SUBMISSION

AUSNET DRAFT PLAN | APRIL 2019

EUAA
Energy Users Association of Australia

INTRODUCTION

The Energy Users Association of Australia (EUAA) is the peak body representing Australian energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing and materials processing industries. Combined they employ over 1 million Australians, pay billions in energy bills every year and are desperate to see all parts of the energy supply chain making their contribution to the National Electricity Objective. Our members are highly exposed to movements in both gas and electricity prices and have been under increasing stress due to escalating energy costs.

These increased costs are either absorbed by the business, making it more difficult to maintain existing levels of employment or passed through to consumers in the form of increases in the prices paid for many everyday items. Many of our members have operations in AusNet's service area.

The AusNet Electricity Distribution Regulatory Proposal is the first network reset to trial the "New Reg" approach to network revenue determination being developed jointly by the AER/ENA/ECA. AusNet is to be congratulated for taking on this initiative. It involves an immense amount of work, commitment and resources by all parties involved. The EUAA welcomes the opportunity many networks are now taking to put emphasis on early engagement and the publication of a Draft Plan. This enables more fruitful discussions to be had prior to the submission of the Initial Regulatory Proposal.

Further we would congratulate AusNet on their willingness to expose their consumer engagement to the scrutiny of the Customer Forum (CF). We are very encouraged by AusNet's timely and substantive responses to the CF's findings as it implements many improvements ahead of the start of the next regulatory period in 2021.
The EUAA has actively participated in this process both as a participant in the AusNet and Consumer Forum engagement process and as part of the AER/ENA/ECA Reference Group on New Reg. This submission draws on that experience.

This submission covers both:

- Comments on the role of the Customer Forum in its Interim Engagement Report of 6th February 2019 and
- The AusNet Draft Plan issued on 12th February 2019

In doing so we also refer to the AER Staff Guidance Note 9 New Reg: Towards Consumer-Centric Energy Network Regulation (AER Note) published on 1st April 2019.[1]

On the Consumer Forum Interim Engagement Report our main conclusions are:

- Reflecting the Customer Forum's strong skills, it has undertaken an excellent consumer engagement process that provides rich data and findings on AusNet's level of consumer engagement and where improvements might be made; it has provided a model for AusNet to work with in the future
- The actual scope of the negotiations is probably less than 5% of the total proposed revenue of $3.6b in 2021-26
- We doubt the effectiveness of the Customer Forum to negotiate with AusNet on the substantive issues within scope of forecast opex and capex expenditure; this is due to a combination of a lack of expertise and the level of detailed information that AusNet can provide at this early stage of their proposal development.

[1] https://www.aer.gov.au/system/files/AER%20Ausnet%20Services%20trial%20-%20Guidance%20note%209%20-%20draft%20proposal%20and%20interim%20engagement%20report%20-%20March%202019.pdf

On the substantive parts of the Draft Plan, our main conclusions are:

- The proposed reductions in opex and capex for the 2020-25 period are relatively small with the customer price reduction driven more (57%) by changes in the WACC parameters following from the new binding WACC Guideline published last December than by actions actually taken by AusNet;
- The price impact of these external actions will only increase when AusNet also includes the impact of lower bond rates and the impact of recent AER decisions on opex productivity (0.5% reduction) and the calculation of the tax allowance
- WACC is now at the low point of the cycle; any change to increasing interest rates will leave consumers very exposed to significant price increases unless AusNet makes further reductions in opex and capex
- We look forward to further detailed engagement with AusNet to get confidence that all possible improvements in efficiency and productivity are being included in their Initial Regulatory Proposal
- It is difficult to answer the specific questions on expenditure given the early stage we are at in the reset cycle – but we would be surprised if there were not considerable further scope for expenditure reductions and hence price falls, excluding the impact of external factors outside of AusNet's control (interest rates, opex productivity and tax allowances)
- We look forward to the AER's analysis in its Draft Determination to inform further specific comments on proposed expenditure
- We support the customer experience actions, particularly the appointment of the Retailer & Large Customer Liaison role

Finally, we look forward to AusNet detailing the form of consumer engagement following submission in the Initial Regulatory Proposal and the completion of the Consumer Forum's work in July 2019.

Andrew Richards
Chief Executive Officer

18 April 2019

CUSTOMER FORUM INTERIM ENGAGEMENT REPORT

This is a very comprehensive and well written report. This submission will comment on its findings from its extensive consumer engagement activities and then the subsequent negotiations it has undertaken with AusNet.

Consumer engagement findings

The report clearly sets out the extensive consumer engagement undertaken by the Forum and well highlights the concerns that consumers have with AusNet's performance. The report notes:

> "…the Customer Forum recognised AusNet Services' greatest strength was its electrical engineering expertise…However in contrast to its engineering and regulatory management expertise, (we) considered AusNet Services awareness of, and experience dealing with customers was less well developed… (we) found a broad and deep disassociation between AusNet Services and some of its customers. For some customers the relationship is strained… AusNet has under-resourced its customer relationship function, resulting in a largely reactive approach to addressing customer problems." (p.11)

Then for larger customers:

> "AusNet Services lacks a pro-active service presence among its customers. This makes the business slow to recognise their issues and hampers prompt responses. Large business customers told the Customer Forum that they expect dedicated AusNet Services support staff." (p.11)

which accords with some of our members' experiences. So, AusNet is to be congratulated for the transparent approach it has taken to the findings and its commitment, as noted by the Forum:

> "…to initiate a series of reforms that will start delivering benefits to customers well ahead of 2021" (p.2)

In the case of larger consumers, we are very supportive of the recent AusNet decision to appoint an very experienced person to the role of Retailer & Large Customer Liaison.

Given the context of these finding on customer service, we note with interest the Forum's conclusion questioning whether the NEO will:

> "…automatically ensure a satisfactory level of customer service"

because while AusNet satisfies minimum regulatory performance targets, there is still considerable concerns about its level of customer service.

Our experience across network revenue resets shows a variety of approaches to consumer engagement and service – both during a reset consultation process and in the business as usual context. The best networks see engagement as an ongoing process in which a revenue reset is an important part. They demonstrate a transparency around communicating a network's issues in a way that allows consumer representatives to understand the inevitably complex trade-offs in service, reliability and cost. They see that noble gestures at a reset process need to be continued in first class service in the field. We think that this is achievable within the existing NEO without amending the NEO.

The Forum made some interesting observations on AusNet's customer research programme – "primarily outsourced", "not clear… how AusNet Services has applied the knowledge gained", "research program appeared to be limited to ad-hoc projects to address specific issues" and "…much of (their) research focusses on residential customers" (p.13).

We are pleased to see the results of the Forum's requested Business Customer Survey completed in August 2018.[2] While most of the respondents were smaller to medium sized businesses, their concerns over affordability accord with EUAA members. As the Forum notes:

> "With some notable exceptions, customers are generally satisfied with the current level of reliability. This was apparent from the Newgate Focus Group Research and the Customer Forum's consultations with customers. This evidence indicates customers generally accept outages (both planned and unplanned) will occur periodically. However, they are:
>
> > "more tolerant if they are provided with accurate, up-to-date information about the likely duration, and if they can see efforts to reduce blackouts." (Newgate Research, *Perceptions of AusNet Services*, page 20)." (p. 31)

Overall, we consider that the Forum has made significant advances in AusNet having a much better understanding on consumer needs and being able to better respond with appropriately targeted initiatives.

Negotiation Process

(i) What is in scope?

The Forum notes:

> "In accordance with our prescribed role, the Customer Forum had limited influence in shaping the overall price of energy to customers. That is, 36% of the average residential customer bill is associated with AusNet Services distribution and metering.
>
> The framework limited the Customer Forum's influence to less than half of the 36% of the average residential customer bill." (p.8)

This implies that the Forum has influence over ~50% of the AusNet revenue for 2021-26 or $1.8b out of $3.6b. The table comments on revenue covered by what we think the Forum might actually have some influence over in its negotiations with AusNet – probably under 5% of total revenue.

Category in-scope	Costs ($2020) under negotiation	Costs where the Forum might have an influence
Operating expenditure	• Step changes totalling ~$50 net (given offsetting benefits from shared data and communications infrastructure) • Review of opex productivity • Total Draft Plan opex of $1,229m	• Some of the step changes – say $15-20m/yr
Capex: • Major augmentation projects • Major replacement projects	• $12.8m over two projects • 10 substation refurbishments totally $112m (though focus seems to be on 6 at a value of $95m) out of total repex of $600m • Total Draft Plan capex of $1,451	• ~$120m in capex – say $10m/yr from WACC and depreciation
Innovation (separate from DMIS)	• $11.4m	• $11.4m

[2] See Week 6

DER integration	• No complete proposal presented to the Forum for consideration	• ?
Metering	• Decrease in metering costs; discussion on timing of $10m to transition to Telstra 4G	• $10m
Total		Say $150m – or ~4% of total revenue

(ii) Base year opex

While opex is in-scope, the Forum's comments on the Base Year (the vast majority of opex) that:

> "AusNet Services proposed 2018 as a base year for the 2021-2025 period. The Customer Forum accepted this proposal, subject to the AER confirming 2018 is an efficient year using its benchmarking methodologies." (p.19)

do not indicate any "negotiation" has taken place and for the AER to conclude that this is a "Draft agreed outcome"[3] is not really anything of significance.

The Forum's approach is consistent with that used in other network reset engagements outside the New Reg framework. The selection of the Base Year is a highly technical matter. Consumer advocates have taken two complementary approaches to this:

- Seeking an understanding of the network's arguments around productivity that they will/have used to justify their proposed base year was "not materially inefficient" given the AER's 0.75 benchmark – this is particularly the case for networks, like AusNet, that are below that benchmark in the latest AER benchmarking data, and
- Question the AER on its 0.75 benchmark that was originally set for the NSW DNSPs for the 2015-20 reset period and which, unfortunately, was not part of the recent opex productivity review

Then left the very complex issue to the AER to undertake its benchmarking process.

(iii) Step changes

The Forum's Report notes for the various step changes:

(a) Accounting treatment of leases ($31m opex reduction as moved to capex)

There was no comment. The AER made no comment in their Guidance note.

(b) REFCL ($8.5m)

"The Customer Forum accepted AusNet Services REFCL bushfire mitigation expenditure proposal, subject to the AER being satisfied this level of expenditure was required for the mandated works and was not already embedded in base year expenditure. (p.20)

(c) Five-minute metering ($2.6m):

"The Customer Forum accepted AusNet Services' five-minute metering proposal, subject to the AER being satisfied the revenue sought fairly covered the cost involved of this mandatory change." (p.21)

(d) IT move to the cloud ($7.85m)

[3] AER op cit p.4

"…the Customer Forum supported, in principle, AusNet Services' proposed investment in the Customer Relationship Management and Outage Management systems. The Customer Forum concluded the proposed budget and scope for these projects was outside its expertise. It further concluded that the AER would be better equipped to analyse these aspects of the proposals."

(e) Relocation of costs associated with shared data and communications offset by a reduction in metering charges ($31.7m)

"… the Customer Forum noted this is a methodological change, requiring a decision from the AER."

All this suggests there was not a lot of negotiation – either because of a lack of expertise or lack of information or both.

(iv) Productivity growth

We welcomed the Forum's support for a productivity factor of 1.5%, but this was never going to be a negotiation issue. AusNet's position[4] was that it was simply going to accept the outcoming of the AER's opex productivity review – which concluded with a factor of 0.5%.

Given the Forum's conclusions on opex that:

> "The Forum believes the proposal represents overall value for money for customers, provided a 1.5% productivity reduction is applied."(p.22)

but that a $15/yr reduction in annual AusNet charges (out of a total of $851 and before application of any opex productivity factor) is a "tangible benefit", we look forward to seeing what further negotiation occurs on opex.

(v) Capex

We note that the negotiations on augex and repex are ongoing and the Forum awaits further information for AusNet and consumer research before expressing a more comprehensive view. We would particularly support the approach of the Forum in two areas associated with repex:

- undertaking further customer research on trading "…a modest reliability decrease for a cost saving" (p.32) which we comment on further below, and
- seeking a stronger justification for capex. The Forum's experience is similar to what the EUAA has experienced in many other network consultations:

  "Individual projects were also lacking a clear link between expenditure, work and customer benefit. None of the projects featured in the repex presentation articulated how customers would benefit, beyond reliability, including those life support customers affected by the proposed works. AusNet Services acknowledged this as a weakness and agreed to include customer benefits in future publications." (p.32)

It was always going to be difficult for the Forum to negotiate a particular category of expenditure and this was shown in the repex deep dive on 13th March:

- in the case of the specific projects discussed the costs, not surprisingly, keep moving about and will continue changing after the conclusion of the Forum's work in June

[4] Draft Plan p. 53

- much of repex is best considered in the context of the AER's repex model, but the complexity of this model, especially the recent moves to four different scenarios, does not seem to have been discussed with the Forum.

The Forum's discussion of innovation expenditure again shows the value of its customer research to inform expenditure decisions. We look forward to AusNet providing a much more comprehensive justification for innovation expenditure along the lines of the principals set out by the Forum on p. 34. We would add one more – that the innovation being undertaken by AusNet is actually "innovation" i.e. adds significantly to the network and its customers knowledge and is not a repetition or variant of research previously or currently being undertaken by another network or research organisation. AusNet needs to undertake more comprehensive engagement if they are to convince consumers that innovation expenditure is in their long-term interests.

We look forward to the further deep dives on DER and Innovation (23rd May) and ICT (30th May) to get a better understanding of AusNet's approach and justification for capex expenditure.

(vi) Price path

The EUAA supports the final negotiated variation of Option 1 price path with the maximum price reduction in year

1. We also support the comments of a consumer advocate who highlighted that their constituents only understood nominal price when talking about price paths – they are the prices customers actually pay.

Overall reasonableness of the proposal

We agree with the Forum's conclusion that:

> "AusNet Services management has a genuine intent to improve the company's customer orientation. We have seen tangible evidence of this intent in:
>
> - Structural, policy and process changes
> - Increased resources allocated to customer-facing initiatives
> - A willingness to agree to Customer Forum recommendations during the negotiation process

Otherwise the Forum's conclusions on this matter are confusing:

> "…cannot offer a definitive opinion…at this point in time"
> "…the draft proposal appears reasonable"
> "… a 1.5% productivity reduction in opex is appropriate and the inclusion of this reduction would make the proposal reasonable for customers" (all on p.43)

The EUAA's approach is that, rather than using the term "reasonable" we come to a view on whether the proposal is "capable of acceptance" by the AER. We are some way from that position at this time and, based on other network resets we have been involved in, we are unlikely to come to a view before the AER's Draft Determination.

We find it difficult to see how the Forum could come to a view on the reasonableness of the proposal prior to the end of its role when AusNet submits its proposal in July. For example:

- as we noted above, the Forum is looking to the AER to pass judgement on the Base Year and this will not occur until the Draft Determination in March 2020
- the Forum's considerations cover ~9% of forecast capex; the AER will run its repex model to assess the reasonableness of this $600m capex component and this will not be formally available until the March 2020

- given the Forums support for 1.5% opex productivity, the AER's decision for 0.5%/yr will mean that opex will be much higher that the Forum's preferred position on which they argue for "reasonableness"

Where the CF can help is in developing the information required to assist consumer advocates in arriving at a conclusion post the AER's Draft Decision, that the proposal in "capable of acceptance". While we support increased consumer research on the trade-off between cost and reliability, this research is notoriously difficult to do in a way that gets information that can be directly applied in developing the revenue proposal. The initial repex survey results provided to the repex deep dive on 12th March should be used with caution:

- the questions asked took no account of the expected contribution of the specific repex projects to reliability vs other matters that have a much greater impact on reliability
- there are limitations from asking about "17 cents extra per year in 2022 increasing to around 70 cents per year in 2025" for one project; in theory this would mean if you had 50 different willingness to pay surveys that all got a >70% preferring to pay more, that you could add up all the 17/70 cents and argue that there is a willingness to pay an additional $35/yr from 2022; but that is not the case.

Concluding Comments

The Consumer Forum has conducted a comprehensive analysis of consumer preferences that has provided substantial information input to facilitate their negotiation process and to inform AusNet as it has developed its Draft Plan. This is very welcome.

The EUAA is looking forward to further advice from AusNet on how it will structure consumer engagement post the finish of the Consumer Forum in July with the submission of AusNet's revenue proposal to the AER.
We are less convinced of the Consumer Forum's results from their negotiation process with AusNet. There are two aspects:

(i) the skills of the Consumer Forum

The AER Guidance Note 9 says (p.2):

> "The Customer Forum does not represent the perspectives of particular interests, instead it conducts research and customer engagement to ensure it can effectively represent the perspectives of all the network businesses' customers. The Customer Forum's representatives are selected to credibly represent perspectives of all end users, be they residential, small business or commercial and industrial. These persons are also required to have relevant skills and experience to ensure they function as an effective and robust counterparty to the network business."

We have no doubt about the Forum's skills in consumer engagement. However, we have concerns around their ability to act as an effective counterparty in negotiations on opex and capex expenditure. While they have had extensive briefings from the AER and AusNet on the processes used and issued involved, there is still a large information and knowledge asymmetry between the Forum and Ausnet.

(ii) the scope of the negotiations

The scope covers less than 10% of the 2021-26 revenue cap. An even then we are unclear about the value add than the negotiation process has provided to consumers. In most segments of the negotiation the Forum either did not have the skills or did not have the information from AusNet (or both) to be able to undertake an effective negotiation.

We think it is premature to make any judgement about "reasonableness" and indeed, given the Forum's timetable, we doubt they can ever make any judgement about "reasonableness" of the whole proposal, only about their very limited scope. These conclusions can only reasonably be made post the AER's Draft Determination. Which is why we look forward to further advice from AusNet (and the AER/ENA/ECA) on where they see consumer engagement heading post July 2019.

Our final comments relate to the AER Note issued on 1st April 2019. It says that:

> "The purpose of this guidance note is for AER staff to assist the New Reg process."

But the New Reg process finishes in July with AusNet's submission of its Initial Regulatory Proposal. The suggestions for additional information AusNet could provide on opex and repex came after the opex deep dive on 11th February and the repex deep dive on 12th March. Perhaps we will see the AER Note recommended information at the remaining deep dives on DER/innovation and ICT.

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The discussion here covers some of the issues already discussed in the context of the Forum's Interim Engagement as well as the Forum's out of scope issues. We structure this part of the submission using the specific questions AusNet has asked.

The AusNet deep dive sessions which have provided very useful information to assist our understanding of their Draft Plan. What was not possible in these sessions was to answer the specific questions eg:
At the deep dive on 11th February:

> "Your feedback is sought on which base year we should use for our regulatory proposal."

At the deep dive on 12th March (slide 24) referring to major repex projects:

> "Which of the proposed portfolios do you consider strikes the right balance between cost and reliable supply to customers?
>
> "Would customers be willing to consider project deferrals that would reduce costs but also reduce network reliability? e.g. the alternative portfolio shown on slides 21-22"

These questions came at the end of a discussion for ~75min on the six repex major project portfolio options that were presented to the Customer Forum. A complication was that a different Option 7 had been discussed with the Customer Forum but it was not described in the slides. It was impossible for consumer advocates to answer these questions.

The best that can be said, at this stage in the reset cycle, is to comment on the information provided and suggest further information that needs to be provided to assist us to make a fully informed decision.

This approach informs our comments below on specific expenditure questions.

1. *<u>Improving customer experience</u>*
   - *Do you support the proposed customer experience actions?*
   - *What other service improvement could we take that would increase the value of our services?*

The CEO Forward puts it well:

> "…to ensure our industry can deliver services and service levels that meet customers' expectations, we will need to work more closely with customers and communities, particularly at a grassroots level, and with other parts of the energy supply chain. This Draft Proposal has been developed with this in mind…
>
> Whilst we have made many improvements in our service delivery, decisions have been made in conjunction with regulators and other stakeholders but often without direct customer input, albeit with customers' best interest in mind.
>
> We are committed to building a truly customer-focused, modern energy business."

We welcome this approach and our involvement over the last 6 months has showed that these sentiments are genuine as AusNet seeks to transform its consumer engagement.

2. *<u>Incentive to improve customer satisfaction</u>*

- *Do you support the principle of an incentive scheme that provides electricity distribution companies with financial rewards if customer satisfaction improves, and penalises them if it declines?*

Yes. As the Draft notes (p.16):

> "We have also been challenged to provide customers with better value from what we currently do and to reduce customer bills"

3. *Extending the use of smart meters to deliver services to customers*
   - *Would you value the listed services that can be delivered by smart meters?*

The EUAA supports the use of smart meters to enable more efficient network management to improve reliability, for improving the information available to consumers to manage their electricity consumption and for the implementation of more cost reflective pricing to various customer segments to reduce the level of inefficient cross-subsidies. We also recognise the importance of consumer education on the benefits of smart meters.

4. *Overall revenue requirement and price path*
   - *Do you have any comments or feedback on the total revenue requirement?*
   - *Do you support the proposed approach to adjusting prices over 2021-25, specifically a reduction from 2020 to 2021, after which base prices would increase with inflation?*

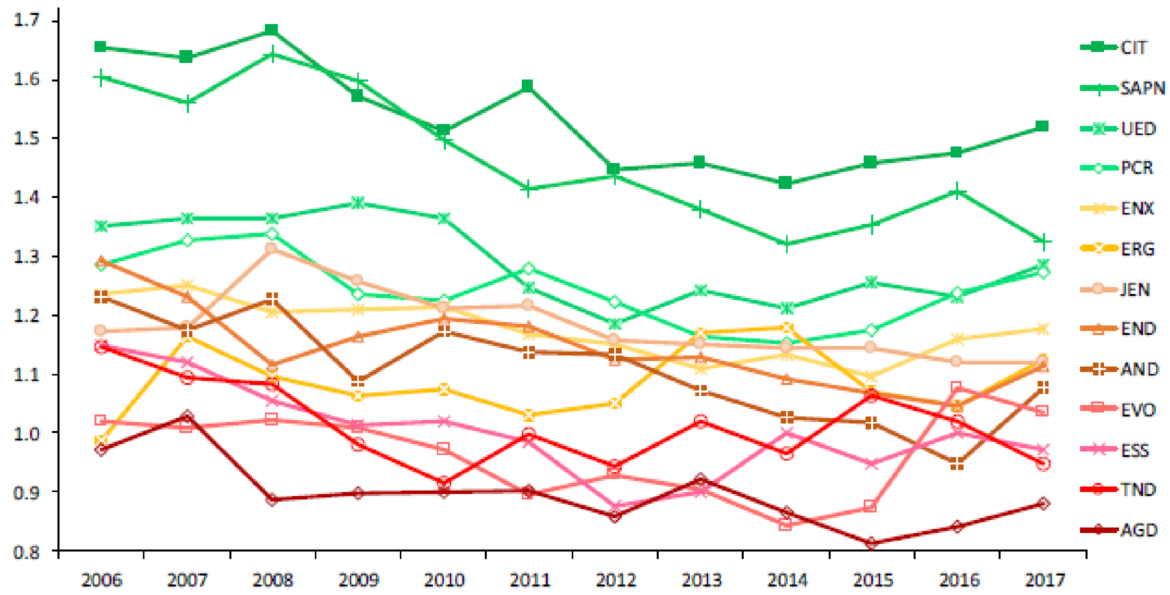
We note that forecast 2021-25 revenue is 2.6% higher in real terms than forecast for 2016-20 and that excluding EBSS and CESS benefits from the current period, forecast 2021-25 revenue would be 3% less (assume this is a real terms comparison) than forecast 2016-20. We focus on revenue excluding metering costs.

We also focus on nominal price changes as we believe they better reflect what consumers are paying. The numbers presented are "per customer" which does not provide the detail on the impact on our members so we look forward to giving further comments when this more granular data is presented.

The context is that while the Draft Plan highlights AusNet's improved its overall multi-factor total productivity in 2017 (p. 10), the trend is falling productivity over the 2006-17 period. There is a similar trend for opex partial productivity. Even with this improvement in MTFP, AusNet only improved from 12th to 9th out of 14 DNSPs.[5]

[5] See AER "Annual benchmarking report Electricity distribution network service providers" November 2018 pp iv and v

Figure 4.2 MTFP indexes by individual DNSP, 2006–17



It is not convincing to argue as the Draft Report does (p.54):

> "AusNet Services' operating costs are influenced by factors that are outside of our control and which do not affect all distributors similarly, including the rural reach of our network into mountainous areas and our costly obligations to manage high bushfire risk (only faced by one other network in Australia)."

Every network argues that it is "different" and environmental factors vary. However, that does not explain AusNet's *relative* performance in the league table. We look forward to seeing the evidence that (p.54):

> "The AER's analysis shows that AusNet is an efficient business."

Further, as the Houston Kemp report attached to the AusNet December 2018 submission on opex productivity argued, productivity trends can only be viewed on a long-term basis:

> "However, the diversity and volatility of historical productivity changes illustrated in Figure 3 and uncertainty as to future drivers of productivity underlines the importance of a conservative approach to forecasting future productivity growth, ie, consideration of the longest possible measurement period to reduce the risk that short-term volatility in productivity is not mistaken to be representative of long-term trends in productivity."[6]

So, we take the improvement in 2017 as welcome, but not indicative of a longer-term improvement.
What we do see in the Draft Plan is:

- Continued improvement on the level of reliability (p. 24):

[6] See HoustonKemp "Pre-emptive productivity adjustments" May 2018 p.10

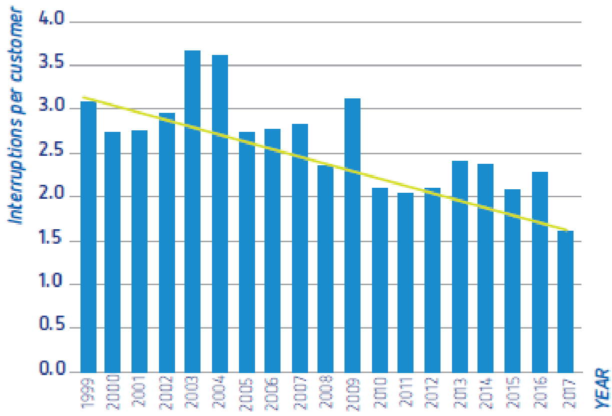


Figure 3.3: Total number of unplanned interruptions per customer

- EBSS payments of $95m and CESS payments of $85m in 2021-25 flowing from reductions in expenditure in the current regulatory period

The purpose of these incentive schemes is to reward a network for reducing expenditure below the efficient and prudent level. At first glance it is reasonable to conclude that the combination of these two factors would suggest a considerably lower level of both opex and capex in 2021-25 as AusNet seeks to improve its relative productivity performance - noting that other networks are making significant “catch-up” gains.

The issues are:

- what level of reduction in capex and opex should consumers get 100% of the benefit for (through a reduction in approved expenditure) and what should be the starting level of expenditure from where the incentive schemes, where the consumer only receives 70% of the benefit, start?”

While AusNet is being told that (p. 51):

> “Business customers are particularly focused on reliability, with 96% describing it as ‘very important’”.

our members are telling us that the existing levels of reliability are generally acceptable. They are not willing to pay for further improvements in reliability and they expect existing levels of reliability to be provided at lower real costs as networks improve their productivity.

The AusNet advice is that ~57% of the proposed price falls in year 1 are the result of the revised AER binding WACC guideline – excluding the impact of lower interest rates. It also excludes the impact of the 0.5% opex productivity and revised tax allowance calculations, both of which flow from recent AER reviews. These will further increase the price falls and further reduce the contribution to those price falls of the actual reduction in opex and capex by AusNet.

We generally support a price path that brings the price reductions in year 1.

5. *Operating expenditure proposal for 2021 to 2025*
    - *Which aspects of our operating expenditure proposals do you support and why?*
    - *What changes, if any, would you like to see?*

It is not possible at this stage to indicate support for any particular aspect of the proposed opex. All we can say is:

- We are encouraged by the proposed 5% real reduction prior to application of the AER's 0.5% productivity factor applies; it provides a good starting point for discussions around further reductions
- We will engage with the AER on the issues around whether the base year is "not materially inefficient" to ensure that the EBSS is only applied to the efficient and prudent level of opex

  As AusNet argued in its submission to the AER's review of opex productivity:

  "It is important to highlight that the AER's draft decision only concerns a productivity adjustment for 'frontier shifts' and that other, firm-specific productivity gains (catch-up) is treated separately in the regulatory regime. AusNet Services has enacted significant cost reduction programs in the 2016-2020 regulatory period, which has lowered opex and resulted in a significant improvement in productivity in 2017. We expect this trend to continue up to at least 2019. These productivity improvements are specific to AusNet Services and are an example of 'catch-up' rather than a shift in the productive frontier. Due to the operation of the Efficiency Benefit Sharing Scheme (EBSS) our customers capture 70% of the benefits of this catch-up and AusNet Services retains 30%. This provides a strong incentive for DNSPs to pursue operational efficiencies, while ensuring customers share the benefits."[7]

  We would argue that "catch-up" should not get EBSS benefits. These should only apply after a network has "caught up".

- While we understand the reasons behind the proposed step changes we are unable to support these before the AER undertakes a more detailed assessment; this is also the case for labour cost trends

6. <u>Capital expenditure proposal for 2021-25</u>
   - *Which aspects of our capital expenditure proposals do you support, taking into account the understanding that reduced expenditure in some areas will result in lower reliability and that AusNet Services is obliged to spend on certain things because of its statutory obligations?*
   - *What changes, if any, would you like to see?*

The EUAA believes that the characterisation of the issues in the question is misleading. We do not accept the implicit premises in the question that:

- Reduced expenditure will result in lower reliability – after all reliability has improved in the current period with a considerable reduction in capex compared with allowed levels giving AusNet a significant CESS benefit in 2021-26
- Reduced reliability in return for lower prices is not desired by at least some consumers
- A statutory requirement to spend on certain functions only sets a requirement to meet certain standards, it does not specify a certain $ level of expenditure. That is up to the network to ensure that it is the least cost way of achieving that statutory requirement

As noted above, we await the AER's analysis of the proposed capex eg through the repex model and other investigations, before expressing a view. We will have a particular focus in ICT – similar to our approach in other concurrent revenue resets. Just because (p.55):

> "Our IT costs are in line with previous periods, excluding the impact of new regulatory obligations."

Is not a reason to support the proposed expenditure.

[7] AusNet Submission 20 December 2020 p.3

It falsely assumes the current period level was efficient. Just because it was approved by the AER does not necessarily mean it was efficient. We look forward to a much more robust analysis of the benefits of the proposed ICT expenditure which we prefer to be assessed on a totex basis. Networks are changing the way they incur ICT costs eg

- Outsourcing functions previously performed in-house so a capex and opex spend becomes an opex spend
- Looking to change depreciation lives so that ICT expenditure is written-off relatively quickly
- Incurring much higher costs in areas like cyber security

We look forward to the ICT deep dive on 30th May and the forthcoming AER wide review of ICT expenditure.

7. *Innovation expenditure proposal for 2021 to 2025*
   - *Do you support the principle that we should spend on innovation to prepare for:*
     - *even greater levels of solar and battery uptake?*
     - *future disruption, such as electric vehicles?*
   - *What (else) do you consider the innovation programs should focus on or deliver?*

We have completed an initial review of the proposed Innovation expenditure as part of the deep dive process. We look forward to the AER's analysis of the items. We would encourage AusNet to consider the approach to be adopted by Ausgrid for its 2019-24 innovation expenditure - the establishment of a Network Innovation Advisory Committee with consumer advocates as members to review proposed capex and the exclusion of that capex from CESS.

8. *Supporting solar installations*
   - *There is a trade-off between allowing solar exports to the network (selling back into the grid) and controlling costs. How do you think this should be balanced?*
   - *Do you with the view expressed by our customers that all customers should contribute to upgrading the network to support solar exports?*

The EUAA does not support unconstrained solar exports to the grid. The full costs in increased solar exports to the grid should be met by the consumer who wishes to export. We see socialisation of these costs as inefficient and inequitable.

9. *Pricing structures*
   - *Do you support keeping the current cost reflective pricing structures for commercial and industrial an large business customers?*

Yes. Want support the moves though the AER's TSS guidelines for moving quickly towards cost reflective pricing for all customers.

10. *Metering charges*
    - *Do you have any comments on the proposed metering charges?*

No comments.