5 July 2017

Mr Sebastian Roberts
General Manager
Australian Energy Regulator
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Business SA
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Working for your business.
Working for South Australia

Dear Mr Roberts

I write in response to the AER's request for submissions on ElectraNet's 2019-23 Revenue Proposal. I would also like to acknowledge Andrew McKenna has represented Business SA's views during the consultation process through ElectraNet's Consumer Advisory Panel.

Executive Summary

- Business SA welcomes a drop in electricity transmission prices which are forecast to fall by 10% in 2019, largely driven by a 39% decrease in ElectraNet's capital expenditure program and a forecast decline in 'rate of return' from the existing 7.5% to 6.02%, both combining for an average annual $28 saving on small business electricity bills and $14 on residential bills.
- Business SA acknowledges that businesses have had to absorb significant increases in electricity prices over the past decade, until relatively recently primarily driven by rising network costs, and all of ElectraNet's future spending proposals need to be considered in the context of past investments and impacts on its regulatory asset base which directly impacts two thirds of revenues.
- Business SA acknowledges ElectraNet for being open with key stakeholders with respect to future spending plans. While ElectraNet and its customers may have some competing priorities, we have much more to gain from South Australia's future prosperity underpinned by reliable and affordable electricity.
- South Australia continues to hold the mantel of having the nation's highest unemployment rate, 6.9%, and any AER decision to allow real labour cost increases, the largest driver of Electranet's nominal operating expenditure increases, needs to be predicated on the actual labour demand/supply situation, most recently judged by the Essential Services Commission of South Australia in its decision on SA Water's 2016-20 regulatory business proposal.

Should you require any further information or have questions, please contact
Andrew McKenna, Senior Policy Adviser, on (08) 8300 0000 or andrewm@business-sa.com.

Yours sincerely,

Anthony Penney
Executive Director, Industry and Government Engagement

Why this matter is important to South Australian businesses

As South Australia's Chamber of Commerce and Industry, Business SA is the peak business membership organisation in the State. Our members are affected by this matter in the following ways:

- The increase in electricity prices, particularly over the last two years, has had a devastating impact on South Australian business at a time when the State's economy is attempting to transition with the pending closure of Holden's manufacturing operations in October.

- South Australia has the highest proportion of non-firm renewable generation in the National Electricity Market (NEM) and the exit path of Alinta's Northern Power Station which began in mid-2015 has put significant pressure on South Australia's wholesale electricity market, effectively leaving two key players to hedge the base-load electricity needs of industry meaning large market customers, which consume as little as 160MW hours per annum, have experienced peak energy cost increases from seven cents per KWh to as high as 22 cents today.

- South Australia's small market customers, which include most small businesses, have also been caught up in the energy crisis and although the impacts have been delayed due to nature of annual price reviews, last year bill increases were approximately 10% on average, depending on the retailer, and small businesses have been hit again this year with circa 20% bill increases effective from 1 July 2017.

- Up until mid-2015 when South Australia's wholesale electricity prices began to rise dramatically, network costs had been the primary driver of the significant increases in electricity costs over the past decade and South Australian businesses cannot afford to return to the spending patterns associated with that period which have been compounded through rising regulated asset bases.

- South Australia's blackout on 28th September 2016 crystalised the importance of reliability to business, costing at least $450 million[1], and it is important that ElectraNet, along with generators and Governments, take reasonable steps at appropriate costs to mitigate impacts of similar events in future.

Key Policy Points

1. As at 1 January 2003, ElectraNet's regulated asset base (RAB) stood at $824 million. By 2008, this had grown to $1.27 billion and by 2013, $2.09 billion. ElectraNet's current RAB is $2.55 billion rising to $2.67 billion by 2022/23 which we acknowledge is now rising at a rate slower than inflation, meaning no real growth.

   Business SA recognises that total electricity demand in South Australia was growing for much of the decade up until the Global Financial Crisis (GFC) but that it has actually fallen 9.61% since 2010[2] while maximum demand has also declined in recent years, offset by the rising contribution of solar PV, and is forecast to decline a further 9.3% over the period 2019-23.

   Electranet has taken a welcome step of assuming output growth of 0%, against an output change averaging 0.44% using weightings from the AER's consultant benchmarking analysis. Nonetheless it remains important for the AER to carefully consider all future spending proposals by ElectraNet in light of its current RAB value which will determine two thirds of its combined $1.74 billion in revenues for the 2019-23 regulatory proposal.

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[1] Business SA, adjusted cost following additional public company results since Blackout Survey Results report, http://business-sa.com

[2] Business SA calculations from AEMO historical data, http://aemo.com.au/Electricity/National-Electricity-Market-NEM/Data-dashboard#aggregated-data

2. Business SA has volunteered its time to be represented on both ElectraNet's recently established Consumer Advisory Panel and its sub-panel working group which aim to solicit feedback from consumers throughout the revenue determination process.

   We acknowledge that the early engagement process has been a learning exercise for both sides and ElectraNet have shown a genuine degree of openness with consumer representatives which has helped to instil a sense of confidence in the processes behind construction of its 2019-23 revenue proposal.

   Although the early engagement process should not be viewed as forming individual or collective agreement from stakeholders in relation to ElectraNet's proposal, Business SA has found the process helpful in enabling consumer groups to become more informed, in turn facilitating constructive engagement on key issues.

3. The Essential Services Commission of South Australia (ESCOSA) recently determined SA Water's revenues for the period 2016-20, a significant component of which related to labour costs. Considering all utility infrastructure companies employ a substantial number of technicians and engineers, Business SA expects drivers for SA Water's labour costs to be quite comparable to those experienced by ElectraNet and we acknowledge the following comments from ESCOSA in reaching its decision on SA Water's labour costs:

   'In doing so, it (ESCOSA) has reached the view that the base rate of increase in the cost of labour – which is an input to the calculation of SA Water's total labour costs – should be capped by the rate of change in the Australia wide Consumer Price Index (CPI). SA Water had proposed a base rate of change at half a percentage point above the CPI. However, given current evidence and economic circumstances in this State, the Commission is not persuaded that a higher base rate of change is prudent and efficient.'

   Furthermore, ESCOSA stated '*SA Water did not propose any real labour cost escalation for its contracted delivery costs, suggesting that labour can be maintained within CPI for these externally delivered costs.'*

   Business SA acknowledges that the independent cost escalations in the Aquenta report[3] have been redacted and in the interests of transparency and understanding how those escalations in section F may relate more broadly to assumed real labour cost increases, the largest driver of ElectraNet's nominal operating expenditure increases, Business SA requests this point be addressed. We also note that this entire piece of supporting material is heavily redacted which seems inconsistent with transparency across the regulatory proposal more broadly.

   Real labour cost increases will impact both future operating and capital expenditure costs for ElectraNet and it is critical that any increases allowed by the AER are carefully considered to ensure they are in the long term interests of consumers, particularly considering broader electricity price increases experienced by South Australian consumers in recent years.

[3] Aquenta, independent cost review report for range of capital expenditure proposals, 12 December 2016

4. Business SA recognises that ElectraNet will adopt rate of return parameters in line with recent AER determinations and subsequent court rulings. This is a welcome step forward and should largely avoid unnecessary expenditure by both ElectraNet, the AER and consumer groups on expert consultants contesting cost of capital models.

   On this point, we would expect ElectraNet will now adopt the AER's determination of 0.4 for the calculation of gamma, not the 0.25 chosen in its revenue proposal, following the recent Federal Court decision on NSW based energy network businesses.

5. Business SA supports ElectraNet's endeavours to improve reliability on the Eyre Peninsula, not only to Port Lincoln but also to northern customers situated within the State's largest single grain growing region which is mostly exported. The blackout events highlighted the vulnerability of Pt Lincoln customers which were particularly exposed given businesses expected the regional city's backup generator to provide support in the event of a network failure.