Final Decision
Ausgrid
Determination 2024 to 2029
(1 July 2024 to 30 June 2029)

Attachment 6
Operating expenditure

April 2024

AUSTRALIAN ENERGY REGULATOR

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1	30 April 2024	31

List of attachments

This attachment forms part of the AER's final decision on the distribution determination that will apply to Ausgrid for the 2024–29 period. It should be read with all other parts of the final decision.

As a number of issues were settled at the draft decision stage or required only minor updates, we have not prepared all attachments. The final decision attachments have been numbered consistently with the equivalent attachments to our draft decision. In these circumstances, our draft decision reasons form part of this final decision.

The final decision includes the following documents:

Overview

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 12 – Customer service incentive scheme

Attachment 13 – Classification of services

Attachment 14 – Control mechanisms

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Attachment 16 – Alternative control services

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6 Operating expenditure

Operating expenditure (opex) refers to the operating, maintenance and other non-capital expenses incurred in the provision of standard control services. Forecast opex for standard control services is one of the building blocks we use to determine a service provider's total regulated revenue requirement.

This attachment outlines our assessment of Ausgrid's proposed total opex forecast for the 2024–29 regulatory control period (2024–29 period).

6.1 Final decision

Our final decision is to not accept Ausgrid's total opex forecast of $2,233.7 million ($2024–24) for the 2024–29 period. We consider Ausgrid's revised proposal largely reflects prudent and efficient costs required to achieve the opex objectives in the 2024–29 period. However, we consider that Ausgrid's Software as a Service (SaaS) implementation costs (which it had allocated to capital expenditure (capex) in its revised proposal) should be reallocated to total forecast opex, consistent with the accounting treatment of these costs and our draft decision.

Accounting for this reallocation, our alternative estimate of total forecast opex (including SaaS implementation costs) is $2,344.0 million ($2023–24). This is not materially different to Ausgrid's revised proposal total opex forecast (including SaaS implementation costs) of $2,364.9 million ($2023–24) on a like-for-like basis.[1]

Our final decision is therefore to determine a substitute total opex forecast of $2,364.8 million ($2023–24), including our estimate of debt raising costs, for the 2024–29 period, as reasonably reflecting the opex criteria.[2] This consists of Ausgrid's revised proposal opex forecast of $2,233.7 million ($2023–24), plus SaaS implementation costs of $131.2 million ($2024–24), which we have allocated to opex, and our estimate of debt raising costs.

Table 6.1 sets out Ausgrid's revised opex proposal, its revised proposal with SaaS implementation costs added back into opex as a step change (the basis for our comparison), our alternative estimate, and the difference between our alternative estimate and Ausgrid's revised proposal (including SaaS implementation costs).

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1 Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis. Includes SaaS implementation costs of $131.2 million and our estimate of debt raising costs.

2 The opex criteria are set out in cl. 6.5.6(c) of the NER.

Table 6.1: Comparison of Ausgrid's revised proposal and our final decision on total forecast opex ($million, 2024–29)

	Revised Proposal	Revised Proposal (with SaaS and AER debt raising costs) (a)	Alternative Estimate (b)	Difference (b – a)
Based on reported opex in 2022–23	2,087.6	2,087.6	2,081.5	–6.0
Total base year adjustments	**34.7**	**34.7**	**34.7**	**0.0**
2022–23 increment	**10.0**	**10.0**	**10.0**	**–0.0**
Total trend	**40.1**	**40.1**	**42.4**	**2.2**
Step change: Cyber security	18.1	18.1	18.1	–
Step change: Insurance premiums	11.3	11.3	–	–11.3
Step change: Climate resilience	5.9	5.9	3.2	–2.7
Step change: Smart meter data	10.2	10.2	10.2	–
Step change: Network innovation program	–	–	–	–
Step change: ICT enablement for CER integration	6.4	6.4	6.4	–
Step change: Property	–15.3	–15.3	–15.3	–
Step change: SaaS	–	131.2	131.2	–
Total step changes	**36.5**	**167.7**	**153.7**	**–14.0**
Debt raising costs	46.3	46.3	46.2	–0.1
Category specific forecast: Network innovation program	4.5	4.5	1.6	–2.9
Category specific forecast: remove debt raising costs	0.2	0.2	0.2	–0.0
Total	**2,233.7**	**2,364.9**	**2,344.0**	**–20.9**

Source: Ausgrid, *Att. 6.1.a – Opex model, 31 January 2023*; Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.

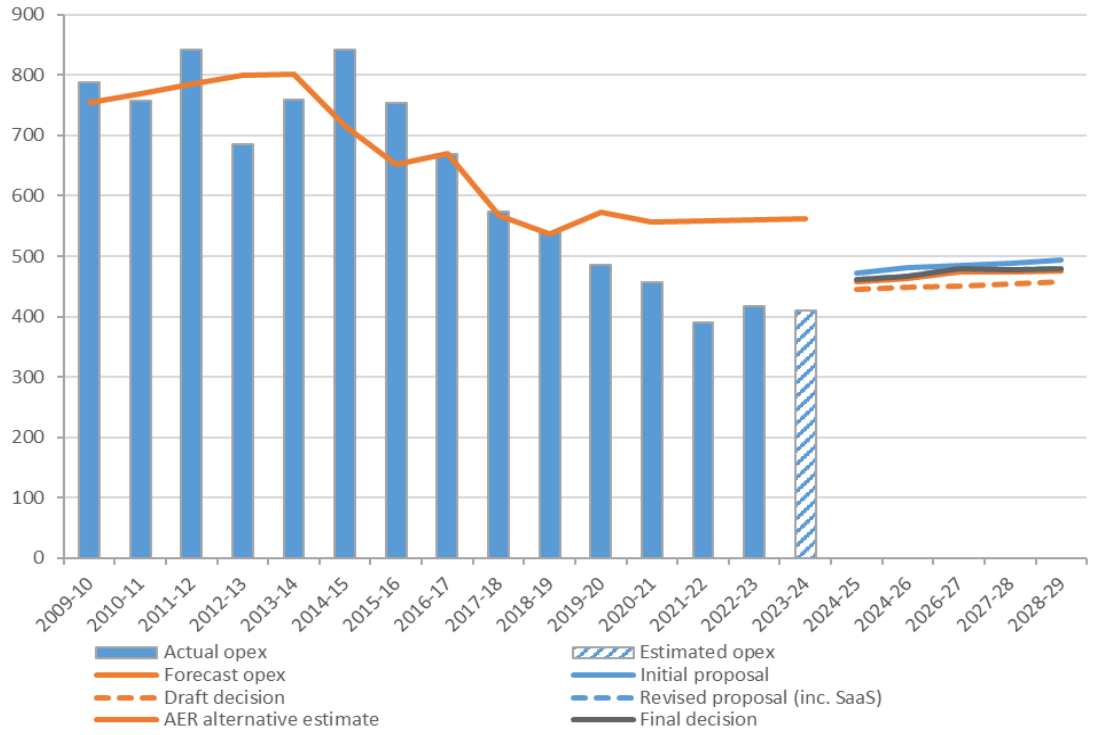
Note: Numbers may not add up to totals due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

Figure.6.1 compares the total opex forecast for Ausgrid we have included in the final decision for the 2024–29 period[3] (dark blue line) to Ausgrid's revised total opex proposal (blue dashed line), as well as Ausgrid's actual and estimated opex in the previous and current regulatory control period (the blue bars). We have also included the forecasts we approved in past decisions (the orange line), Ausgrid's initial proposal for the 2024–29 period (light blue line) and our alternative estimate for the draft decision (orange dashed line).

Our final decision total opex forecast is:

- $447.6 million ($2023–24) or 15.9% lower than the opex forecast we approved in our final decision for the 2019–24 regulatory control period[4]
- $202.9 million ($2023–24) or 9.4% higher than Ausgrid's actual (and estimated) opex in the 2019–24 regulatory control period
- $55.7 million ($2023–24) or 2.3% lower than Ausgrid's initial proposal
- $110.5 million ($2023–24) 4.9% higher than our draft decision
- $0.1 million ($2023–24) or 0.0% lower than Ausgrid's revised proposal (with SaaS).[5]

Figure.6.1: Comparison of past and forecast opex ($million, 2024–29)



Source: Ausgrid, *Economic benchmarking – RIN response 2009–23*; AER, Final decision PTRM 2009–14; AER, *Final decision 2014–19 PTRM*; AER, *Final decision 2019–24 PTRM* and *Opex model*; Ausgrid, *Revised proposal – Att. 6.2 – Opex model, 30 November 2023*; AER analysis.
Note: Includes debt raising costs and movements in provisions.

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3 Ausgrid's revised proposal opex forecast plus its SaaS implementation costs.

4 Difference is calculated based on the opex allowance for the five-year 2019–24 period converted to real 2023–24 dollars using unlagged inflation.

5 Due to our slightly lower estimate of debt raising costs.

The following factors contributed to our slightly lower alternative total opex forecast for our assessment purposes (when compared to Ausgrid's revised proposal opex forecast, including SaaS implementation costs):

Step changes ($14.0 million lower than Ausgrid's revised proposal):

- we have not included Ausgrid's proposed step change for insurance ($11.3 million), consistent with our draft decision
- we have included a lower estimate for Ausgrid's proposed climate resilience step change ($3.2 million) which is $2.7 million lower than Ausgrid's revised proposal.

Category specific forecasts ($2.9 million lower than Ausgrid's revised proposal):

- we have included a lower estimate ($1.6 million) for Ausgrid's network innovation program, which is $2.9 million lower than Ausgrid's revised proposal.

6.2 Ausgrid's revised proposal

Ausgrid included total forecast opex of $2,233.7 million ($2023–24) in its revised proposal for the 2024–29 period. Including SaaS implementation costs (which is our approach for this final decision), this opex forecast is $2,364.9 million ($2023–24), as set out in Table 6.2.

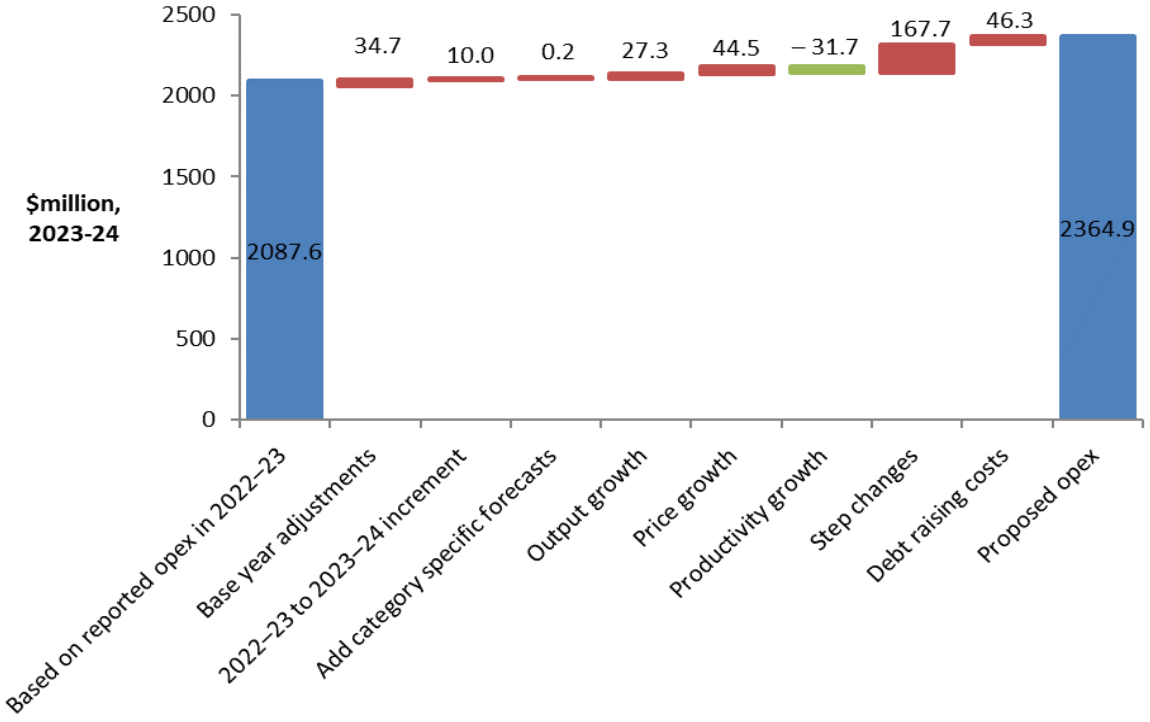
Table 6.2: Ausgrid's proposed opex ($million, 2024–29)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Total opex excluding debt raising and SaaS costs	429.2	435.8	436.8	440.8	444.7	2187.4
SaaS implementation costs	23.2	22.0	32.6	28.0	25.4	131.2
Debt raising costs	9.2	9.3	9.3	9.3	9.3	46.3
Total opex	**461.6**	**467.0**	**478.7**	**478.1**	**479.4**	**2,364.9**

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model, 30 November 2023.*
Note: Numbers may not add up due to rounding.

Figure 6.2 separates Ausgrid's revised proposal total opex forecast (including SaaS costs as a step change) into its different components.

Figure 6.2: Ausgrid's revised proposal opex forecast – inc. SaaS ($million, 2024–29)



Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model, 30 November 2023*; AER analysis.

Ausgrid continued to use our standard 'base-step-trend' approach[6] to forecast opex for the 2024–29 period in its revised proposal.

In applying our base-step-trend approach to forecast opex for the 2024–29 period, Ausgrid:[7]

- used actual opex in 2022–23 as the base from which to forecast ($2,087.6 million)
- removed $26.3 million from base opex to reflect non-recurrent efficiency gains
- removed $0.3 million from base opex related to ongoing lease costs
- added $35.0 million to base opex to reflect its updated cost allocation method
- added $10.0 million to reflect the change in opex between 2022–23 and 2023–24
- added $0.2 million to account for the removal of opex categories forecast separately from its base opex
- applied an overall rate of change forecast to its base year opex, increasing opex by $40.1 million, comprising of:
  - output growth ($27.3 million)
  - real price growth ($44.5 million)
  - productivity growth (–$31.7 million) or 0.5% per year.

6 Our base-step-trend approach is set out in our expenditure guideline. See AER, *Expenditure forecast assessment guideline – distribution*, August 2022, pp. 24–27.

7 Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023.

- added 6 step changes totalling $36.5 million for:
  - insurance premiums ($11.3 million)
  - climate resilience ($5.9 million)
  - cyber security uplift ($18.1 million)
  - smart meter data ($10.2 million)
  - ICT enablement for CER integration ($6.4 million)
  - lower property costs (–$15.3 million)
- added $4.5 million as a category specific forecast for its network innovation program
- added $46.3 million of debt raising costs to arrive at total forecast opex of $2,233.7 million ($2023–24) over the 2024–29 period.

As stated, Ausgrid's revised proposal allocated SaaS implementation costs to capex, rather than opex as per its initial proposal. For our final decision, we have included these costs ($131.2 million ($2023–24)) in Ausgrid's total opex forecast.

6.2.1 Stakeholder views

We received 3 submissions on Ausgrid's 2024–29 revised proposal that raised issues related to opex. These submissions were from Ausgrid's Regulatory Customer Panel (RCP), which broadly supported Ausgrid's revised opex forecast,[8] Ausgrid's Network Innovation Advisory Committee, which supported Ausgrid's Network Innovation Program,[9] and the Consumer Challenge Panel (CCP26), which queried aspects of the revised proposal related to Ausgrid's reclassification of its SaaS implementation costs and its proposed climate resilience and network innovation programs. CCP26 deferred to the AER to have careful consideration of these issues.[10]

These submissions are discussed in more detail in Section 6.4 below.

6.3 Assessment approach

Under the regulatory framework, a business must include a forecast of total opex that it considers is required to meet or manage expected demand, comply with all applicable regulatory obligations, and to maintain the safety, reliability, quality, and security of its network and contribute to achieving emissions reduction targets (the opex objectives).[11]

Our role is to decide whether to accept a business's total opex forecast. We are to form a view about whether a business's forecast of total opex 'reasonably reflects the opex criteria,' including whether it is a prudent and efficient way of meeting the opex objectives.[12] In doing so, we must have regard to each of the opex factors specified in the National Electricity

8 RCP, *Submission on Ausgrid's revised proposal and draft decision 2024–29*, January 2024.

9 Networks Innovation Advisory Committee, *Submission on Ausgrid's revised proposal and draft decision 2024–29*, January 2024, p.3.

10 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision – Ausgrid*, January 2024, pp. 9-11.

11 NER, cl. 6.5.6(a).

12 NER, cl. 6.5.6(c).

Rules (NER).[13] We must make our decision in a manner that will, or is likely to, contribute to the achievement of the National Electricity Objective.[14]

The *Expenditure forecast assessment guideline* (the Guideline) sets out our assessment approach in detail.[15] While the Guideline provides for greater regulatory predictability, transparency and consistency, it is not mandatory. However, if we make a decision that is not in accordance with the Guideline, we must state the reasons for departing from the Guideline.[16] Where relevant we must also assess opex associated with emissions reduction proposals taking into account our *Guidance on amended National Electricity Objective*.[17]

Our approach is to assess the business's forecast opex over the regulatory control period at a total level, rather than to assess individual opex projects. To do so, we develop an alternative estimate of total opex using a 'top-down' forecasting method, known as the 'base-step-trend' approach.[18] We compare our alternative estimate with the business's total opex forecast to form a view on the reasonableness of the business's proposal. If we are satisfied the business's forecast reasonably reflects the opex criteria, we accept the forecast. If we are not satisfied, we substitute the business's forecast with our alternative estimate that we are satisfied reasonably reflects the opex criteria.

In making this decision, we take into account the reasons for the difference between our alternative estimate and the business's proposal, and the materiality of the difference. Further, we take into consideration interrelationships between opex and the other building block components of our decision.[19]

Figure 6.3 summarises the ‘base-step-trend’ forecasting approach.[20]

13 NER, 6.5.6(e).

14 NEL, s. 16(1)(a). The National Electricity Objective is set out in s. 7 of the NEL.

15 AER, *Expenditure forecast assessment guideline – distribution*, August 2022; AER, *explanatory statement – expenditure forecast guideline*, November 2013.

16 NER, cl. 6.2.8(c).

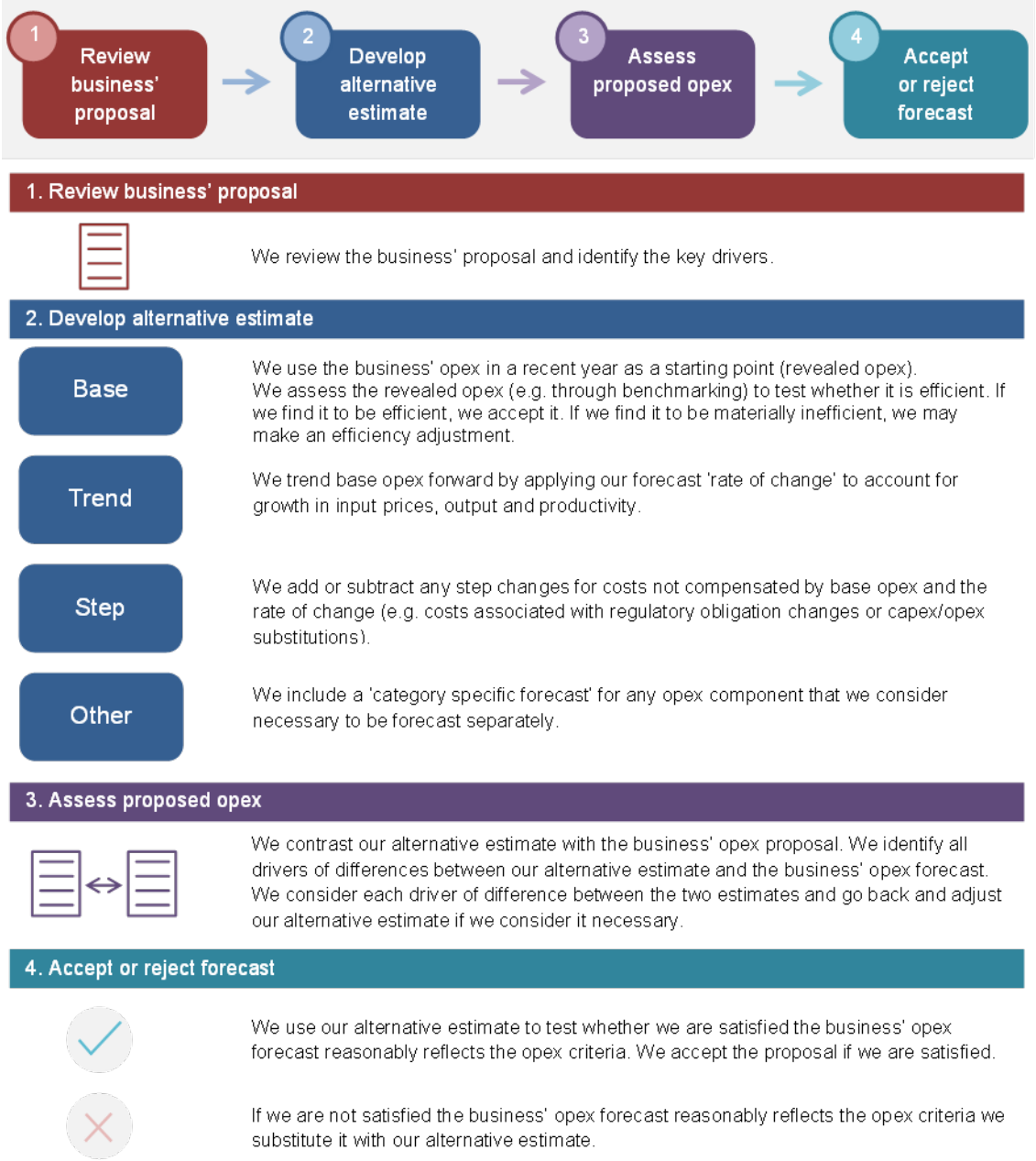
17 AER, *Guidance on amended National Electricity Objective*, September 2023.

18 A 'top-down' approach forecasts total opex at an aggregate level, rather than forecasting individual projects or categories to build a total opex forecast from the 'bottom up’.

19 We are required to take into account these interrelationships under s. 16(1)(c) of the NEL.

20 Our base-step-trend approach is set out in our expenditure guideline. See AER, *Expenditure forecast assessment guideline – distribution*, August 2022, pp. 24–27.

Figure 6.3: Our opex assessment approach



6.3.1 Interrelationships

In assessing Ausgrid's total forecast opex, we took into account other components of its proposal and our determination, including:

- the efficiency benefit sharing scheme (EBSS) carryover—the estimate of opex for 2023–24 (the final year of the current regulatory control period (2019–24)) that we used to forecast opex, was the same as the level of opex we used to calculate EBSS carryover amounts. This consistency ensures that the business is rewarded (or penalised) for any efficiency gains (or losses) it makes in the final year the same as it would for gains or losses made in other years
- the operation of the EBSS in the 2019–24 period, which provided Ausgrid an incentive to reduce opex in the base year

- the impact of cost drivers that affect both forecast opex and forecast capital expenditure (capex). For instance, forecast labour price growth affects forecast capex and our forecast price growth used to estimate the rate of change in opex
- the approach to assessing the rate of return, to ensure there is consistency between our determination of debt raising costs and the rate of return building block
- concerns of electricity consumers identified during Ausgrid's engagement with consumers.

6.4 Reasons for final decision

We consider Ausgrid's revised proposal total opex forecast, with the re-inclusion of its SaaS implementation costs (which it had allocated to capex for its revised proposal), is prudent and efficient and therefore reasonably reflects the opex criteria.[21]

Ausgrid's total opex forecast in its revised proposal, $2,233.7 million ($2023–24), plus its SaaS implementation costs of $131.2 million ($2023–24), is not materially different from our alternative estimate on this basis (that is, including SaaS implementation costs). As such, we approve a total opex forecast of $2,364.8 million ($2023–24), including our estimated debt raising costs, for Ausgrid over the 2024–29 period.[22]

Ausgrid had re-classified its SaaS implementation costs as capex for its revised proposal, inconsistent with its initial proposal and our draft decision, as an affordability measure. However, for the reasons discussed at section 6.4.3.1, we consider these costs should be treated as opex in the 2024–29 period. When our alternative estimate is compared with Ausgrid's revised proposal opex forecast on a like-for-like basis (that is, if Ausgrid's revised proposal had included its SaaS implementation costs in opex), then our alternative estimate is only $20.9 million (0.9%) lower than Ausgrid's forecast.

The following sections outline the key inputs and assumptions we made in developing our alternative estimate of efficient costs for Ausgrid, using our base–step–trend approach. The opex model we used to calculate our alternative estimate is published on our website.

6.4.1 Base opex

This section provides our view on the prudent and efficient level of base opex that we consider Ausgrid would need for the safe and reliable provision of services over the 2024–29 period.

6.4.1.1 Proposed base year

Consistent with our draft decision and Ausgrid's revised proposal, we have used 2022–23 opex as the base year for forecasting our alternative estimate of opex.

We have used 2022–23 opex of $416.3 million ($2024–24), net of movements in provisions, as the starting point for our alternative estimate of total forecast opex. This is $2,081.5 million ($2024–24) over 5 years. This is slightly lower than Ausgrid's revised proposal of

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21 NER, cl. 6.5.6(c).

22 Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023.

$2,087.6 million ($2024–24), due to us using the latest Consumer Price Index (CPI) estimates available from the Reserve Bank of Australia (RBA).

Final year increment

Our standard practice to calculate final year opex, is to add the difference between the opex forecast for the final year of the preceding regulatory control period and the opex forecast for the base year, to the amount of actual opex in the base year.[23]

By forecasting opex in this way, the opex forecast assumes Ausgrid makes no efficiency gains between the base year and the final year. This allows Ausgrid to retain the efficiency gains it makes in the final year through the opex forecast.[24] This is consistent with the decision to apply the EBSS during the 2019–24 regulatory control period.

Efficiency of Ausgrid's base year opex

Our draft decision view regarding the efficiency of 2022–23 opex has not changed.[25] In our draft decision, we determined to use opex in 2022–23 as the starting point for our alternative estimate of total forecast opex over the 2024–29 period. We have considered Ausgrid's opex in the past, its performance in terms of opex multilateral partial factor productivity (MPFP), and the fact that Ausgrid's opex was subject to the incentives of the EBSS in the 2019–24 period, which gave it a continuous incentive to reduce opex, including in the base year.

6.4.1.2 Adjustments to base year opex

We have maintained the following adjustments from our draft decision, updating the numbers as relevant to reflect the most up-to-date information:[26]

- remove $26.2 million from base opex to reflect non-recurrent efficiency gains
- remove $0.3 million from base opex related to Ausgrid's ongoing lease costs
- add $35.0 million to base opex to reflect Ausgrid's updated cost allocation method
- add $10.0 million for the forecast change in opex between 2022–23 and 2023–24 (the final year increment)
- remove $0.2 million for opex categories forecast separately (debt raising costs).

These adjustments have increased our alternative estimate of total forecast opex by $18.70 million ($2024–24). This is slightly higher than Ausgrid's increase of $18.66 million ($2024–24) due to our use of the latest CPI estimates available from the RBA to bring numbers to $2023–24 terms.

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23 AER, *Expenditure forecast assessment guideline – distribution*, August 2022, p. 25.

24 AER, *Expenditure forecast assessment guideline – distribution*, August 2022, p. 25.

25 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid 2024–29 Distribution revenue proposal*, September 2023, pp. 11–16

26 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid 2024–29 Distribution revenue proposal*, September 2023, pp. 16–17.

As discussed below in section 6.4.3.1, we have included Ausgrid's SaaS implementation costs as a step change for our final decision. These costs were initially included as an opex base adjustment in our draft decision.

6.4.2 Rate of change

Having determined an efficient starting point, or base opex, we trend it forward to account for the forecast growth in prices, output and productivity. We refer to this as the rate of change.[27]

We have included a rate of change that increases opex, on average, by 0.7% each year in our alternative estimate. This contributes $42.4 million ($2023–24) to our alternative estimate. When rounded, this is the same Ausgrid's average annual rate of change (also 0.7%).[28]

Ausgrid's revised proposal accepted our draft decision approach to calculating price, output and productivity growth. It updated price growth forecasts to reflect updated wage price index (WPI) forecasts from BIS Oxford Economics,[29] as well as its output growth factor to reflect the updated output elasticities from the 2023 AER annual benchmarking report. Our final decision position on the approach to forecast the rate of change and its various components remains unchanged.[30] However, we have updated WPI to reflect the most recent forecasts from our consultant KPMG.

Table 6.3 shows both Ausgrid's revised proposal, and our alternative estimate for each component of the rate of change.

27 AER, *Expenditure forecast assessment guideline – distribution*, August 2022, pp. 25–26.

28 Ausgrid, *Revised proposal – Att. 6.2 – Opex model*, 30 November 2023.

29 Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure,* 30 November 2023, p. 19.

30 AER, *Draft Decision, Ausgrid – 2024–29 Distribution revenue proposal – Opex model,* September 2023.

Table 6.3: Forecast rate of change (%)

	2024–25	2025–26	2026–27	2027–28	2028–29
Ausgrid's revised proposal					
Price growth	0.8	0.8	0.5	0.5	0.6
Output growth	0.3	0.4	0.4	0.8	0.8
Productivity growth	0.5	0.5	0.5	0.5	0.5
Overall rate of change	**0.6**	**0.7**	**0.4**	**0.8**	**0.9**
AER's alternative estimate					
Price growth	0.9	0.9	0.5	0.5	0.5
Output growth	0.3	0.4	0.4	0.8	0.8
Productivity growth	0.5	0.5	0.5	0.5	0.5
Overall rate of change	**0.7**	**0.7**	**0.5**	**0.8**	**0.8**
Difference	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023.; AER analysis.
Note: Numbers may not add up to totals due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

6.4.3 Step changes

We have included $153.7 million ($2023–24) for step changes in our alternative estimate of total forecast opex. This is $14.0 million ($2023–24) lower than Ausgrid's revised proposal (with its SaaS implementation costs added back in), and $133.9 million ($2023–24) higher than our draft decision (see Table 6.1).

In its revised proposal, Ausgrid:

- included 6 step changes totalling $36.5 million ($2023–24), specifically Ausgrid:[31]
  - reincluded its step change for increased insurance premiums ($11.3 million), with further information. This was excluded in our draft decision
  - reincluded its step change for its climate resilience program ($5.9 million), with further information. This was excluded in our draft decision
  - included a lower step change for cyber security of $18.1 million. We included $19.0 million in our draft decision
  - included a lower step change for smart meter data of $10.2 million. We included $10.7 million in our draft decision
  - included a higher step change for ICT enablement for CER integration of $6.4 million. We included $4.6 million in our draft decision

[31] Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure*, 30 November 2023, pp. 22–23.

  - accepted our draft decision for its property strategy negative step change ($15.3 million), with minor updates for inflation ($0.8 million higher than our draft decision).

In our alternative estimate, we have:

- included 7 step changes totalling $153.7 million ($2023–24), specifically we have:
  - excluded Ausgrid's insurance premium step change
  - included a lower estimate ($3.2 million), for its climate resilience step change
  - included $18.1 million for cyber security, consistent with Ausgrid's revised proposal
  - included $10.2 million for smart meter data, consistent with Ausgrid's revised proposal
  - included $6.4 million for ICT enablement for CER integration, consistent with Ausgrid's revised proposal
  - included a negative step change of $15.3 for its property strategy
  - included $131.2 million for SaaS implementation costs reallocated from capex.

We have also updated for inflation where relevant.

Importantly, we have included the additional step change for Ausgrid's proposed SaaS implementation costs ($131.2 million ($2023–24)). This was previously included as a base adjustment in our draft decision, and in Ausgrid's initial proposal. In its revised proposal, Ausgrid revised these costs to $131.2 million ($2023–24) and allocated them to capex[32]. We have reallocated these costs back into opex for this final decision.

We discuss each of these step changes below. Table 6.4 shows Ausgrid's revised proposal along with our alternative estimate for the final decision, which is to include step changes totalling $153.7 million ($2023–24).

Table 6.4: Step changes ($million, 2023–24)

	Revised proposal	Revised proposal (with SaaS costs) (a)	Alternative estimate (b)	Difference (b – a)
Cyber security	18.1	18.1	18.1	–
Insurance premiums	11.3	11.3	–	–11.3
Community resilience	5.9	5.9	3.2	–2.7
Smart meter data	10.2	10.2	10.2	–
ICT enablement for CER integration	6.4	6.4	6.4	–
Property strategy	–15.3	–15.3	–15.3	–
SaaS implementation	–	131.2	131.2	–
Total step changes	**36.5**	**167.7**	**153.7**	**–14.0**

Source: Ausgrid, *Att. 6.2 – Opex model*, 30 November 2023; AER analysis.
Note: Numbers may not add up to totals due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

[32] Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure*, 30 November 2023, pp. 15–17.

6.4.3.1 SaaS implementation costs

Our final decision is to include a step change of $131.2 million ($2023–24) for Ausgrid's SaaS implementation costs.

Table 6.5: SaaS implementation costs step change ($million, 2023–24)

	2024–25	2025-26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal (included as capex)	23.2	22.0	32.6	28.0	25.4	131.2
AER alternative estimate	23.2	22.0	32.6	28.0	25.4	131.2
Difference	–	–	–	–	–	–

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

SaaS implementation costs have historically been treated as capital expenditure in revenue determinations. However, in April 2021, the International Financial Reporting Standards Foundation (IFRSF) clarified that in most cases, a business utilising SaaS services:

- does not control the software being configured or customised, and
- that those configuration and customisation activities do not create a resource that is controlled by the business, separate to the software, from which the business then has the power to obtain a future economic benefit.

The IFRSF consequently determined that these SaaS implementation costs should more accurately be expensed as opposed to being capitalised.[33]

Ausgrid's revised proposal approach

In its initial proposal for its 2024–29 revenue determination, Ausgrid proposed to follow IFRSF guidance in treating its SaaS implementation costs as opex rather than capex, and so proposed a base year opex adjustment to account for these SaaS implementation costs. We endorsed this position in our draft decision,[34] but our estimate for this base year adjustment was lower than Ausgrid's due to our draft decision on the underlying ICT project costs.[35]

In its revised proposal, Ausgrid included a higher estimate ($131.2 million ($2023–24)) for its SaaS implementation costs compared to our draft decision ($74.3 million ($2023–24)), and reversed its original approach to treat SaaS implementation costs as opex in the 2024–29 period in accordance with IFRS guidance. Ausgrid proposed to keep these costs in capex until the 2029–34 regulatory period, when it intended to recognise its SaaS implementation costs as opex for regulatory purposes.

Ausgrid submitted that this new treatment was included in its revised proposal as an attempt to address general affordability concerns raised by customers.[36] Ausgrid submitted that this

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33 IFRS, *AP12A: Finalization of agenda decision*, April 2021, pp. 5–6.

34 AER, *Draft Decision, Ausgrid – 2024–29 Distribution revenue proposal – Opex model*, September 2023.

35 AER, *Draft Decision, Attachment 6 – Operating expenditure – Ausgrid Distribution revenue proposal,* September 2023, pp. 18–20.

36 Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure*, 30 November 2023, p. 15.

approach would 'smooth' the net revenue impact because of the longer cost recovery timeframe associated with capex as opposed to opex. This would result in lower bills for its consumers in the short-term, who voiced concerns on affordability. Overall, Ausgrid submitted that this approach would result in $14.5 million ($2024–24) less revenue required over the next two regulatory periods.[37]

Ausgrid also submitted that "expensing SaaS implementation costs does not align with the characteristics of opex for the purpose of economic regulation. As noted in the AER's Expenditure Forecast Assessment Guideline, opex is considered to be largely recurrent, whereas SaaS implementation costs are not. Further, these costs have an economic life of a number of years over which customers derive benefit, which is a characteristic of a capitalised asset".[38]

Stakeholder views

In terms of the consumer perspective, we note that Ausgrid's RCP supported Ausgrid's revised proposal to keep its SaaS costs in capex on the following basis:

> Ausgrid's SaaS expenditure in 2024–29 be treated as capex, subject to AER considering adverse impacts on customer bills in future regulatory periods, on the basis Ausgrid reports SaaS as both opex and capex in the RINs to enable ongoing AER benchmark reporting. This is an important affordability initiative designed specifically to reduce bill impacts and to provide further cover to approve the cyber, innovation, resilience and CER programs which are customer priorities.[39]

Conversely, we note the CCP26 was sceptical of this measure and the risks it posed for consistency with how these costs are treated for other networks and the accounting guidance. CCP26 noted:

> This proposal was raised very late in the regulatory process and raises complex issues, particularly as other DNSPs are moving to treating SaaS as opex in accordance with regulatory guidance. Ausgrid acknowledges that it may be difficult for the AER to implement its proposed approach. We consider that further analysis is required to understand potential affordability impacts in future regulatory periods, as well as any unintended impacts on the regulatory system. In order for the AER to accept this proposal, the known affordability benefits should outweigh these potential costs.[40]

AER consideration and conclusion

We have considered Ausgrid's reasons for treating SaaS implementation costs as capex in its revised proposal, as well as the views from the CCP26 and Ausgrid's RCP. Ultimately, we

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37 Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure*, 30 November 2023, p. 15.

38 Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure,* 30 November 2023, pp. 15-17.

39 RCP, *Submission on Ausgrid's revised proposal and draft decision 2024–29*, January 2024.

40 CCP26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision – Ausgrid*, January 2024, pp.3–4.

maintain our view in the draft decision that Ausgrid's SaaS implementation costs should be treated as opex.

Our rationale for this decision is as follows:

Regulatory consistency and alignment with accounting standards guidance

Ausgrid's revised approach is inconsistent with our recent regulatory determinations,[41] as well as the concurrent 2024–29 regulatory proposals from Power and Water Corporation, Endeavour Energy and Essential Energy,[42] where SaaS implementation costs have been treated as opex. We also note that SA Power Networks proposed to move its SaaS implementation costs into opex for its 2025–30 proposal, with a quantum of SaaS implementation costs not dissimilar to Ausgrid's proposal.[43] While we do not believe it is appropriate to be constrained by past decisions if they are not suited to the current context, we do not consider Ausgrid's circumstances to be unique, in terms of the nature and quantum of its SaaS implementation costs, to justify departing from our previous guidance and treatment of these costs.

Additionally, our decision conforms to the latest IFRSF's guidance on the correct treatment of these costs according to the accounting standards. As the terms 'capex' and 'opex' are not defined by the National Electricity Rules, our standard approach is to adopt these accounting standards definitions and IFRSF's guidance for how costs should be classified.

We consider maintaining consistency in our treatment of opex across networks, wherever possible, is beneficial when comparing costs and for benchmarking purposes. This consistency allows us to ensure equitable treatment of costs between networks.

Treatment of SaaS costs as opex

In its revised proposal, Ausgrid stated that SaaS implementation costs should be classified as capex due to their non-recurrent nature and the ability for consumers to derive benefit from the related projects over several years. However, the IFRSF's guidance concluded that the most appropriate treatment of SaaS implementation costs is to expense them as opposed to capitalise them, given that they do not relate to an asset that is controlled by the entity (which is a key feature of capital expenditure).

Additionally, Ausgrid's revised proposal did not suggest SaaS implementation costs should be treated as capex indefinitely, but instead proposed a delay in the shift to opex until the 2029–34 regulatory period. This indicates that Ausgrid considers that in the long-run SaaS implementation costs will likely be treated as opex, so the key reason to delay this change in treatment in the interest of consumer affordability in the short term.

We understand that Ausgrid's proposed SaaS implementation costs are non-recurrent in nature (not incurred every regulatory period). However, we consider that non-recurrent SaaS implementation costs are likely to be incurred every regulatory period, but the exact amount of these costs will fluctuate between periods depending on the associated ICT projects. We consider this is not inconsistent with our standard opex assessment approach. Our

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41 For example, see AER final decision for ElectraNet and Transgrid's 2023-28 opex forecasts.

42 See AER's final decision for PWC, Endeavor and Essential's 2024-29 opex forecasts.

43 SAPN, *SAPN – 6.1 – Opex Model*, January 2024.

guidelines note that total opex as "*largely* recurrent",[44] implying that some categories of opex will not be fully recurrent.

Potential consumer savings are relatively small and temporary

We note that submissions from both the RCP and CCP26 refer to our consideration of the bill impacts of this change in future periods as well as the 2024–29 period. Ausgrid identified its proposed approach would reduce customer bills by approximately $2.30 per year in the 2024–29 period. Based on Ausgrid's analysis, this approach would then increase bills in the 2029–34 period by approximately $1.90 per year. Ausgrid's approach would also marginally increase customer bills in the 2034–39 period, assuming longer life capital assets will continue to be recovered into that period. Ausgrid's justification for this change as an affordability measure relies on the assumption that affordability will be less of an issue for consumers in the 2029–34 period than it is in the 2024–29 period. Ausgrid has not provided evidence that supports such an assumption.

Additionally, Ausgrid submitted that in the long run "there is no impact on the quantum or efficiency of forecast SaaS implementation costs" between its proposed approach and our draft decision approach.[45] As the two approaches will be net cost neutral for customers in the long run, we do not consider that Ausgrid's proposed treatment represents a genuine saving or affordability measure for consumers.

Further, Ausgrid's estimated savings of $14.5 million over the next two regulatory periods would represent a very small percentage of its total revenues over those two periods (less than 0.1% if we take it as a percentage of 2024–29 total revenue multiplied by 2). We consider this to be immaterial.

Step change vs base adjustment

We consider that a step change more accurately recognises that Ausgrid's SaaS implementation costs are forecast to occur in the 2024–29 period, and are non-recurrent, and therefore should not be included in its base year. Base year opex (and any adjustment to base year opex) is intended to reflect the level of expenditure a network is expected to incur in any typical year and is considered recurrent.

Conclusion

Our preferred approach is to therefore include Ausgrid's revised proposal SaaS implementation costs ($131.2 million ($2023–24)) as opex for our final decision, in the form of a step change, as:

- We consider the most appropriate treatment of SaaS implementation costs, for regulatory purposes, is to treat them as opex given the alignment with the accounting treatment of these costs. Given Ausgrid's circumstances are not unique, this approach should be adopted here as it has for other networks.
- We do not consider the treatment of SaaS implementation costs in the 2024–29 period to be a true affordability measure (and therefore in the long-term interest of consumers

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44 AER, *Expenditure forecast assessment guideline – distribution*, August 2022, p. 8.

45 Ausgrid, *Revised proposal – Att.6.1 – Proposed operating expenditure*, 30 November 2023, p. 17.

with respect to price), but rather a reclassification of costs resulting in a net neutral cost position in the long term.

- Ausgrid's proposal benefits current consumers at the expense of future consumers, without providing evidence to support the assumption that future consumers will be better placed to deal with cost increases than current consumers.

It is not clear that this approach is in the long-term interests of consumers generally, given the risks and downsides associated with creating inconsistency issues with other networks and with the accounting guidance around these costs.

We expect that Ausgrid will consider, in preparing its regulatory proposal for the 2029–34 period, whether it is likely to require the same level of SaaS implementation costs as for 2024–29 period. At that time, we encourage Ausgrid to consider whether any adjustment to its 2029–34 opex forecast will be required to account for any decrease in its level of SaaS implementation costs relative to those forecast for the 2024–29 regulatory period.

6.4.3.2 Insurance premiums

We have not included Ausgrid's $11.3 million ($2023–24) insurance premium step change in our alternative estimate of forecast opex for the final decision.

Table 6.6: Insurance premium step change ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	1.7	2.4	2.6	2.5	2.1	11.3
AER alternative estimate	–	–	–	–	–	–
Difference	**–1.7**	**–2.4**	**–2.6**	**–2.5**	**–2.1**	**–11.3**

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.

Our draft decision did not include an insurance premium step change in our alternative estimate of forecast opex, as we considered the insurance premium increases are likely to be captured in the non-labour price growth (CPI) component of the rate of change.[46]

Ausgrid's revised proposal included an $11.3 million ($2023–24) step change for significant increases in insurance premiums over the 2024–29 period.[47] Ausgrid stated the step change is driven by a major external factor outside of its control and does not include forecast growth that is already accounted for in the trend factor.

Ausgrid's revised proposal further stated our draft decision rejected this step change on the basis that the expenditure was not material. Ausgrid considered:[48]

- that there is no basis in the NEL or the NER to apply a materiality threshold to opex step changes

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46 AER, *Draft Decision, Attachment 6 – Operating expenditure – Ausgrid – 2024-29 Distribution revenue proposal,* September 2023, pp. 27–29.

47 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure,* November 2023, p. 26.

48 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure,* November 2023, pp. 24–26.

- the AER is required to make an assessment of total opex and not the individual forecast expenditure components – that is, the cumulative impact of expected changes is the relevant consideration and not the individual components
- the step change is driven by a major external factor outside of its control and does not include forecast growth that is already accounted for in the trend factor
- the efficient costs are not provided by other components of their total forecast opex including base year opex.

Our draft decision, consistent with recent determinations, was not solely based on the expenditure being immaterial as a proportion of total opex. We considered:

- that the costs did not represent a material proportion of opex for which price growth is materially above the non-labour price growth (CPI) included in the rate of change
- for the non-labour price growth (CPI) component of the rate of change, we expect some non-labour components will increase by more than CPI and some by less than CPI
- to the extent insurance premiums rise by more than CPI, we expect this will to an extent be offset by other non-labour costs rising by less than CPI
- there may be circumstances where it is appropriate to consider increasing specific cost categories, particularly where they represent a material proportion of total opex, but this was not the case for Ausgrid's proposed insurance step change.

As stated in our *Expenditure forecast assessment guideline*, our starting position is that only exceptional events are likely to require explicit compensation as step changes.

For the final decision, and consistent with our draft decision, we have not included Ausgrid's proposed $11.3 million ($2023–24) insurance premiums step change in our alternative estimate of forecast opex. We consider this proposed step change to insurance premium costs is likely to be offset by other non-labour costs rising by less than CPI, and therefore captured in the non-labour price (CPI) component of the rate of change.

6.4.3.3 Climate resilience

We have included $3.2 million ($2023–24) for climate resilience in our alternative estimate of opex for the final decision. This is $2.7 million ($2023–24) less than Ausgrid's revised proposal of $5.9 million ($2023–24), and reflects that we are not satisfied that all proposed components of this step change reflect prudent and efficient expenditure.

Table 6.7: Climate resilience step change ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	0.8	1.6	1.2	1.2	1.2	5.9
AER alternative estimate	0.6	0.6	0.6	0.6	0.6	3.2
Difference	**–0.1**	**–0.9**	**–0.5**	**–0.5**	**–0.5**	**–2.7**

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

Ausgrid's initial proposal included $8.4 million ($2023–24) for the implementation of community-based resilience initiatives. After submitting its initial proposal, Ausgrid continued

its consumer engagement on its climate resilience proposal, and subsequently (before our draft decision) submitted a revised climate resilience business case of $5.9 million ($2023–24). We discuss our assessment, and the reasons for not including this step change, in further detail in our draft decision.[49]

Ausgrid's revised proposal included the same total of $5.9 million ($2023–24) for this program but stated that it had responded to the AER's feedback to refine its analysis and continue its consumer engagement with both its customers and broader resilience actors.[50] Following these engagements and in response to consumer concerns, Ausgrid noted that it had also included a new category in its proposal for heat resilience.[51] However, Ausgrid stated that it again tested affordability concerns, and submitted that it had further streamlined work, including market testing, to achieve greater efficiencies in its program.[52] This included providing an overview of the costs it has both absorbed and reduced from its initial proposal.[53] Ausgrid also again submitted that the resilience program was consistent with and required in response to regulatory requirements, most notably to meet obligations under the Security of Critical Infrastructure (SoCI) Act.[54]

We recognise the importance of climate resilience for distribution networks and local communities, and that it is prudent to appropriately plan and effectively respond to the increased risks of related events. We are also conscious of the inherent uncertainty around planning and forecasting in this environment. Therefore, our assessment approach balances these considerations, and places emphasis and weight on both analytical evidence that supports the prudency and efficiency of any proposed programs, as well as on the outcomes of consumer engagement programs. Ultimately, we seek a well thought-through plan with clearly demonstrated net benefits for consumers.

In forming our final decision, we further reviewed the supporting information provided by Ausgrid on its resilience proposal, including Ausgrid's updated resilience business case and information received through information requests. Additionally, our decision had regard to and placed weight on the strong community support Ausgrid has achieved throughout its extensive consumer engagement program.

For the final decision, we have included a lower amount of $3.2 million ($2024–24) for this step change in our alternative estimate of total opex for the final decision. This amount directly relates to the 'community resilience' program component of the proposed step change. We recognise that Ausgrid engaged with the feedback we provided through our draft decision to refine its analysis, and found efficiencies and identified opportunities to streamline and absorb components of this work. We are also satisfied that this proposed program responds to consumer preferences and will result in tangible outcomes to increase community resilience (e.g. delivery of the black-out plan). For these reasons, we are satisfied

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49 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid – 2024–29 Distribution revenue proposal*, September 2023, pp. 36–38.

50 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, pp. 28–29.

51 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, pp. 29–30.

52 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 28.

53 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 30.

54 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 30; Ausgrid, *Revised proposal – Att. 5.5 – Climate Resilience business case*, 30 November 2023, pp. 3 & 7.

that the revised community resilience proposal reasonably reflects prudent and efficient costs.

In terms of the remaining $2.7 million ($2024–24), we are not satisfied based on the information available that these projects will result in meaningful outcomes in relation to building consumer-focused resilience, or that some activities are not already part of business-as-usual operation and therefore already compensated in our opex forecasting approach.

In regard to the new heat resilience category of this step change, as discussed further in relation to the capex component of this expenditure in Attachment 5 of this final decision, we are not satisfied that Ausgrid has provided sufficient evidence to support the prudency and efficiency of this program. It is not clear how, as a network service provider, Ausgrid will utilise the program outputs to benefit consumers and improve consumer resilience. Further, we are also not satisfied that the proposed initiatives address, or are a direct response to, new regulatory obligations placed on Ausgrid to uplift its security requirements. Specifically, Ausgrid has not provided supporting information to demonstrate how these initiatives mitigate material risks in relation to critical infrastructure assets.

In relation to other minor components of the proposed climate resilience step change, such as expenditure on performance monitoring, research and program reviews, we consider such activities to be inherently business-as-usual in nature, and to be part of existing prudent asset management and business practices. We have therefore not included these costs for performance monitoring and reviews in our alternative estimate of the required step change costs. Further discussion on our assessment of Ausgrid's proposed climate resilience expenditure, both opex and capex, is included in Attachment 5 of this final decision.

6.4.3.4 Cyber security

We have included $18.1 million ($2023–24) for cyber security in our alternative estimate of opex for the final decision. This is consistent with Ausgrid's revised proposal, and reflects that we are satisfied that this amount likely reflects a prudent and efficient amount to uplift Ausgrid's cyber security maturity.

Table 6.8: Ausgrid's cyber security step change ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	2.0	3.0	4.0	4.3	4.7	18.1
AER alternative estimate	2.0	3.0	4.0	4.3	4.7	18.1
Difference	–	–	–	–	–	–

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

Ausgrid's initial proposal included $20.6 million ($2023–24) to uplift its cyber security maturity. We discuss this step change, our assessment and the reasons for the inclusion of a lower amount of $19.0 million ($2023–24), in further detail in our draft decision.[55]

For its revised proposal, Ausgrid included a lower amount of $18.1 million ($2023–24), or $0.9 million lower than our draft decision, to uplift its cyber security maturity in the 2024–29 period. Ausgrid stated that although it requires the highest level of cyber protection, it has taken onboard AER feedback to embed productivity improvements to lower its cyber security proposal to achieve this uplift.[56]

For the final decision, we have assessed the information provided by Ausgrid to support its revised proposal, including information received through information requests and Ausgrid's updated cyber security cost-benefit analysis. This included providing supporting information that demonstrated the preferred option associated with this step change had the highest net economic benefit of the options considered in its cyber security analysis. Consistent with our capex decision, we are satisfied Ausgrid's cyber security revised proposal is prudent and efficient. Attachment 5 of our final decision provides further information on our assessment of Ausgrid's revised cyber security proposal for both capex and opex.

6.4.3.5 Smart meter data

We have included $10.2 million ($2023–24) for smart meter data in our alternative estimate of opex for the final decision. This amount is consistent with Ausgrid's revised proposal.[57]

Table 6.9: Ausgrid's smart meter data step change ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	2.8	3.3	1.1	1.4	1.6	10.2
AER alternative estimate	2.8	3.3	1.1	1.4	1.6	10.2
Difference	–	–	–	–	–	–

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

For its initial proposal, Ausgrid proposed $24.9 million ($2023–24) for the acquisition of smart meter data and real-time smart meter functionality to increase its network visibility.[58] We discuss this step change, our assessment and the reasons for including a lower amount of $10.7 million ($2023–24), further in our draft decision.[59]

Ausgrid's revised proposal included $10.2 million ($2023–24) for the smart meter data step change, or $0.5 million lower than our draft decision. Ausgrid stated the revised amount takes into consideration the AER's draft decision, the impact of the Australian Energy Market

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55 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid – 2024–29 Distribution revenue proposal*, September 2023, pp. 29–31.

56 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, pp. 9, 22–23.

57 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 5.

58 Ausgrid, *Att. 6.1 – Proposed operating expenditure*, 31 January 2023, pp. 32–33.

59 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid – 2024–29 Distribution revenue proposal*, September 2023, pp. 33–35.

Commission's (AEMC) metering review final decision on smart meter data purchases, and updated cost estimates it received through further market testing. Additionally, Ausgrid also outlined its data strategy both in the short and longer term, consistent with developments stemming from the AEMC's metering review. It further confirmed that the previously identified benefits will continue to be realised with the revised and lower amount.[60]

For the final decision, we have included Ausgrid's proposed step change of $10.2 million ($2023–24) in our alternative estimate. We are satisfied that this amount likely represents the prudent and efficient investment required to enable Ausgrid the use of the required data streams to increase its network visibility, including the associated benefits of increased safety, reliability and enabling higher volumes of CER on its network.

6.4.3.6 ICT enablement for CER integration

We have included a step change of $6.4 million ($2023–24) for 'ICT enablement for CER integration' in our alternative estimate of opex for the final decision. This is $1.8 million ($2024–24) higher than our draft decision, and reflects that we are satisfied Ausgrid's proposed investment is likely to be prudent and efficient.

Table 6.10: Ausgrid's CER integration step change ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	0.4	1.1	1.6	1.6	1.7	6.4
AER alternative estimate	0.4	1.1	1.6	1.6	1.7	6.4
Difference	–	–	–	–	–	–

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

Ausgrid's initial proposal included $10.4 million ($2023–24) to build foundational capabilities to become a dynamic platform and facilitate the cost-effective transition to net zero by 2050.[61] We discuss this step change, our assessment, and the reasons for our draft decision to include a lower amount of $4.6 million ($2023–24), in greater detail in our draft decision.[62]

For its revised proposal, Ausgrid included $6.4 million ($2023–24) for this step change, or $1.8 million higher than our draft decision, and stated that it accepted our decision on 2 of the 3 components of this step change (modelling and analytics, and connections, compliance and education). Ausgrid further stated that in response to AER feedback, it had updated its modelling and justification for the dynamic services capability component of this step change, which we did not include in our alternative estimate for the draft decision.[63]

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60 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 34.

61 Ausgrid, *Att. 6.1 – Proposed operating expenditure*, 31 January 2023, pp. 35–37; Ausgrid, *Att. 5.7 – CER integration program*, 31 January 2023 p. 4.

62 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid – 2024–29 Distribution revenue proposal*, September 2023, pp. 32–33.

63 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid – 2024–29 Distribution revenue proposal*, September 2023, p. 33; Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 36.

For the final decision, consistent with the capex decision for the dynamic services capability, we consider Ausgrid has satisfactorily demonstrated the updated proposal represents prudent and efficient investment. The dynamic services capabilities, including our assessment of its revised proposal and reasons for our decision, are discussed further in our final decision on forecast capex (Attachment 5 of this final decision).

6.4.3.7 Property strategy

Ausgrid has accepted our draft decision to include a negative step change in forecast opex arising from property sales in the current 2019–24 period that reduce land tax and other costs associated with properties sold. Ausgrid has updated the forecast to account for more recent inflation data.[64] We have included this step change in our alternative estimate of forecast opex for this final decision.

Table 6.11: Ausgrid's property strategy step change ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	–3.1	–3.1	–3.1	–3.1	–3.1	–15.3
AER alternative estimate	–3.1	–3.1	–3.1	–3.1	–3.1	–15.3
Difference	**–**	**–**	**–**	**–**	**–**	**–**

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

6.4.4 Category specific forecasts

While our preferred forecasting approach is to apply the base–step–trend approach described in section 6.3, there are some categories of opex we do not include in our base–step–trend forecast. We include these as category specific forecasts instead. Our reasons for decision regarding Ausgrid's proposed category specific forecasts are outlined below.

6.4.4.1 Network innovation program

Ausgrid's revised proposal included a $4.5 million ($2023–24) category specific forecast for its proposed network innovation program (NIP).[65] We have included a lower forecast in our alternative estimate of total opex for the reasons outlined below.

Table 6.12: Network innovation program category forecast ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	0.9	0.9	0.9	0.9	0.9	4.5
AER alternative estimate	0.3	0.3	0.3	0.3	0.3	1.6
Difference	**–0.6**	**–0.6**	**–0.6**	**–0.6**	**–0.6**	**–2.9**

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Numbers may not add due to rounding.

64 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p 10.

65 Ausgrid, *Revised proposal – Att. 6.1 – Proposed operating expenditure*, 30 November 2023, p. 38.

In its initial proposal, Ausgrid included a step change of $5.0 million ($2023–24) for a NIP, which comprised a range of research and development related to trials and pilots covering energy technologies to support the evolving electricity sector.

We did not include a step change for Ausgrid's NIP in our draft decision. We concluded that Ausgrid had not provided sufficient information to support the prudency and efficiency of the proposed network innovation program.[66]

Ausgrid's revised proposal responded to the AER's feedback at the program and project level. It did this primarily in the capex section of its revised proposal, as that is where the majority of its NIP costs are allocated, with a more modest opex component.

Ausgrid included a lower estimate for its NIP of $4.5 million ($2023–24) in its revised proposal. Ausgrid also changed the treatment of these costs to be a category specific forecast rather than a step change following consultation with AER staff. Ausgrid submitted that as these costs are not forecast on the basis of a single year revealed cost forecasting approach, and are unlikely to be so in future, it is appropriate to treat these as a category specific forecast so they do not automatically become part of recurrent expenditure in future periods. We support this proposed treatment of innovation expenditure allocated to opex.

CCP26 noted in its submission the strong community support behind innovation funding, but also advised that innovation guidance by regulators might be needed to determine if innovation needs are not already being met by other mechanisms or policies.[67] We also received a submission from Ausgrid's Network Innovation Advisory Committee, which strongly endorsed Ausgrid's network innovation program.[68]

Consistent with the capex component of our final decision for Ausgrid (Attachment 5), we have included a portion of Ausgrid's costs for its NIP in our alternative estimate of total opex. Our alternative forecast is for totex of $16.2 million ($2023–24). We note that as Ausgrid's NIP forecast of $49.2 million ($2023–24) was split into capex and opex in a ratio of 90.9/9.1, we have applied the same ratio to the alternative forecast with capex of $14.7 million ($2023–24) and opex of $1.6 million ($2023–24).

Our alternative forecast is based on three adjustments to Ausgrid's total $49.2 million ($2023–24) NIP forecast:

- reducing the volumes in projects that are over-scaled to a level appropriate for a trial or pilot. This involves the scaling back of 12 programs
- removing project that are not innovative. This involves the removal of 7 projects
- removing projects that are not clearly linked to the expenditure objectives. This involves the removal of one project.

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66 AER, *Draft decision, Attachment 6 – Operating expenditure – Ausgrid – 2024–29 Distribution revenue proposal*, September 2023, pp 35–36.

67 Consumer Challenge Panel 26, *Advice to AER – 2024–29 Revised Electricity Determination and Draft Decision – Ausgrid*, January 2024, pp. 11–12.

68 Networks Innovation Advisory Committee, *Submission on Ausgrid's revised proposal and draft decision 2024–29*, January 2024.

The full extent of our analysis and assessment criteria (which we will apply to future network innovation proposals) is in the capex attachment of this final decision (Attachment 5).

6.4.4.2 Debt raising costs

We have included debt raising costs of $46.2 million ($2023–24) in our alternative estimate. We show this in Table 6.13.

Table 6.13: Debt raising costs ($million, 2023–24)

	2024–25	2025–26	2026–27	2027–28	2028–29	Total
Ausgrid's revised proposal	9.2	9.3	9.3	9.3	9.3	46.3
AER final decision	9.2	9.3	9.3	9.2	9.2	46.2
Difference	0.0	0.0	0.0	–0.1	–0.1	–0.1

Source: Ausgrid, *Revised proposal – Att. 6.2 – Opex model,* 30 November 2023; AER analysis.
Note: Number may not add due to rounding; Values of '0.0' and '–0.0' represent small non-zero amounts and '–' represents zero.

Debt raising costs are transaction costs incurred each time a business raises or refinances debt. Our preferred approach is to forecast debt raising costs using a benchmarking approach rather than a service provider's actual costs in a single year. This provides consistency with the forecast of the cost of debt in the rate of return building block. We used our standard approach to forecast debt raising costs, which is discussed further in Attachment 3 to the final decision.

Shortened forms

Term	Definition
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Capex	Capital expenditure
CCP26	Consumer Challenge Panel 26
CER	Consumer energy resources
CPI	Consumer price index
EBSS	Efficiency benefit sharing scheme
IFRSF	International Financial Reporting Standards Foundation
MPFP	Multilateral partial factor productivity
NEL	National Electricity Law
NER	National Energy Rules
NIP	Network innovation program
Opex	Operating expenditure
RBA	Reserve Bank of Australia
RCP	Ausgrid's Regulatory Customer Panel
SaaS	Software as a Service
WPI	Wage price index
2024–29	2024–29 regulatory control period