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Seed Advisory

Deep Dive Workshop One – Summary Report

AusNet Services Electricity Distribution Price Review
2021 – 2025

10 April 2019



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Disclaimer

This report is only a summary of key items discussed at the deep dive workshop held on 11 February 2019.

The information in this report is not necessarily reflective of the views of each attendee at the workshop, AusNet Services or Seed Advisory.



1. Introduction

1.1. Background

AusNet Services owns and operates a regulated electricity distribution network delivering electricity to more than 720,000 customers in Melbourne's north, east and across all of eastern Victoria.

Regulated electricity network businesses must periodically (typically every five years) submit a Regulatory Proposal which outline their plans and proposed expenditure to the Australian Energy Regulator (AER) for assessment. AusNet Services is currently developing its 2021 – 2025 Regulatory Proposal. On 12 February 2019 AusNet Services released its draft Regulatory Proposal.

As part of developing its Regulatory Proposal, AusNet Services is undertaking an extensive customer engagement program. One component of this engagement program is a series of 'deep dive' workshops with attendees including customer representatives, consumer advocates, AER representatives, consumer challenge panel representatives and other stakeholders.

These workshops were designed to:

- share detailed information;
- consult on and enable open and frank discussion of AusNet Services draft Regulatory Proposal and plans with attendees; and
- enable AusNet Services to consider the feedback and views of attendees while developing its plans and respond accordingly.

AusNet Services engaged Seed Advisory to assist in the preparation and facilitation of these workshops and to develop a summary report for each workshop.

At the time of publishing this report, AusNet Services are planning on holding, or will have held the following workshops:

- Workshop 1: Overview of the draft Regulatory Proposal, customer experience, operating expenses and innovation;
- Workshop 2: Public Lighting;
- Workshop 3: Replacement Capital Expenditure; and
- Workshop 4: Innovation and Distributed Energy Resources.

1.2. Purpose of this report

This report summarises the key items of discussion from Workshop 1 which was held on 11 February 2019 in Melbourne. The names and organisations represented of the attendees of this workshop are included in Appendix A and the complete agenda for the workshop is included in Appendix B.

In brief, the workshop agenda covered four broad areas:

- An overview of the overall draft Regulatory Proposal;
- A discussion on customer experience in particular specific initiatives agreed with AusNet Services Customer Forum and the proposed customer satisfaction incentive scheme;
- A discussion on the operating expenditure component of the draft proposal including specific discussion on information technology related expenditure; and



- A discussion on innovation related expenditure.

It is important to note that the information in this report is not necessarily reflective of the views of each attendee at the workshop, AusNet Services or Seed Advisory. This report is only a summary of key items discussed at the workshop. The workshop was held under Chatham House rules, so no comments from attendees have been attributed to any one attendee. AusNet Services responses or comments in relation to matters raised by attendees has been noted as such.

1.3. Other related documents

This report should be read in conjunction with three key documents which are co-located on the same page of the AusNet Services website that contains this report. The documents will provide important information and context when reading this report, the documents are:

- Pre-reading materials developed by AusNet Services for the relevant workshop – this document contains background and other information provided to workshop attendees to prepare them for their workshop attendance;
- Presentation materials developed by AusNet Services for the relevant workshop – this document contains the material presented at the workshop; and
- AusNet Services draft Regulatory Proposal for the 2021 – 2025 period – this document contains the actual draft Regulatory Proposal published by AusNet Services on 12 February 2019.



2. Key discussion items

This section contains the key items discussed at the workshop and broadly follows the flow of the agenda. AusNet Services responses or perspectives provided either during or post the workshop are included where relevant and required in the shaded boxes.

2.1. Overall Proposal

The discussion on the overall draft Regulatory Proposal covered three main areas which are outlined below.

2.1.1. Overall revenue reductions

There was acknowledgement by attendees of the \$38 average revenue reduction per customer in the current draft Regulatory Proposal. However, there were a number of observations and questions in this regard:

- Some attendees considered that the average revenue reduction may not be adequate. Attendees were interested in understanding how much of the average revenue reduction was due to the change in the methodology for the Weighted Average Cost of Capital (WACC) versus general expenditure reductions?

After the workshop AusNet has advised that 43% of the real price reduction presented in the draft Regulatory Proposal is due to forecast reductions in expenditure, the remainder is due to the WACC parameters.

AusNet Services also noted that further substantial revenue reductions associated with the AER's tax and productivity adjustment are yet to be included in the Regulatory Proposal and are therefore not included in the average price reduction of \$38 per customer.

- A question was raised whether any specific tariff assumptions were made in the development of the draft Regulatory Proposal?

No specific assumption on tariff design has been included in the draft Regulatory Proposal. It was noted that tariff design is being considered in a parallel process in conjunction with the other Victorian electricity networks.

- The differences between residential and business customers was noted. In particular in relation to their desired level of reliability, management of outages and the balance between affordability and reliability.

2.1.2. Balancing affordability and reliability

There was discussion of the need to balance affordability and reliability. Some queried how AusNet Services made this balance with no real increase in average revenue in the draft Regulatory Proposal.



In developing the draft Regulatory Proposal, AusNet Services maintained current reliability levels without any specific reduction in levels of service.

It was also noted by some attendees that many large (and even some small) businesses invest in their own assets (usually behind the meter) to provide additional reliability rather than necessarily receiving this via the network business. This is in contrast to residential customers who largely rely on the network to provide the required level of reliability.

In this regard some commented that large businesses may not be supportive of the inclusion of high impact low probability events in the AER's review of the Value of Customer Reliability.

2.1.3. Views on the Customer Forum process to date

There was general acknowledgement of the level of effort invested by AusNet Services, the AER and the Customer Forum as part of the development of the draft Regulatory Proposal and the strong interest by many in the sector of the outcomes of this process.

Some attendees did question the overall benefit of this process versus other processes, but others noted that there is likely to be great value created through, and as part of the Customer Forum process.

2.2. Customer Experience

The discussion on the customer experience covered an overview by AusNet Services of specific customer experience improvement initiatives and the proposed customer satisfaction incentive scheme. The discussion also covered an overview of AusNet Services proposal to undertake ongoing customer research, There was discussion with workshop attendees of their views of current issues with customer experience and better meeting customer needs.

2.2.1. Current issues with customer experience

A number of areas were raised about issues in relation to customer experience, most notably these included:

- Paying for energy bills and energy affordability more broadly.
- Information provision, in particular:
 - Receiving timely and accurate outage related information – both planned, unplanned and any special communications required during heatwaves.
 - Transparency of costs on customer's bills – some raised the merit of unbundling the network charge on the bill to improve transparency.
 - Provision of information and education to customers on how to interpret and utilise the meter and other data provided by network businesses. Noting that many customers are not actually interested in the data itself just the desired outcome (e.g. a better energy deal)
 - Understanding the appropriate channel to provide this information such as working with retailers to provide peak demand information on the bill.
- Reliability issues for some consumers, including issues with easily contacting AusNet Services directly when there are outages. One attendee raised a question on how



will AusNet Services help cover any costs associated with outages for customers (for example if the food in the fridge or freezer needs replacing post an outage).

- Improved planned outage management including the timing of outages – such as higher density business areas on the weekends and higher density residential areas during the week. This would also try to maintain power to businesses that may be important to local communities.
- Better use of technology to minimise outages such as voltage management – AusNet Services was seen as a poorer performer compared to other Victorian electricity networks in this regard.
- AusNet Services must ensure that the customer experience work programs align with priority customer needs rather than just what AusNet Services can fix. This includes potentially involving customers in ‘co-designing’ any new processes.
- More clearly demonstrate efficiencies achieved with smart meters
- Better address communications gaps and customer engagement with non-English speaking customers.
- The importance of utilising existing customer data in any research program, for example complaints, customer satisfaction metrics and metering data.

The issues raised were noted and will be considered in the development of the customer experience and broader work program.

It was also noted that some of the comments raised are currently in progress or have been implemented by the business including voltage management, better addressing communication with non-English speaking customers and the GoodGrid program (demand management to improve reliability).

2.2.2. Customer Satisfaction Incentive Scheme

AusNet Services discussed their proposed customer satisfaction incentive scheme and the broad approach / methodology underpinning the scheme.

There was general support for the concept of a customer satisfaction related incentive scheme as well as an acknowledgement that the current metric and scheme based on answering the telephone within certain timeframes does not reflect customer satisfaction even if this should be retained.

There were some comments in relation to the details of the scheme and metrics such as:

- AusNet Services may want to consider increasing the complaints value up to \$1m and reduce unplanned outages down to \$0.5m. However, some noted this may skew the data and outcome due to the complaints.
- It was unclear why AusNet Services capped the scheme at 0.5% of revenue instead of 1% of revenue?
- Are business customers (e.g. those with large solar PV systems >30kW) appropriately reflected in the metrics?
- What stops AusNet Services ‘de-prioritising’ non-measured customer experience pain points to meet requirements of the proposed parameters?
- Further information and transparency will need to be provided to validate the results and ensure it is appropriate (if the scheme is approved and operational).



- Should “do not disconnect” (including life support) customers be a specific focus and segment within the scheme? Some noted that there are already measures and incentives in place to appropriately deal with such customers.
- Could a single high-level customer satisfaction measure be included in the scheme?

The issues raised were noted and will be considered in the further development of the proposed scheme. AusNet Services is not proposing to increase the size of the scheme, its size will be maintained at 0.5% of revenue

AusNet Services will ensure appropriate publication of the measures, assumptions, data quality and other details to ensure transparency and accuracy in reporting.

2.3. Operating Expenditure

The discussion on the operating expenditure covered:

- an overview by AusNet Services of the operating expenditure component in the draft Regulatory Proposal including key assumptions such as materials / labour growth rates and productivity adjustments.
- a discussion on the choice of base year in the calculation of operating expenditure
- a discussion of the step changes in particular Information Technology (IT) cloud related expenditure.

2.3.1. Overview of operating expenditure

There was discussion of the overall operating expenditure and the base, step and trend elements of the operating expenditure proposal. This section covers the overall operating expenditure and the trend parameters in particular the labour growth and productivity assumptions. The base year and step changes are separately covered in the next two subsections.

Stakeholders commented that the draft Regulatory Proposal included a forecast operating expenditure of \$1,229m and that this was approximately 5 per cent below the approved allowance for 2016-20 but also higher than the (forecast) actual operating expenditure in 2016-20.



For the 2021 to 2025 period the required total opex will be \$1,229 million (real \$2020).

This forecast amount is 5% or \$59 million (real \$2020) below the total opex allowance for the 2016 to 2020 period. These cost reductions have been delivered through a companywide 'cost-out' program which was implemented in 2017 and is expected to continue delivering savings at least through to 2019.

AusNet Services have selected 2018 as the base year, primarily because 2018 is the most recent regulatory year for which audited regulatory accounts and other financial information is available.

The selection of a 2019 base year should (presuming forecast savings are achieved) result in a greater reduction in our proposed opex allowance. However, the operation of the EBSS would then result in a corresponding larger reward and ensures that the total revenue is unaffected by the choice of base year. The apparent increase in the opex allowance above actuals is a presentation issue, arising from the selection of the 2018 base year.

The discussion of the labour growth assumption noted that the use of two consultants (one appointed by the AER and one from AusNet Services) is consistent with the traditional approach and that taking the average tends to smooth out what is a usually higher business assumption than that of the AER.

Some questioned how the labour growth assumption can be at its current assumed level given we are in a low wage growth environment. Others noted that there appears to be an inconsistency between the materials and labour growth assumptions, materials are zero whilst labour growth is non-zero, when labour costs are expected to impact future material costs.

The assumption of no extra allowance for materials growth was chosen because there is currently no clear evidence of above CPI increases in materials prices, whereas labour growth is forecast to be above CPI.

There was a view shared by many that the productivity growth assumption should not be less than 1% and that AusNet Services should not wait for the AER to determine the assumption before including this assumption in their Regulatory Proposal.

Some questioned the difference between movement of the efficient frontier/ versus on catch up to the efficient frontier and that this difference is important given it will impact the allocation of productivity between AusNet Services and consumers (i.e. 70% versus 100% of the productivity growth).

AusNet Services noted the position and is adopting the AER's productivity decision in the Regulatory Proposal.

There was a brief discussion on capitalised leases and in particular how they change or are reflected in the Regulated Asset Base (RAB).



AusNet Services commented that the current assumption impacts the RAB by approximately \$40m over 7 years, but that the final impact and NPV neutrality does depend on the WACC assumption.

2.3.2. Base year

There was general indifference between the choice of 2018 or 2019 as the base year. There was also a comment that this is a technical matter and therefore best considered by the AER. There was some acknowledgement that 2018 is likely to be a better choice of base year due to the availability of audited accounts. However ultimately attendees expressed the view that the final decision is best left to the AER.

There was also a question raised regarding how a business can achieve significant operating expenditure reductions from an efficient base year and also that the AER should review the 0.75 threshold for determining if the base operating costs are not materially inefficient.

AusNet Services commented that the current assumption impacts the RAB by approximately \$40m over 7 years, but that the final impact and NPV neutrality does depend on the WACC assumption.

2.3.3. Step changes

There was discussion on the key step changes assumed by AusNet Services in their draft Regulatory Proposal. Many attendees were seeking more information and insights into the breakdown of these costs to evaluate the proposed changes.

For example, there was discussion on the need for further information regarding the 5-minute settlement related step change and whether there was any double counting of this step change and others related to information technology expenditure.

AusNet Services noted the desire for more detailed information and this will be included in the final Regulatory Proposal.

There was an acknowledgement of the need for the Rapid Earth Fault Current Limiter (REFCL) step change, however some questioned if it was already in the base year assumption and the relationship if any with insurance costs.

AusNet Services commented that the operating costs for REFCL were not included in the base year.

Some attendees noted that AusNet Services should absorb the security related step change given its (lack of) materiality.

Similarly, some also questioned if the EPA step change could be absorbed, its actual level of materiality given many of the processes would be in place already. It was also discussed that other networks (Ausgrid for example) absorbed some environmental costs as it considered it could effectively manage the risk.



AusNet Services noted these views and comments.

There was discussion on the customer relationship management (cloud-based system) related expenditure and attendees again noted that further information was required to assist in better understanding the costs and benefits of the proposed change.

For example, there should be analysis covering 'do nothing', a capital (on-premises) solution and the cloud-based option. It must be demonstrated that the step changes provide an attractive value proposition to the bottom line and meets customer's needs. Some questioned how the benefits of this system for customers will be measured.

Some attendees also noted that like for any IT system that the data quality and the maintenance of good quality data is critical for the system to be effective. Some noted the potential need to incentivise staff to keep the data in the system up to date and to ensure they use it during all client interactions.

In this regard some attendees questioned how many interactions does an average customer (or segment) have with AusNet Services on an annual level? This information would help assess any business case or proposal.

Others also questioned if there are any case studies for similar systems in other network businesses.

The need for further information to assist stakeholders was noted and will be actioned and included in any final Regulatory Proposal.

AusNet Services also commented that they believe other Victorian electricity networks (Citipower and Jemena) may have customer relationship management systems and will discuss what information can be provided in this regard.

2.4. Innovation

The discussion on innovation covered the broad energy market context, the possible future (changing) customer needs, the high-level innovation program and the capabilities and innovation required for AusNet Services to move to a dynamically managed network in the future.

It was noted that the energy industry is undergoing a major structural change and is currently in transition and that it is important to consider future customer needs when developing innovation plans. In other words, it was acknowledged there is a need for more customer-focused innovation. Ausgrid was cited as having an example of a 'use it or lose it' innovation program with customers involved in overseeing the program.

Attendees first questioned whether AusNet Services (and other networks) already spend their existing allowance on innovation through the Demand Management Innovation Allowance (DMIA) and whether or not a broader allowance was a better approach than a specific set of initiatives.

This discussion also included considering whether other existing incentive regimes already provide incentives for innovation such as the regimes for opex, capex, reliability, fire starts and the new customer satisfaction incentive scheme.



It was also noted that the AER would seek to ensure there is no double counting with existing or proposed incentive schemes and an appropriate funding mechanism for innovation.

AusNet Services commented that they have a good track record on spending their innovation allowance under the DMIA.

In addition the timeframes and scope of existing incentive schemes do not provide incentives for regulated networks to undertake strategic innovation.

There was discussion on the perceived lack of adequate collaboration across the electricity networks in relation to innovation through knowledge sharing and avoided duplication of effort. It was suggested that this would necessarily lead to inefficiencies and higher costs for consumers.

AusNet Services commented that there is significant collaboration and knowledge sharing amongst the electricity networks and that they (and other network businesses) need to do a better job in explaining this and providing sufficient evidence of the collaboration.

Some commented or questioned why AusNet Services and other networks don't fund their own internal innovation and take on more risk in this regard. Especially if it is primarily done to improve operating efficiencies and doesn't present a clear customer benefit.

Similarly, some attendees noted the potential issue with current customers funding the innovation related change and capability development that will only deliver benefits in the longer term for potentially other customers. Related to this some expressed concern that the benefits of innovation will vest in networks or with engaged customers, rather than with the majority of customers. This was particularly noted in the current environment of energy affordability related issues.

There was also a discussion on whether or not innovation can be incrementally developed (or in a modular way) so that benefits can accrue over time. This also included possibly using milestones and forming innovation efforts as a project with incremental benefits realised by customers.

AusNet Services is proposing an incremental and modest innovation program, the concept and models of risk sharing can be considered. The innovation program is designed to achieve better outcomes for all customers, further information including case study examples will be provided.

The need for customer input across a broad spectrum of customers is noted as well as the need to consider longer vs shorter term costs and benefits.



A. Workshop attendees

Name	Organisation
Shelley Ashe	Energy Consumers Australia
Leigh Clemow	Department of Economic Development, Jobs, Transport and Resources (Victorian Government)
Mark Grenning	Energy Users Association of Australia
David Headberry (by phone)	Major Energy Users
Mark Henley	Consumer Challenge Panel
Andrew Ley	Australian Energy Regulator
Emma O'Neill	Victorian Council of Social Services
Evan Orun	Australian Energy Regulator
Robyn Robinson	Consumer Challenge Panel
Zoe Pilven	Department of Environment, Land, Water and Planning (Victorian Government)
Helen Bartley	AusNet Services Customer Forum
Greg Camm	AusNet Services Customer Forum
John Mumford	AusNet Services Customer Forum
Di Rule	AusNet Services Customer Forum
Tony Robinson	AusNet Services Customer Forum
Peter Caccaviello	AusNet Services
Charlotte Eddy	AusNet Services
Catherine Gip	AusNet Services
Penny Gray	AusNet Services
Tom Hallam	AusNet Services
Justin Harding	AusNet Services
Stephanie Judd	AusNet Services
Michael Larkin	AusNet Services
Alistair Parker	AusNet Services
Deirdre Rose	AusNet Services
Tom Strawhorn	Seed Advisory
Peter Eben	Seed Advisory

**B. Workshop Agenda**

Deep Dive 1: Monday 11 Feb Agenda

9.30 – 9.45am: Welcome: Tom Hallam, General Manager, Regulation

9.45 – 10.00am: Brief overview of the Deep Dive and the Draft Proposal

10.00 – 10.30am: Opportunity for initial/general feedback from participants

10.30 – 10.45am: Morning tea

10.45am – 12.45pm: Customer experience deep dive

10.45 – 10.55: Overview of overall customer experience proposal

10.55 – 11.15: Feedback on overall customer experience proposal

11.15 – 11.25: Presentation to support discussion of deep dive customer experience initiatives

11.25 – 12.05: Roundtable discussion of deep dive customer experience initiatives

12.05 – 12.15: Presentation to support discussion of customer satisfaction incentive scheme

12.15 – 12.45: Roundtable discussion of customer satisfaction incentive scheme

12.45 – 1.15pm: Lunch break (lunch provided)

1.15 – 3.15pm: Opex deep dive

1.15 – 1.25: Overview of opex proposal

1.25 – 1.55: Feedback on overall opex proposal

1.55 – 2.05: Presentation to support discussion of base year

2.05 – 2.35: Roundtable discussion of base year

2.35 – 2.45: Presentation to support discussion of IT Cloud opex

2.45 – 3.15: Roundtable discussion of IT Cloud opex

3.15 – 3.25pm: Short break

3.25 – 4.35pm: Innovation deep dive

3.25 – 3.35: Overview of innovation proposal

3.35 – 4.35: Roundtable discussion of innovation proposal

4.35 – 4.45: Close and final discussion

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