



Revised Proposal Attachment 5.05 Capital Expenditure Decision-making Framework

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Table of contents

1	INTRODUCTION	3
2	DECISION-MAKING FRAMEWORK	4
2.1	Overview	4
2.2	Elements of framework	4
2.3	Ausgrid Board	5
2.4	Regulatory Reset Executive Committee	5
2.5	Investment Governance Committee	6
2.6	Network Asset Management System	6
3	DECISION MAKING FOR CAPEX FORECAST	7
3.1	Risk management framework	7
3.2	Safety obligations	7
4	OUR REVISED FORECAST CAPEX IS PRUDENT AND EFFICIENT	9

1 Introduction

The purpose of this document is to provide information about Ausgrid's governance and decision-making process for the revised capital expenditure (capex) proposal for the 2019-24 regulatory period.

In particular, the information provided demonstrates that:

1. We have understood and responded to the matters raised by the Australian Energy Regulator (AER) in its Draft Decision and by our customers through our engagement process; and
2. The improvements we have introduced to our governance and decision-making processes provide strong assurance that our total capex forecast is prudent and efficient in accordance with the requirements of the National Electricity Rules (NER).

This document forms part of our revised Regulatory Proposal (Revised Proposal), which is submitted to the AER, in accordance with the NER. It should be read in conjunction with Chapter 5 of the Revised Proposal and other supporting documentation that are referenced where appropriate. Additional supporting documents have been prepared in relation to our network and non-network capex forecasts, and also form part of our Revised Proposal.

2 Decision-making framework

2.1 Overview

Good governance delivers good decisions. It provides confidence that the right level of strategic guidance, risk management, review, challenge and testing is occurring in a business. We have enhanced our internal review, challenge and decision-making processes to forecast our capex requirements.

Ausgrid maintains an Investment Governance Framework to provide clear guidance and accountability for the planning, development, endorsement and approval of network and non-network investments. The Investment Governance Framework consists of policies, procedures and standards that cover how Ausgrid plans and invests in network and non-network assets.

The business-as-usual governance framework was enhanced to ensure that our Revised Proposal:

- fully addressed the needs of our customers, including by taking specific account of the feedback received on our Initial Proposal, and
- maintained a consistent strategic approach across Ausgrid.

The governance and decision-making framework for the capex forecasts is discussed below.

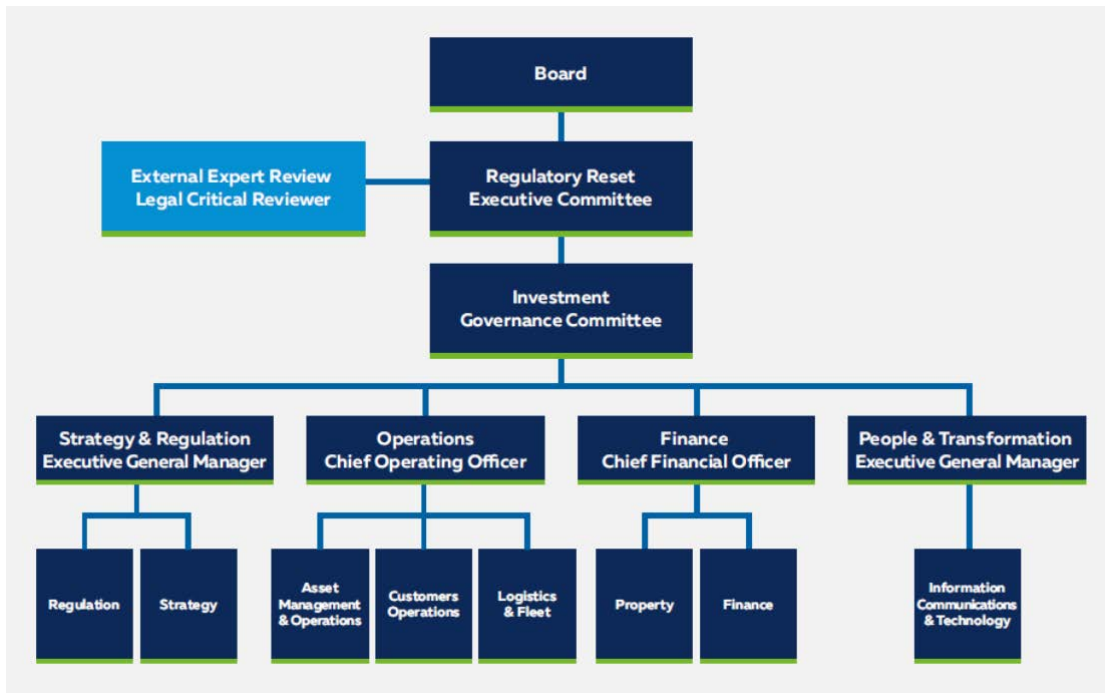
2.2 Elements of framework

In summary, the key changes to the way our forecasts are prepared include:

- Enhanced role of the Reset Regulatory Executive Committee (RREC)
- Enhanced role of the Investment Governance Committee (IGC)
- Update of Ausgrid's Risk Management Framework
- Network Asset Management System certified to ISO 55001:2014 Asset Management System - Requirements

Our revised governance and decision-making framework for capex forecasts is shown in Figure 1 below.

Figure 1: Decision-making framework for revised capex forecast



2.3 Ausgrid Board

The Board has provided oversight and guidance on the strategic direction, risk management, review and challenge and final approval for the Revised Proposal.

Ausgrid's Board set a strategic direction that drove the business to ensure the Revised Proposals delivered against the current energy industry challenges and addressed feedback provided by stakeholders. In particular, the strategic direction is to:

'connect communities and empower lives with a focus on providing services that are reliable, affordable and sustainable.

To achieve affordability, a guiding principle for our capex forecast was to target no growth in the value of the regulatory asset based (RAB) per customer.

2.4 Regulatory Reset Executive Committee

The Regulatory Reset Executive Committee (RREC) was established to support the delivery of a compliant, credible and reasonable regulatory proposal that aligned with the strategic direction set by the Board and Ausgrid's corporate objectives. The RREC reports to the Ausgrid Board.

Following the publication of the AER's Draft Decision, the RREC charter was amended. This was to formalise the RREC's review and challenge role; strengthen the requirement to consider feedback from stakeholder consultation; and specify that it was to take into account the long-term interests of consumers in its deliberations.

The role of the RREC as set out in the charter includes:

- Provide strategic direction for the 1924 Reset project and oversight of Ausgrid's response to specific strategic regulatory issues contained in the AER's draft determination
- Monitor project progress against deliverables and timeframes
- Monitor key project risks and provide strategic advice on actions to mitigate risks
- Monitor regulatory developments for implications on Ausgrid's response to the draft regulatory determination
- Provide a forum to review, discuss, challenge and resolve key strategic issues relating to the AER's 2019-24 determination from the perspective of the long-term interests of consumers

- Provide a forum to discuss and resolve key issues raised by stakeholders during consultations, as appropriate
- Identify options and recommendations for Board approval for issues that fall outside the Regulatory Reset Executive Committee charter or cannot be resolved by the Committee
- Review and endorse the revised proposal, plain English overview paper and revised tariff structure statement, for approval by the Board
- Review and endorse key assumptions and forecasts within the proposal for verification by the Board, as required under the NER.

The RREC charter provides additional assurance that the revised capex forecasts comply with the NER and can be approved by the AER.

2.5 Investment Governance Committee

Prior to being considered by the RREC, the revised capex forecasts were subject to review and challenge by the Investment Governance Committee (IGC). The IGC, typically used to review and challenge projects prior to their funding and commencement, was tasked with the role of challenging and verifying that forecasts are fully substantiated before proceeding to the RREC.

A General Manager with accountability for each expenditure category is also required to review and challenge the forecast capex before it is subject to review by the IGC.

The five-year plans and forecasts for network and non-network projects and programs were submitted to the IGC for review. The IGC performed an important role in ensuring that our revised capex forecasts are prudent and efficient in accordance with the NER requirements.

The IGC's role includes:

- verifying that our revised forecasts are consistent with our regulatory obligations;
- ensuring that consistent investment evaluation principles are applied across our capital expenditure categories; and
- applying a portfolio-wide project and program review so that synergies are captured and reflected in our revised total capex forecasts.

Our revised capex forecasts were initially submitted to IGC for review and challenge on 7 November 2018. Following a detailed review, the IGC requested further changes to the capex forecasts. A further review was conducted by the IGC on 5 December 2018 before the updated revised forecasts were submitted to the RREC.

The papers and minutes from the IGC meetings are available to the AER upon request.

2.6 Network Asset Management System

In September 2018, Ausgrid's asset management system was certified to ISO 55001 Asset Management System – Requirements. The ISO55001 certification meets a licence requirement under Ausgrid's NSW Distribution Licence Conditions. The certification of our asset management system reinforced the appropriateness of our core beliefs and asset management practices for an electricity network business.

Achieving the ISO55001 certification demonstrates that Ausgrid's asset management processes are in line with best practice asset management. It provides assurance that the asset management processes and data analytics that underpin the development of our network capex forecasts are reasonable.

Further information about the Network Asset Management System is presented in Attachments 5.01 and 5.13.

3 Decision making for capex forecast

3.1 Risk management framework

Our revised capex forecasts have been developed in accordance with our Risk Management Framework, which was approved by the Board in May 2018. Our risk framework and the risk management cycle are consistent with ISO 31000:2018.

The key elements of our Risk Management Framework are summarised in Figure 2 below.

Figure 2: Ausgrid's Risk Management Framework



Good risk management is an essential aspect of determining prudent and efficient capex forecasts that comply with the NER. The Board, RREC and IGC require that our five-year capex forecasts reflect a consistent application of the approved Risk Management Framework.

3.2 Safety obligations

Since March 2015, Ausgrid has been required to comply with the NSW Electricity Supply (Safety and Network Management) Regulation 2014 as one of our licence conditions, with licence condition compliance forming a significant component of our long term lease conditions.

This regulation requires us to have a comprehensive electricity network safety management system (ENSMS) which addresses the risks associated with our network. Amongst other things, it requires us to 'as far as is reasonably practicable' (SFAIRP), take steps to operate and maintain the network to ensure integrity of the assets at all times.

This requirement is routinely audited, with results and actions externally monitored by the Independent Pricing and Regulatory Tribunal (IPART). IPART has the power to direct actions and to make recommendations regarding suspension or removal of our licence if necessary.

Ausgrid's management and Board take this obligation very seriously in relation to considerations of risk appetite. Safety is therefore a key driver in developing our revised capex forecasts.

4 Our revised forecast capex is prudent and efficient

The improvements we have introduced to our governance and decision-making processes provide strong assurance that our total capex forecast is prudent and efficient in accordance with the requirements of the NER. In particular, we have strengthened the review and challenge process by enhancing the roles of the RREC and IGC to ensure that:

- The objectives of the business in approving capital expenditure are fully aligned with the requirements of the NER
- Customer feedback is given full consideration in our review, challenge and approval process.

In addition to governance, the following improvements have been made to the development of our capex forecasts:

- Our risk management framework has been reviewed to ensure that risk is subject to an economic assessment
- Our network asset management system is certified to ISO55001 standard, which provides confidence that our asset management processes are consistent with good industry practice.

In aggregate, these initiatives have significantly improved our approach to capex forecasting and played an essential role in ensuring that the resulting forecasts are prudent and efficient.

Further information that demonstrates the prudence and efficiency of our network and non-network capex forecasts is provided in Chapter 5 of our Revised Proposal, Attachments 5.01 and other supporting material.