AUSNET SERVICES EDPR 2022-26

Energy Users Association of Australia

AER Public Forum Presentation – 20 April 2020

SUMMARY

EUAA
Energy Users Association of Australia

- This presentation makes some preliminary comments on the AusNet Services EDPR for 2022-26
- We come to it with the NEO objective central to our considerations
- As the AER highlights in its Issues Paper, there is the unknown impact of COVID-19 factors on the proposal and we:
  - appreciate the flexibility the AER has provided to allow discussion of the proposal and how it might change over time, and
  - acknowledge that AusNet Services will wish to change information provided esp. what would flow from lower demand growth forecasts
- The EDPR proposal provides a clear pathway for significant improvement across a range of measures to help AusNet move away from being one of the least efficient DNSPs with a relatively poor customer service record to one that
  - hopefully moves up the absolute and relative productivity league table,
  - lays the basis for lower prices in the longer term with the reduction in RAB, and
  - embeds a major cultural change in its customer relations

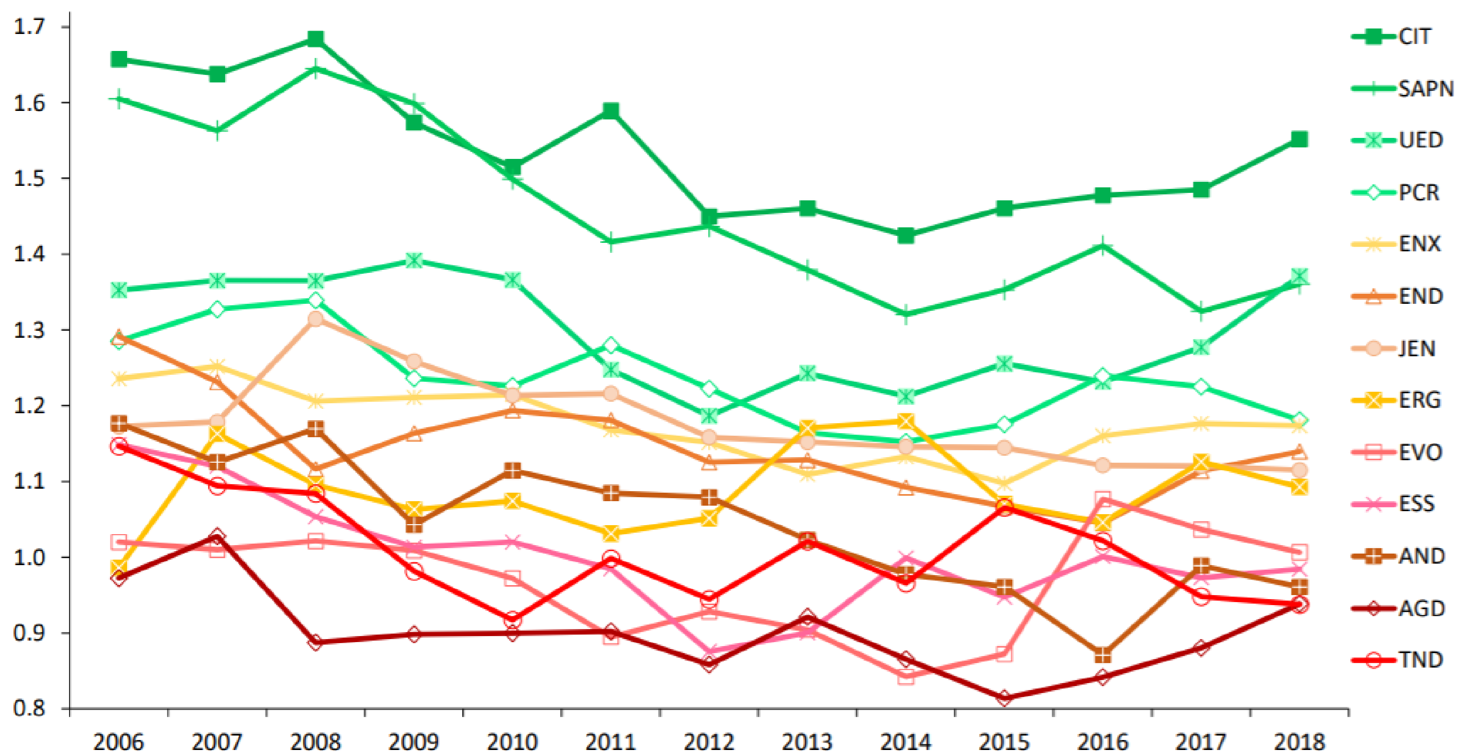
SUMMARY

- The Customer Forum has:
  - brought a significant and welcome improvement in AusNet's consumer engagement and we look forward to that being sustained as part of BAU activities into the future
  - achieved some notable outcomes in its negotiations
- Like all other networks, changes in external factors around WACC and tax allowance have provided a lot of headspace to perhaps lessen the focus on efficiency improvements and introduce some accelerated depreciation, while still providing price falls
  - this potentially sets up a risk of rising prices in the future (despite falling RAB) when the interest rate cycle changes
- While the improvements are very welcome, questions include "Can AusNet do even more?" and "How does this proposal lay the basis for similar improvements in the next regulatory period?"
  - given other networks are also improving, it remains to be seen how much AusNet's relative position improves
- Surprising to see that 18% of the pages submitted in the proposal are subject to a claim of confidentiality vs an average of 6% for the other four networks

CONTEXT

- The most recent AER benchmarking data shows that AusNet is in the bottom quartile for overall MTFP dropping from 10th in 2017 to 11th in 2018; its productivity for 2012-18 fell on average 2% per year, the worst of any DNSP
- It is in the bottom quartile for capex and second bottom for opex

Figure 4.2 MTFP indexes by individual DNSP, 2006–18



CONTEXT

EUAA
Energy Users Association of Australia

- So it was surprising to see in the Proposal (Part III p. 129)

  "The AER's 2019 benchmarking report confirms that we are a reasonably efficient DNSP."

- We note AusNet, like many DNSPs, argue that there are particular circumstances (e.g. treatment of bushfire risk) that distort the AER results
  - but, as the Customer Forum argues (p.16), the AER data is the only evidence consumers have

Question

- How does AusNet see its trend total/capex/opex productivity and performance against its peers trending if the AER accepts its 2022-26 proposal as currently presented?

CONSUMER ENGAGEMENT

- Customer Forum has been a major facilitator of improved AusNet CE
  - e.g. customer relationship managers for larger customers
- Negotiated outcome achieved a number of welcome outcomes
  - the level of revenue involved in the negotiation is relatively small e.g. negotiating the opex base year does not mean that it was negotiating all of opex
- Quality engagement/deep dives in the first half of 2019
- EUAA would have appreciated much more engagement with the CF as the negotiation process proceeded
  - we only had two meetings with the Forum - April 2018 and August 2018 - well before the negotiations began
  - Meetings were more ‘consult’ with no ‘collaboration’ on the IAP2 spectrum
- Given the expenditure by AusNet/AER/ECA on the CF we look forward to seeing the cost benefit analysis

<u>Question</u>

- What form will consumer engagement take from now on given the Customer Forum is finished?

ROLE OF THE AER

- The Issues Paper asks (p.29) for our views, given:
  - the CF process (and the AER's input to it), and
  - the AER's initial analysis that concludes AusNet's proposed opex and capex "…compares well to their peers, historical allowances and historical expenditure levels"

  whether the AER would conduct less extensive assessment of the components of capex and opex than would be the case in the absence of New Reg
- We need further information to express a view:
  - the EUAA had no engagement with the Customer Forum as it developed and then implemented its negotiation strategy so we look to the AER to assess the efficiency of the negotiated outcome no differently that what it would do had AusNet followed a different engagement model
  - there were a number of matters that were not agreed between the CF and AusNet e.g. opex base year, REFCL step change

ROLE OF THE AER

EUAA
Energy Users Association of Australia

- We are told that the counterfactual for assessing New Reg is what AusNet would have done in the absence of New Reg
  - so the AER will need to examine how it would have assessed an AusNet proposal if it were under a different consumer engagement model
- So presumably the AER will have to examine the proposal to answer questions like “Would the AER have come to a different decision in the counterfactual consumer engagement model than what was agreed as part of the Consumer Forum negotiation process?”

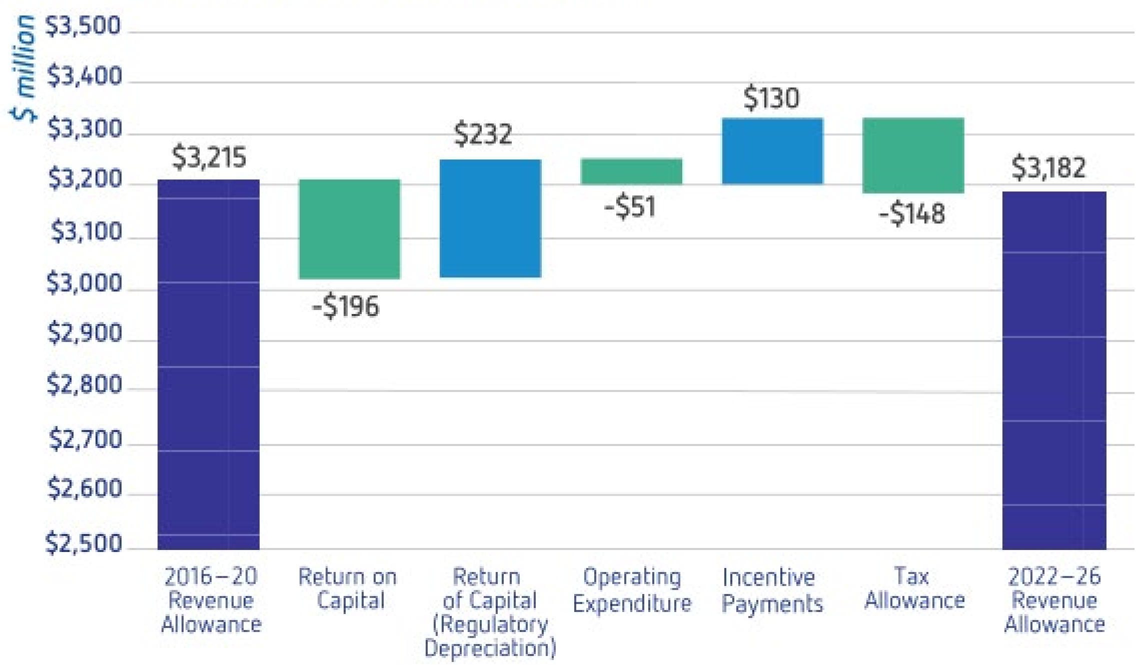
<u>Questions</u>

- Can the AER confirm which particular matters that it proposes to bring less scrutiny to? Are these only the matters where there was agreement between the CF and AusNet or does it include all matters that were in the AER/CF agreed scope or the wider AusNet Services/CF agreed scope?
- Can the AER provide an example of how this reduced scrutiny might apply in practice?

REVENUE BUILDING BLOCKS

- Rather than total revenue decreasing 1% in 2022-26, it would have increased by 8% without the external influences of lower WACC and tax allowances

Figure 5: Changes in the revenue building blocks ($2021)

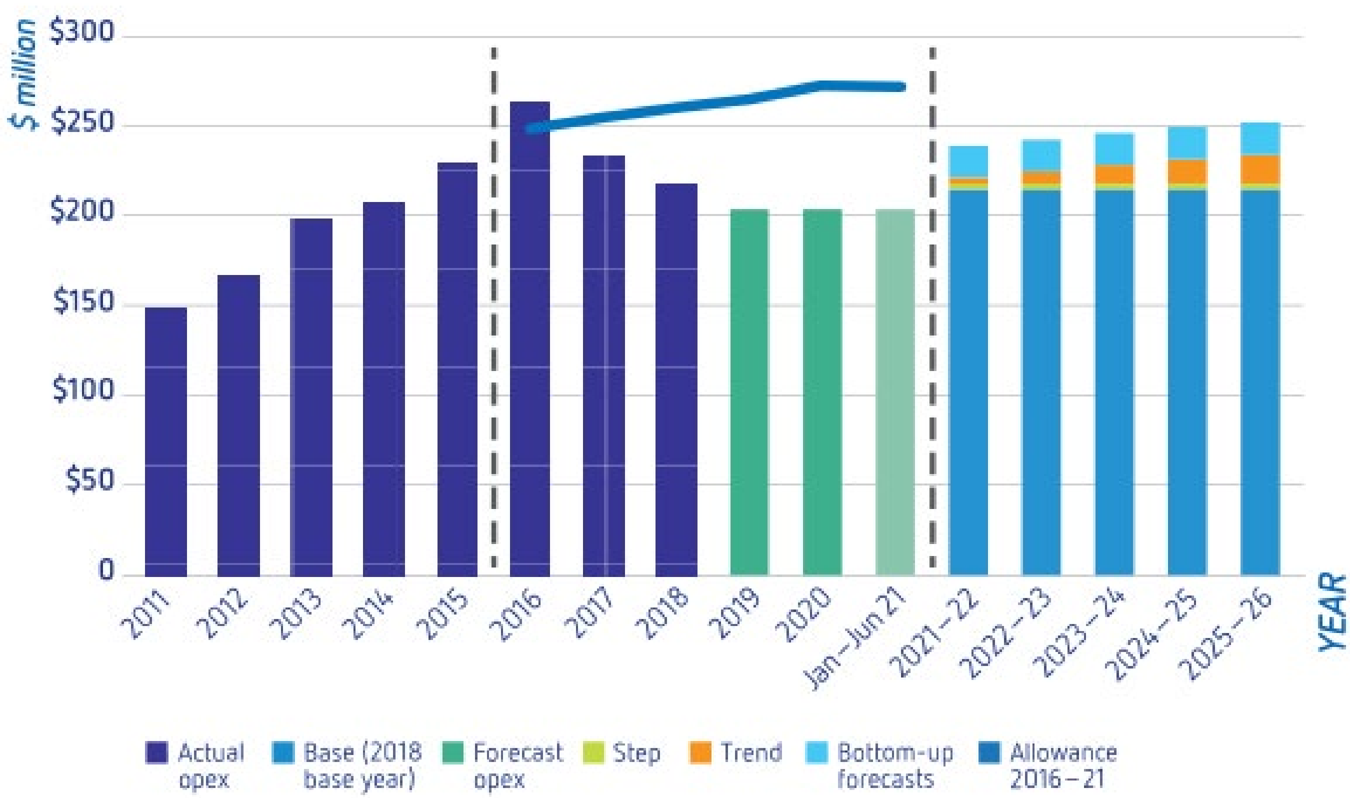


<u>Question</u> – what would have been the average price changes for non-residential without WACC and tax alliance changes – to compare with the $430 or 9% quoted

OPEX

- We welcome the significant improvement in opex in the current period, the agreement to the 1% productivity improvement and additional $21m in absorbed costs in 2021-26

Figure 6: Actual and forecast operating expenditure ($2021)



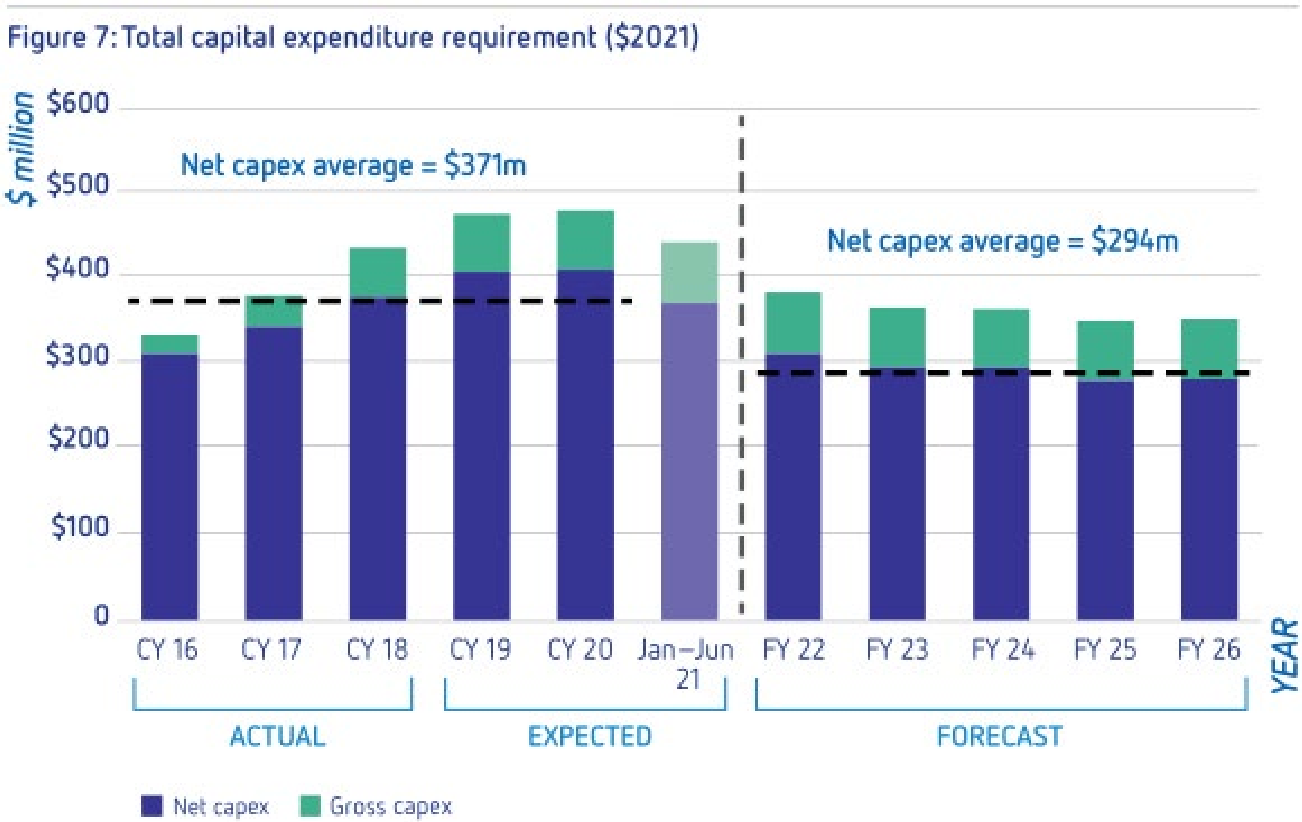
OPEX, EBSS AND EFFICIENCY

EUAA
Energy Users Association of Australia

- Substantial reduction in current period opex relative to the AER allowance will result in a very large ($91m – or > 5 months opex in 2020) EBSS carryover
- Was the AER was too generous in its current period allowance?
- We share the CF's concern about the proposed 2018 Base Year and look forward to the AER analysis around the selection of the base year and whether it is 'not materially inefficient'
- The debate around the measure of base year efficiency is around the level of efficiency that should go 100% to consumers and what should be shared 70/30
  - the large reduction in actual opex suggests there should have been an efficiency adjustment before the EBSS applied in the current period
- AusNet agrees there is further scope in the next period given their agreement with the CF for a 1% productivity improvement, above the mandated 0.5%
- We await the AER's analysis of the remaining step changes and labour cost trends – we support the use of just the Deloitte forecasts rather than the average of the Deloitte and BIS Oxford forecasts
  - and expect revised labour cost forecasts – who is going to get a real wage increase in the next 5 years?

CAPEX

- The 20% decline in net capex is also welcome e.g. work of the CF in negotiating augmentation capex reductions
  - though it is unclear how much of this decline is due to the end of the REFCLs program



CAPEX

- Reflects more subdued customer and peak demand growth
- Completion of safety related capex
- Look forward to AER closely examining DER capex – initial analysis suggests the approach to understanding and optimising DER export capacity (hosting capacity and voltage compliance) is prudent and efficient
- Significant CESS carryover – how much efficiency, how much just not required?

Questions

- What is the capex trend (% reduction over 21-26) excluding REFCLs?
- What analysis has been done by AusNet and the AER to show the extensive expenditure on mitigating bushfire risk (capex and opex) has been successful in reducing risk?

DEPRECIATION

- In common with other networks, AusNet is proposing a change to asset lives that effectively accelerates depreciation with increased depreciation a major factor (+$232m) in increased 2021-26 revenues
- There is a significant reduction in remaining asset lives for:
  - IED protection relays (30-35 yrs. down to 5-6 yrs.) - + $139m, and
  - remote terminal units (30 yrs. down to 3-4 yrs.) - + $22m
- While there may be a case for shorter lives, we:
  - look to the AER to review the case for such a large reduction in asset lives
  - question why the impact is concentrated in 2021-26 rather than spread out over more than one revenue reset - it seems the WACC and tax falls have given headroom to increase depreciation at the same time as offering a price fall

TARIFFS

EUAA
Energy Users Association of Australia

- We need comfort that business tariffs are indeed cost reflective and do not involve cross subsidies to other consumer groups
- As solar PV expands, the benefits to all consumers in lower pool price reduces to provide less justification for cross-subsidies
- We look to retailers to pass on these cost reflective tariffs

Question

- What evidence can AusNet provide to give our members comfort that their tariffs are not cross subsidising the Victorian Government roll out of rooftop solar for residential customers?

THANKYOU

www.euaa.com.au