Summary of meeting

Expenditure Forecast Assessment Guidelines Working Group meeting No. 4

Category assessment – replacement and augmentation capex for distribution businesses

8 March 2013

Held via video link between AER's Melbourne and Sydney offices

On 8 March 2013, the AER, as part of its *Better Regulation* package, hosted a working group meeting on the development of the Expenditure forecast assessment guidelines (the Guidelines). The meeting was chaired by AER Director, Paul Dunn. A full attendee list can be found in Attachment A.

This summary outlines the key topics and themes of the meeting, including views expressed at the meeting, without ascribing particular comments to any one individual or organisation. The outline broadly follows that of the agenda.

1   Introductions

In this workshop, AER staff sought feedback from stakeholders on the information it would require to assess replacement expenditure (repex) and augmentation expenditure (augex).[1] This workshop focuses on the information requirements for distribution network service providers (DNSPs). The AER signalled the potential use of the repex and augex models when assessing DNSPs' capex forecasts.

AER staff highlighted these models are not the only tools it would use to assess repex and augex forecasts, respectively, and would not be used deterministically to set allowances. Rather, they are screening tools that provide the AER an alternative view of capex forecasts, with respect to repex and augex. Ideally, the models would assist the AER in identifying outliers in DNSPs' capex forecasts.

The AER's consultant, Nuttall Consulting, summarised the purpose of the repex model and augex model, emphasising they are regulatory tools, not planning or management tools. Nuttall Consulting

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[1] The AER's 28 February 2013 workshop explored higher level issues such as definitions, drivers and measures, and challenges in assessing repex and augex (for transmission and distribution).

provided example templates in the repex model to illustrate the model's potential information requirements for DNSPs. Nuttall Consulting noted the workshops scheduled for 27 March 2013 will discuss the mechanics of the models in greater detail.

2   Major issues for discussion and feedback from forum

Forum participants discussed issues regarding the repex and augex models and associated information requirements.

General issues with the repex model and its application

Nuttall Consulting noted the AER utilised the repex model in the Victorian and Tasmanian distribution determinations, where DNSPs set their own categories for the specified asset types. However, the AER aims to standardise the repex model categories for future distribution determinations.

DNSP representatives asked how the repex model accounts for differences in operating environments. For example, wood poles deteriorate at different rates in different environments. Nuttall Consulting pointed to the use of "coastal poles" and "inland poles" to account for such environmental differences in the Victorian distribution determination. Nuttall Consulting noted the purpose of the workshop was in part to discuss the most appropriate cost categories in order to account for such differences in operating environment.

DNSP representatives asked how the AER would account for the fact that DNSPs record information at different levels of detail. DNSP representatives also noted some of the data required to populate the repex and augex models are not available and will need to be derived. Nuttall Consulting noted this is not a major issue as long as the derivation is clear and well-documented.

AER staff noted energy users representatives previously requested data for the repex and augex models be made available during a revenue determination. This would enable independent assessment by energy users.[2] DNSP representatives raised concerns energy users will take the outputs of the repex and augex models as deterministic. Therefore, the AER should clearly qualify the results of these models. Further, DNSPs should have the opportunity to explain outputs of the repex model. Ideally the AER's models would be populated with data and outputs made known to DNSPs prior to the submission of their regulatory proposals.

DNSP representatives pointed out the repex model currently produces point forecasts, and queried whether it should produce a range instead.

It was noted that the NSW DNSPs have been investigating the augex model, and agreed to share their findings with other stakeholders for the purposes of model development.

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[2] AER, *Summary of meeting: Expenditure forecast assessment guidelines working group meeting no. 3*, 7 March 2013.

Cost categories in the repex model

AER staff asked whether the repex model in its current form has any important omissions from the broad asset groups in DNSPs' replacement programs.

DNSP representatives noted the repex model does not include metering assets. This is an important point in Victoria as meters in the AMI program will be rolled into the next Victorian distribution determinations. DNSP representatives also noted secondary systems, and SCADA and protection are not currently asset categories assessed in the repex model. AER staff noted it would need to document any omissions from the repex model and the reasons for such omissions.

DNSP representatives stated the repex model requires a better definition of "unit rate" because a replacement activity (such as "pole replacement") may represent a number of distinct activities (for example, replace a cross-arm versus replace the pole itself). The definitions need to make clear what direct and indirect costs are to be included/excluded. A consultant noted aggregation of such unit costs averages out such differentials, and that the AER should therefore focus its investigation where more aggregated unit cost differentials are material.

A DNSP representative noted obtaining more disaggregated information will be harder for smaller networks as statistical indicators become harder to derive. Concerns were also expressed at the AER potentially identifying differences in disaggregated unit costs and making adjustments to expenditure allowances on this basis without a proper consideration of efficiency at the aggregated level.

Inconsistency in the number/ type of asset categories in the AER's templates for historical data versus forecast data was noted. Rather than focus on achieving consistency in categories across businesses, it was suggested that the AER also consider the potential role of normalisation adjustments to deal with unit rate variances.

AER staff proposed to create a draft proposal of asset categories for the purpose of populating the repex model and more generally to enable the AER to assess DNSPs' repex forecasts. This would be provided to stakeholders after 15 March 2013.

General issues with the augex model and its application

DNSP representatives noted the augex model does not account for the fact that there are a range of possible solutions for network segments reaching utilisation thresholds. Nuttall Consulting conceded the augex model is more limited than the repex model for assessing expenditure forecasts. However, the augex model still provides a point of comparison to assessing augex forecasts and having consistent data is in itself useful in a distribution determination.

DNSP representatives noted the augex model aims to capture demand driven augmentations. However, many augmentation projects relate to other drivers such as customer connections, quality and voltage issues. More generally, DNSP representatives asked when in the Guidelines consultation

process will the AER discuss the scope the augex model's utilisation. In this context it was noted that there was some ambiguity in the AER's issues paper and the augex model material regarding whether the model was intended to cover connections capex.

AER staff stated they would consider clarifying the areas the augex model will apply to (and those it will not).

A DNSP representative inquired whether the augex model uses raw demand data, or weather-corrected data. AER staff stated this is currently under consideration and noted the Australian Energy Market Operator's potential role in demand forecasting.

Cost categories in the augex model

Nuttall Consulting asked whether low voltage (LV) augmentations are material enough to be reviewed separately, or whether they should be linked with distribution substation augmentations. DNSP representatives suggested LV works are normally related to customer complaints regarding voltage, and the issue may not be one of materiality but of the need to rely heavily on assumptions to compensate for a lack of quality data. No modelling was currently undertaken by DNSPs at the LV level.

DNSP representatives noted subtransmission augex consists of a small number of large projects. Hence, the augex model may not be appropriate for such expenditure. Nuttall Consulting queried whether classifying circuits by type (short rural, long rural, urban, CBD) was appropriate for the augex model. DNSP representatives discussed these categories may be used, for example under licence conditions reporting, however expressed some reservations as to whether they were consistently applied in all jurisdictions. Such classification may relate more to reliability standards reporting and may not fully reflect underlying cost drivers. No preferably alternatives were discussed.

AER staff suggested they would create a draft proposal of asset categories for the purpose of populating the augex model and more generally to enable the AER to assess DNSPs' augex forecasts. The AER will provide the draft proposal to stakeholders after 15 March 2013.

3   Other matters

Forum participants will need to monitor whether reliability standards and categorisations will become nationalised under the Australian Energy Market Commission's review.

AER staff reflected on concerned expressed about the potential for modelling data e.g. age and capacity utilisation to be published in annual benchmarking reports without proper context. DNSPs were asked to consider what other meaningful information could be collected and reported alongside these data to provide a more accurate view of their relative efficiency.

Attachment A: Attendee list

Melbourne office

Name	Organisation
Renate Tirpcou	CitiPower & Powercor
David Dawson	Strategic Economics Consulting Group
Matthew Abraham	United Energy & Multi Gas
Nicola Roscoe	Energex
Peter Wong	Jemena
Eric Lindner	SA Power Networks
Katie Yates	SP AusNet
Brian Nuttall	Nuttall Consulting
Paul Dunn	AER
Esmond Smith	AER
Matthew Simpson	AER
Israel del Mundo	AER
Max Hooper	AER
Anthony Hynes	AER

Sydney office

Name	Organisation
Terry Holmes	Essential Energy
Ed King	Ausgrid
Rick Wallace	Endeavour Energy
Lawrence Irlam	AER