

12 September 2014

Mr Warwick Anderson  
General Manager  
Network Regulation Branch  
Australian Energy Regulator  
GPO Box 3131  
Canberra ACT 2601

Dear Mr Anderson

**CCP submission on ActewAGL Distribution Regulatory Proposal 2014-19**

Thank you for the opportunity to respond to the Consumer Challenge Panel's (CCP) August 2014 submission to the AER on ActewAGL Distribution's regulatory proposal.

ActewAGL Distribution would firstly like to address comments made by the CCP in relation to the finding that ActewAGL Distribution's consumer engagement has been ineffective.<sup>1</sup>

As stated in its subsequent regulatory proposal (SRP), ActewAGL Distribution has developed a consumer engagement framework which reflects the principles contained in the AER's consumer engagement guidelines. The framework sets out our existing engagement activities, and includes a plan for making recent initiatives and further enhancements become business-as-usual processes. ActewAGL Distribution is committed to continuing and strengthening its consumer engagement activities going forward, and plans to continually monitor these activities to ensure that they are transparent and open to all consumers. Section 3 of ActewAGL Distribution's regulatory proposal sets out in detail our current consumer focus, consumer engagements activities for the 2014-19 determination process and planned activities for the 2014-19 period.

ActewAGL Distribution appreciates that the CCP has recognised that ActewAGL has been active in conducting willingness to pay studies into network service attributes for over a decade and that "an important part of the toolkit for consumer engagement is the use of survey techniques to gauge the relative preferences of consumers between alternative program and expenditure options."<sup>2</sup> This is the approach that ActewAGL Distribution has continued to apply since its first substantive choice modelling work in 2003.

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<sup>1</sup> CCP submission, p.6

<sup>2</sup> Ibid, p.6

ActewAGL Distribution self-initiated and implemented its rigorous and defensible customer survey work over a decade ago. The initial 2003 study was deemed noteworthy for a number of reasons including that “the study sends a clear message that ActewAGL is committed to its customers and seeks service solutions that are commensurate with the needs of customers”<sup>3</sup>. Furthermore, “by identifying what customers prefer and are willing to pay for...avoids any outcome that has ignored the customer base”<sup>4</sup>.

As a result ActewAGL Distribution has been at the forefront of WTP research within the utilities sector, utilising world-leading authorities in the application of choice modelling techniques to the valuation of utilities services quality. The survey approach applied by ActewAGL Distribution “simulates a market situation allowing researchers to gather information on the most preferred aspects of the service, and also the relative value consumers place on an incremental change in each aspect of the service”<sup>5</sup>. The results have been used extensively and referenced in a number of academic journals. For this reason, it is disappointing that in regard to ActewAGL Distribution’s WTP survey information, the CCP “recognise some value in the WTP work undertaken but are cautious about drawing solid conclusions.”<sup>6</sup> Instead the CCP refer the AER to “anecdotal evidence and the views of some consumer organisations”<sup>7</sup> to try and undermine the rigorous and professional nature of ActewAGL’s study approach and findings. The CCP also selectively refer the AER to a WTP study of customers in the UK where the results from this study would apparently better fit with the beliefs of the CCP on how ACT customers should assess the price/reliability trade-off, as though this international study is more relevant and reliable in expressing the views of an ACT customer than the actual preferences revealed in local WTP studies by an ACT customer.

ActewAGL Distribution is also very concerned by some of the CCP’s related comments that appear to question the validity of the results obtained from the surveys undertaken in 2003, 2009 and 2012. Despite the quality of these studies, the CCP advise there is a “lack of adequate evidence” to support ActewAGL Distribution’s statements on the views of its customers on price and service reliability and price/quality trade-off. Yet the 2003 choice modelling survey conducted by ActewAGL Distribution was not only in itself a world first study, it was a “substantial empirical study using state-of-the-art (and practice) methods to establish the preferences of customers”<sup>8</sup>. The lead researcher was a renowned and respected world leader in the development and implementation of the analytical and design methods used in the study. The follow up 2012 study refreshed aspects of the broader and more intensive 2003 study and confirmed the continued relevance of those findings.

These periodic WTP studies have been amongst the most important consumer engagement initiatives undertaken by ActewAGL Distribution. The studies are complex and require substantial organisational commitment. The studies use targeted focus groups and choice

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<sup>3</sup> Professor David Hensher, University of Sydney, 2003, p.6

<sup>4</sup> Ibid, p.6

<sup>5</sup> Ibid,p.2

<sup>6</sup> CCP submission, p.7

<sup>7</sup> Ibid, p.7

<sup>8</sup> Professor David Hensher, University of Sydney, 2003, p.6



modelling techniques to obtain meaningful information on customer preferences in relation to striking a balance between cost and levels of service. The interaction with customers that has taken place as part of this research has enabled ActewAGL Distribution to gain a deep and considered understanding of customer preferences, attitudes and views.

Importantly, the results of these studies continue to influence investment and operation decision making within ActewAGL Distribution, and have informed the expenditure proposals contained in our 2014-19 regulatory proposal. Projects are prioritised, and investment decisions are made on the basis of having knowledge of customer preferences about a whole range of issues including price, service levels, planned outage notification periods and undergrounding. While ActewAGL Distribution intends to further develop its approach to customer engagement, the evidence from the work on these studies alone completely refutes the conclusion by the CCP that ActewAGL Distribution's approach to consumer engagement to date has been ineffective.

ActewAGL Distribution notes the CCP view that "WTP information in and of itself is insufficient to support activities of network businesses"<sup>9</sup> and that a network business should also identify the "need for program expenditure and.....how the costs of the program are outweighed by the benefits."<sup>10</sup> This remains a core feature of the willingness to pay approach adopted by ActewAGL Distribution as the utility must seek to provide the greatest benefits to customers and in doing so "consider the costs associated with alternative ways of satisfying the needs of customers."<sup>11</sup> ActewAGL Distribution also acknowledges the need to "consult further with the customer base as it evaluates ways of delivering what is best for customers"<sup>12</sup>.

ActewAGL Distribution's expenditure forecasts in the 2014-19 regulatory proposal meet the opex and capex criteria contained in the National Electricity Rules. ActewAGL Distribution's internal governance, asset management and planning processes ensure the production of expenditure forecasts that are both prudent and efficient. Moreover, ActewAGL Distribution has provided the AER with economic justification and supporting information in respect of capital expenditure projects that demonstrate the forecasts are consistent with minimising the long run cost of achieving the expenditure objectives.

In relation to customer engagement, ActewAGL Distribution also notes some of the consumer engagement 'stretch questions' listed on pages 7 and 8 of the CCP's submission in relation to the ACT. In particular, they appear to extend beyond the scope of questions raised by the AER in its issues paper, and do not capture ActewAGL Distribution's planned initiative to roll-out stage two of its consumer engagement strategy over the 2014-19 regulatory period.

The CCP submission also raises concerns for ActewAGL Distribution in relation to the accuracy and relevance of other comments. For example, the CCP comments that ActewAGL Distribution has not taken account of 'the new reality' of declining demand and the impacts of new technology such as rooftop solar systems. However, these matters are being addressed as part of

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<sup>9</sup> CCP submission, p.7

<sup>10</sup> Ibid p.7

<sup>11</sup> Professor David Hensher, University of Sydney, 2003, p.7

<sup>12</sup> Ibid, p.7

ActewAGL Distribution's ongoing network tariff strategy, as discussed in chapter 13 of the SRP. In addition, as explained in chapter 6 of the SRP, a key step in the network augmentation process is the annual planning review in which ActewAGL Distribution forecasts peak demand and energy growth for a ten year period.

In its operating expenditure section, the CCP, in relation to vegetation management, states that "little effort is made by the distribution businesses to explain this large expenditure"<sup>13</sup>. ActewAGL Distribution has provided substantive evidence to support its vegetation expenditure. ActewAGL Distribution noted in its SRP that vegetation costs are "forecast using a zero based approach, however these costs are largely recurrent in nature, with adjustments being made for changes in contractual arrangements"<sup>14</sup>. To support the SRP, ActewAGL Distribution also provided the main contract for the trimming and removal of vegetation away from ActewAGL Distribution's network facilities<sup>15</sup>, historical vegetation inspection compliance audits<sup>16</sup> and detailed historical and network characteristics by urban and rural zones in the reset Regulatory Information Notice (RIN) regulatory templates<sup>17</sup>.

The CCP in relation to benchmarking states that it is "of the view that there remains fat in the proposed operating and capital expenditure"<sup>18</sup>. ActewAGL Distribution rejects this statement. In chapter 6 of the SRP, ActewAGL Distribution sets out its network planning and asset management which provide the framework for ensuring that the regulatory obligations and customer requirements are met in the most prudent and efficient way. Chapter 8 and 9 discuss the operating and capital expenditure forecasting methodologies and how these incorporate the systems used by ActewAGL Distribution to generate efficient expenditure levels.

In its submission the CCP also states many of its views in relation to the weighted average cost of capital that ActewAGL Distribution would contest, including that "lower rates of return would adequately recompense shareholders, who have enjoyed ...undue levels of profitability over recent regulatory periods"<sup>19</sup>. As discussed in chapter 10 of the SRP, ActewAGL Distribution notes that its proposed rate of return is supported by expert advice in relation to each of its components to ensure that it is commensurate with the efficient financing costs of a benchmark efficient entity and, hence, in the long term interest of customers.

Please contact David Graham, Director Regulatory Affairs and Pricing, on 6248 3605 should you have any queries in relation to this submission.

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<sup>13</sup> Ibid, p19

<sup>14</sup> ActewAGL Distribution, 2015-19 Subsequent regulatory control period, July 2014, p.237

<sup>15</sup> Attachment A2 Appendix 1-4 Contracts and supporting documentation

<sup>16</sup> Attachment A2 Appendix 2 Compliance audits of vegetation management work

<sup>17</sup> Attachment A3 Regulatory reset (5 year) RIN report template – Consolidated information, sheet 2.7  
vegetation management

<sup>18</sup> CCP submission, p.21

<sup>19</sup> CCP submission, p.10

Yours sincerely

A handwritten signature in black ink, appearing to read "Stephen Devlin". The signature is written in a cursive style with a prominent initial 'S'.

Stephen Devlin  
General Manager Asset Management