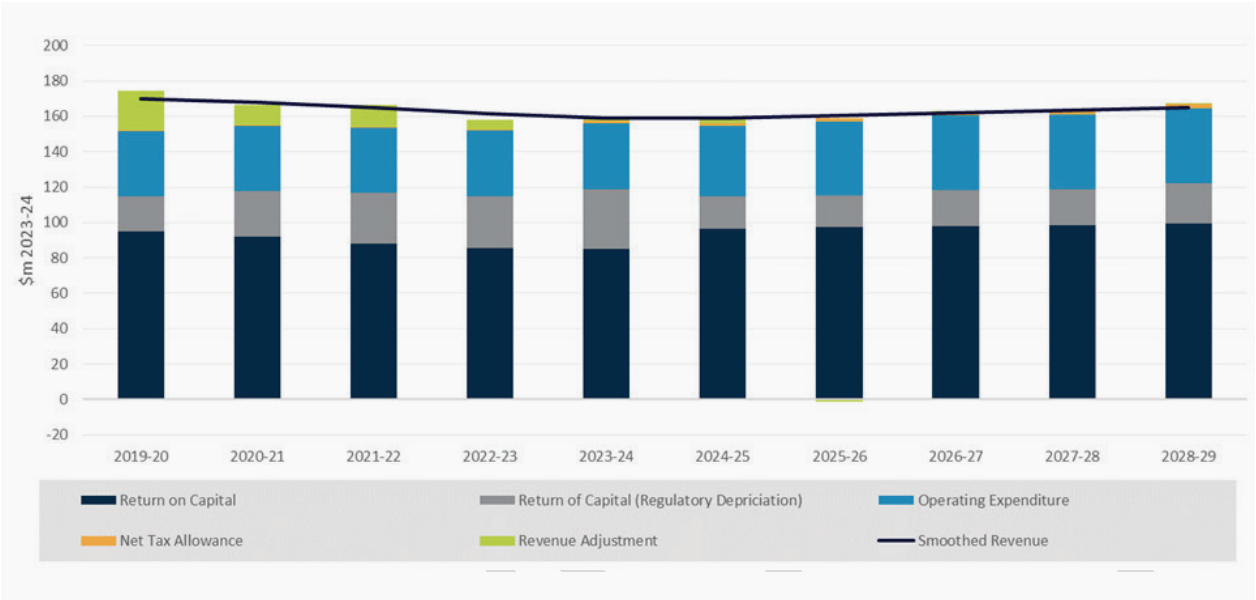
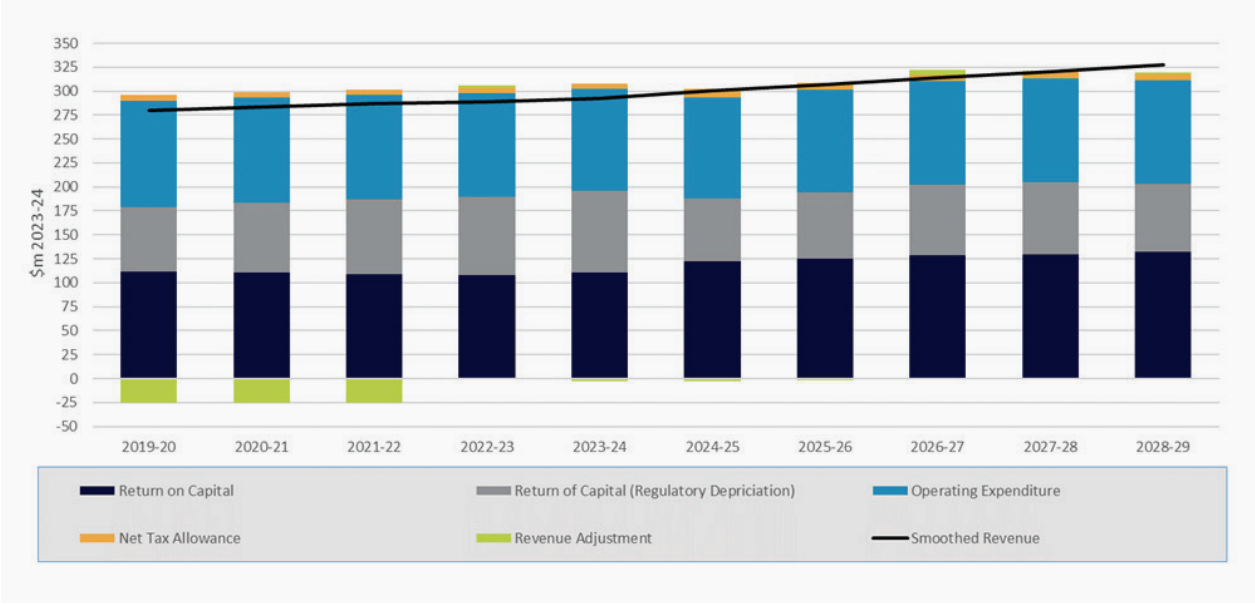


Figure 3 shows a $154.2 million increase in real terms between TasNetworks' total annual revenue forecasts for our distribution network for the 2024-29 regulatory control period compared to the 2019-2024 regulatory control period.

Figure 3. Forecast Distribution Revenue ($ million, 2023-24)



We summarise the various building block components in the following sections of this attachment. Further explanation and substantiation of these components is provided in subsequent attachments of this Combined Proposal.

2.3.1. Regulatory asset base

The value of our regulatory asset base (**RAB**) for each of our transmission and distribution networks determines our return on and return of capital allowances.

Our estimated opening RAB on 1 July 2024 for our transmission network is $1,758.7 million (nominal). Our estimated opening RAB on 1 July 2024 for our distribution network is $2,223.0 million (nominal). Our approach to calculating these opening RAB values is explained in Attachment 3 Regulatory asset base.

We have forecast a roll-forward of our RAB for each year of the 2024-2029 regulatory control period based on our forecasts for inflation (refer Attachment 4 Rate of return), regulatory depreciation (refer Attachment 5 Regulatory depreciation) and capital expenditure (refer Attachment 6 Captial expenditure). The RAB roll forward for each network is shown in Tables 1 and 2.

Table 1. Transmission Forecast RAB roll forward 2024-2029 regulatory control period ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29
Opening RAB	1,758.7	1,799.0	1,858.8	1,908.8	1,958.8
Capital expenditure, as incurred	54.4	73.3	65.6	66.6	61.6
Regulatory deprecation	(14.2)	(13.5)	(15.6)	(16.6)	(18.7)
Closing RAB	1,799.0	1,858.8	1,908.8	1,958.8	2,001.7

Table 2. Distribution Forecast RAB roll forward 2024-2029 regulatory control period ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29
Opening RAB	2,223.0	2,323.7	2,429.7	2,512.5	2,591.1
Capital expenditure, as incurred	162.6	173.6	158.5	158.1	160.5
Regulatory deprecation	(61.9)	(67.6)	(75.7)	(79.5)	(77.6)
Closing RAB	2,323.7	2,429.7	2,512.5	2,591.1	2,674.0

2.3.2 Return on capital

The return on capital is calculated by applying our rate of return (also referred to as the Weighted Average Cost of Capital or **WACC**) to the opening RAB in each year of the regulatory control period. Attachment 4 Rate of return further explains the calculation of our rate of return forecast.

Our return on capital forecast for each network is presented in Tables 3 and 4.

Table 3. Transmission Return on capital ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Opening RAB	1,758.7	1,799.0	1,858.8	1,908.8	1,958.8	
Rate of return	5.68%	5.80%	5.85%	5.93%	6.03%	
Return on capital	99.8	104.4	108.8	113.1	118.1	544.2

Table 4. Distribution Return on capital ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Opening RAB	2,223.0	2,323.7	2,429.7	2,512.5	2,591.1	
Rate of return	5.71%	5.78%	5.85%	5.93%	6.03%	
Return on capital	126.9	134.3	142.2	148.9	156.3	708.5

2.3.3 Regulatory depreciation

Regulatory depreciation (also referred to as the return of capital) is calculated by deducting the inflation adjustment made to the RAB from forecast depreciation. Attachment 5 Regulatory depreciation further explains the calculation of our regulatory depreciation forecast.

Our regulatory depreciation forecast for each network is presented in Tables 5 and 6.

Table 5. Transmission Return of capital ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Straight-line depreciation	73.0	73.7	77.8	80.5	84.3	389.4
Indexation on opening RAB	(58.9)	(60.2)	(62.2)	(63.9)	(65.6)	(310.9)
Return of capital	14.2	13.5	15.6	16.6	18.7	78.5

Table 6. Distribution Return of capital ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Straight-line depreciation	136.3	145.4	157.1	163.6	164.3	766.8
Indexation on opening RAB	(74.4)	(77.8)	(81.4)	(84.1)	(86.6)	(404.5)
Return of capital	61.9	67.6	75.7	79.5	77.6	362.3

2.3.4 Operating expenditure

Our operating expenditure forecast for each of our transmission and distribution networks is shown in Tables 7 and 8. Attachment 8 Operating expenditure further explains the calculation of our operating expenditure forecast.

Table 7. Transmission Operating expenditure ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Controllable operating expenditure	40.2	43.5	46.0	47.7	49.3	226.8
Debt raising costs	0.9	0.9	0.9	1.0	1.0	4.7
Total operating expenditure	41.1	44.4	46.9	48.7	50.3	231.4

Table 8. Distribution Operating expenditure ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Controllable operating expenditure	97.5	102.7	107.4	111.5	115.7	534.7
GSL	4.1	4.2	4.4	4.5	4.7	21.9
Electrical Safety Inspection Levy payments	5.3	5.4	5.6	5.8	6.0	28.1
NEM Levy payments	1.5	1.6	1.5	1.3	1.4	7.3
Debt raising costs	1.1	1.2	1.2	1.3	1.3	6.1
Total operating expenditure	109.5	115.1	120.1	124.4	129.0	598.2

2.3.5 Tax

We forecast the taxation building block for each of our transmission and distribution networks, by applying a statutory tax rate of 30% and value for imputation credits of 0.585 consistent with the AER's 2018 Rate of Return Instrument.2 This is presented in Tables 9 and 10.

Table 9. Transmission Corporate tax ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Corporate tax	2.5	4.1	3.6	4.2	6.1	20.6
Value of imputation credits	(1.5)	(2.4)	(2.1)	(2.5)	(3.6)	(12.0)
Taxation	1.0	1.7	1.5	1.7	2.5	8.5

Table 10. Distribution Corporate tax ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Corporate tax	20.7	16.4	15.1	16.8	16.3	85.3
Value of imputation credits	(12.1)	(9.6)	(8.8)	(9.8)	(9.5)	(49.9)
Taxation	8.6	6.8	6.2	7.0	6.8	35.4

2.3.6 Expenditure incentive schemes

Any capital and operating efficiency gains or losses arising from the Efficiency Benefit Sharing Scheme (**EBSS**) and Capital Expenditure Sharing Scheme (**CESS**) in the 2019-2024 regulatory control period are carried over as an adjustment to the ARR / MAR in the 2024-2029 regulatory control period.

Our EBSS and CESS carryover amounts for each network (refer Attachment 10 Efficiency benefit sharing scheme and Attachment 11 Capital expenditure sharing scheme) from the 2019-2024 regulatory control period are summarised in Tables 11 and 12.

2 AER, Rate of return instrument, Dec 2018

Table 11. Transmission EBSS and CESS carryover amounts ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
EBSS carryover	2.6	(2.2)	(0.2)	0.0	0.0	0.2
CESS carryover	0.7	0.7	0.7	0.7	0.7	3.5
Revenue Adjustments	3.2	(1.5)	0.5	0.7	0.7	3.7

Table 12. Distribution EBSS and CESS carryover amounts ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
EBSS carryover	(3.6)	(3.4)	4.2	0.0	0.0	(2.8)
CESS carryover	2.2	2.2	2.3	2.4	2.5	11.6
Revenue Adjustments	(1.5)	(1.2)	6.5	2.4	2.5	8.8

2.3.7 Shared asset decrements

Electricity network businesses may use assets to provide both regulated electricity services and other (unregulated) services. These assets are called 'shared assets'.

An example of a shared asset is a power pole, paid for by electricity consumers, which also supports a fibre optic cable for communications services. While the AER regulates electricity supply it does not regulate communications services. So, the power pole is a shared asset.

To manage this the AER has published a Shared Asset Guideline[3] which sets out its approach to sharing the benefits of the unregulated transaction with consumers of regulated services.

Importantly, when unregulated revenues from shared assets are more than one per cent of a Network Service Provider's total annual revenue the AER will reduce regulated revenues by around 10 percent of the value of unregulated revenues earned from the shared assets.

TasNetworks has forecast revenue from these shared assets for the 2024-2029 regulatory control period and only the distribution network has shared assets that meet the one per cent revenue threshold. Therefore, a shared asset decrement has been determined for the distribution revenue as shown in Table 13.

Table 13. Distribution Shared Asset Decrement ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Shared Asset Decrement	(0.4)	(0.4)	(0.5)	(0.5)	(0.5)	(2.3)

2.3.8 X-factors and smoothed total revenue

X-factors are utilised in the PTRM as a method for ensuring that year on year differences in revenue are smoothed out for customers. The calculation of X-factors takes into account the NPV of the revenue stream and ensures that customers and networks are no better or worse off from any movements in the timing of revenue. X-factors are updated on a yearly basis to account for the annual update to the rolling cost of debt as part of the rate of return calculation. The AER will release an updated PTRM every year to account for this movement.

We have applied an X-factor to our unsmoothed ARR / MAR to reduce significant variations and/or smooth revenue in each year of the 2024-2029 regulatory control period. The smoothed annual revenue profile is used to set our transmission and distribution prices each year.

Our X-factors and smoothed ARR / MAR for the 2024-2029 regulatory control period are summarised in Tables 14 and 15.

Table 14. Transmission X-factors and smoothed MAR ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Unsmoothed revenue requirement	159.6	162.6	173.5	181.1	190.6	867.5
X-factors	1.63%	(0.78%)	(0.78%)	(0.78%)	(0.78%)	
Smoothed MAR	159.6	166.2	173.1	180.3	187.8	866.9

3 AER, Better Regulation Shared Asset Guideline, Nov 2013

Table 15. Distribution X-factors and smoothed ARR ($ million, nominal)

	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Unsmoothed revenue requirement	305.5	322.7	350.9	362.3	372.2	1,713.5
X-factors	(2.43%)	(2.36%)	(2.36%)	(2.36%)	(2.36%)	
Smoothed ARR	305.5	323.1	341.8	361.6	382.5	1,714.5

2.3.9 Possible additional revenue adjustments

During the 2024-2029 regulatory control period, our ARR / MAR will be updated each year to reflect:

- actual inflation
- changes to the annual return on debt
- any changes in network support costs subject to a pass-through application
- any cost pass-through events approved by the AER
- financial penalties or bonuses being subtracted from or added to our smoothed ARR / MAR due to our transmission and/or distribution network service performance in a year varying from the AER's approved targets (refer Attachment 12 Service target performance incentive scheme).

Our MAR for the transmission network may also change if any of our proposed contingent projects are triggered during the 2024-2029 regulatory control period and approved by the AER following an application from TasNetworks. No contingent projects have been identified for our distribution network in the 2024-2029 regulatory control period. (Refer to Attachment 7 Contingent projects).

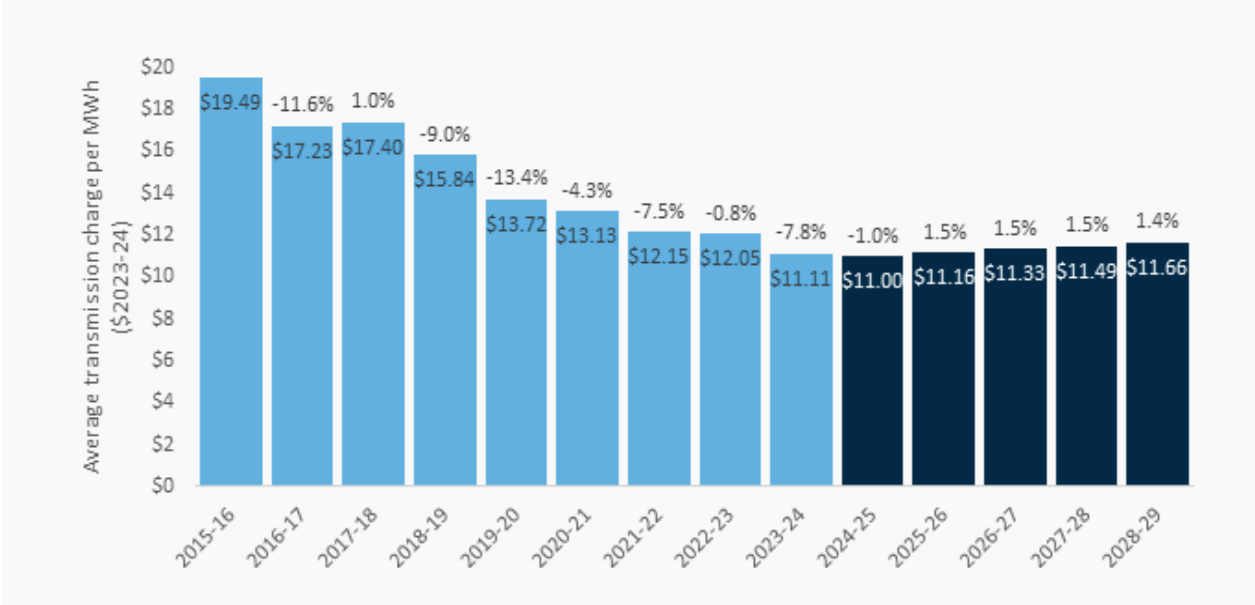
2.4 Indicative price impacts

TasNetworks calculates annual prescribed transmission prices consistent with our approved Pricing Methodology, which must comply with the requirements of the NER and the AER's Pricing Methodology Guidelines for transmission networks.

TasNetworks determines its transmission charges based on the approved smoothed MAR and the pricing principles in Clause 6A.23 of the NER. The average price path is illustrative and estimated using the AER's PTRM, whereby we divide our forecast annual smoothed MAR by forecast energy delivered in Tasmania in each year of the 2024-2029 regulatory control period. This is shown in Figure 4.

It is important to note that price movements for individual customers will vary depending on usage, location and the annual adjustments described above. As such, Figure 4 indicates the implications of our proposal for average transmission prices over the 2024-2029 regulatory control period.

Figure 4. Average charges for all transmission customers, average $/MWh ($real 2023-24)



The distribution revenue allowance for each year, together with approximately 55 per cent of transmission network charges, is recovered from our distribution customers. This revenue recovery is achieved through a framework of distribution network pricing "tariffs" which are applied to each customer and charged to electricity retailers.

Our proposed transmission and distribution smoothed ARR / MAR result in the indicative average annual network charges for residential and small business customers shown in Figures 5 and 6 respectively. Our proposal results in most customers' network charge movements being broadly aligned with forecast inflation. This is consistent with our key objective to balance ongoing affordability of our network services with the need to invest in services that meet Tasmanian electricity customers' long-term interests.

Figure 5. Indicative distribution network charges, residential customer ($real 2023-24)

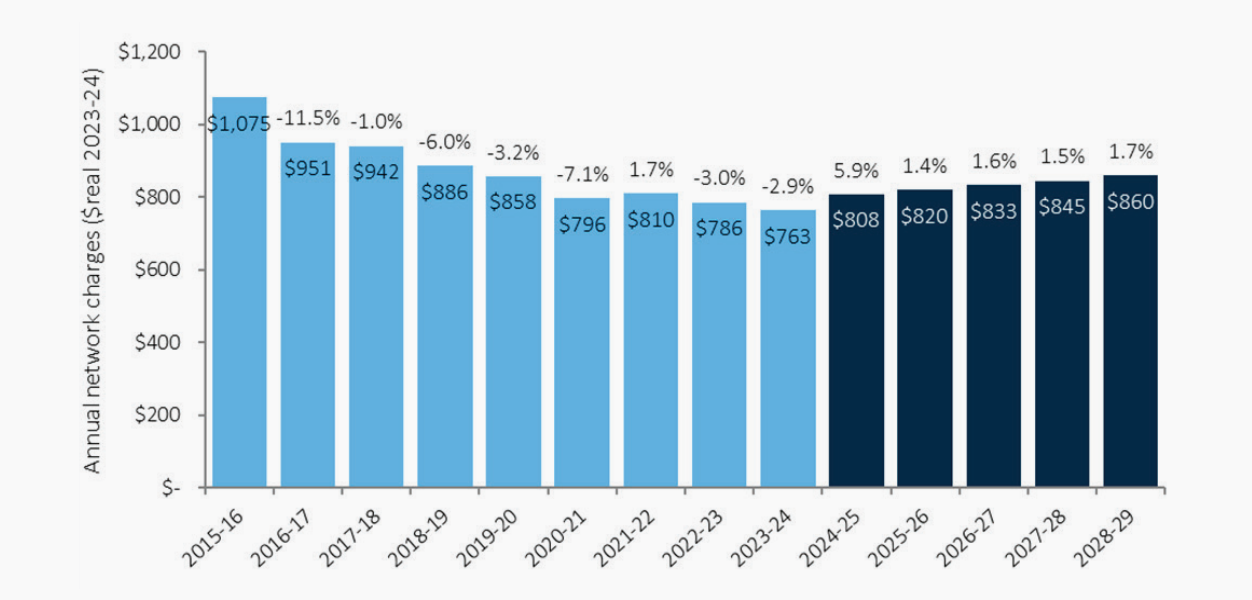
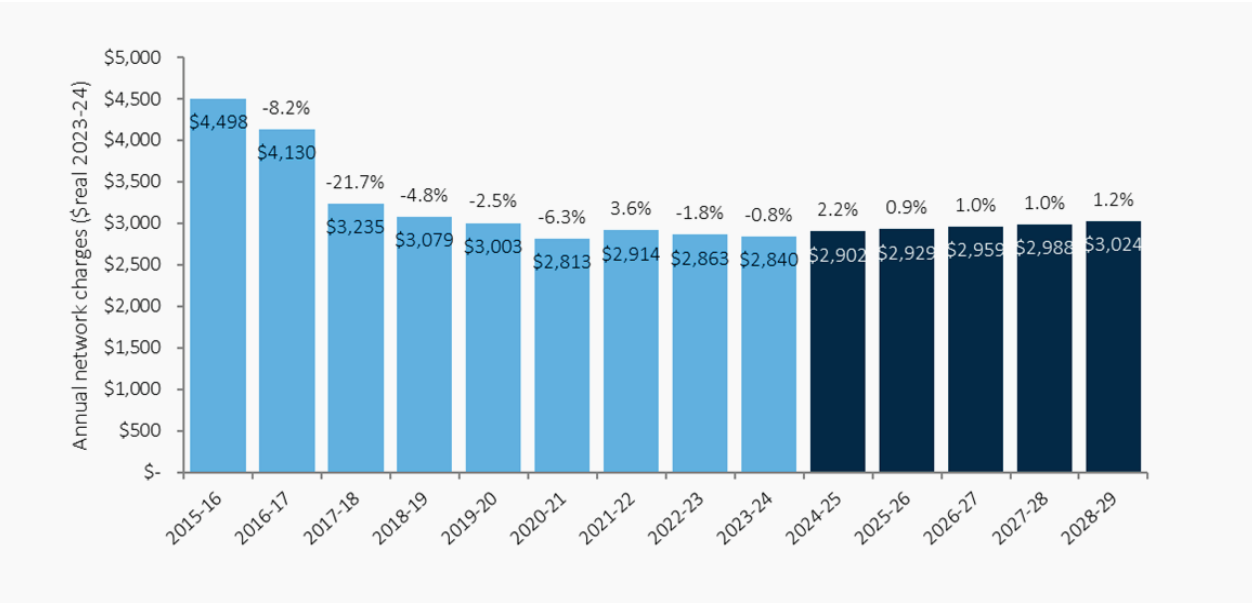


Figure 6. Indicative distribution network charges, small business customer ($real 2023-24)



Transmission and distribution network costs presently make up around 38 per cent of the average Tasmanian residential and small business customer electricity retail bill.

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