PWC - AER Draft Decision 2019-24 Predetermination Conference

Consumer Challenge Panel
29 October 2018

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Objectives of CCP

- We advise the AER on whether:
  - the network businesses' proposals are in the long-term interests of consumers, and
  - effectiveness of network businesses' engagement activities with their customers – who, how, when and what issues PWC engaged with its customers on, how this engagement has influenced the revenue proposal, do consumers agree with the revenue proposal, and is there a process for ongoing review of CE/continuous improvement

- We consider this role in the context of the National Electricity Objective (NEO)
- First time PWC has gone through AER reset process and had its consumer engagement assessed

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AER is guided by the NEO

NEO: “to promote efficient **investment** in, and efficient **operation** and use of, energy services for the **long term interests of consumers** of energy with respect to **price, quality, safety, reliability and security** of supply of energy.”

Therefore, we consider:

– How prudent and efficient is proposed capex/opex expenditure?
– How will costs be allocated to different consumer groups?
– How does the proposal reflect the changing electricity market and long-term issues?

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Discussion Today

- CCP's response to AER's draft decision
- Observations regarding PWC's consumer engagement
- Encouraging submissions to draft decision and Revised Proposal

First time for PWC

- Transition from Utilities Commission to AER regulation
- Concurrent significant change to bring NT into national regulatory framework
- Small, geographically and climatically diverse network – but not unique (Ergon/Essential)
- Immense amount of work required eg accounts in order, planning systems in place, filling out RiNs, answering AER and CCP questions
- Encourage consumer engagement when it is in its infancy
- Interaction with Government's 50% renewables target by 2030 – impact on grid demand?

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Overall perspectives

- Impressed with the level of consumer engagement from a very limited base:
  - no ECA funding to support developing consumer capability
  - >99% of customers covered by the Pricing Order (<750MWh/yr)
  - Comprehensive engagement with large consumers - given they are the ones most impacted by the reset
- Suggestions for the future:
  - need to build BAU consumer engagement
  - develop a Draft Plan next time
- But still some way to go to move from a traditional engineering driven publicly owned utility to one more responsive to ensuring lowest costs to consumers eg asset management, demand response
- We support the Draft Decision and look forward to seeing PWC's revised proposal
  - excellent engagement with Customer Council on AER draft decision
- Transition will be tough in 2019-24 esp with opex

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CCP scope in the AER "building blocks"

In scope	Out of scope
Proposed capex in period	Rate of return – currently under review
Proposed opex in period	Opex productivity – about to be reviewed
Application of incentive schemes	Taxation allowance – currently under review
Tariff Structure Statement	Regulatory depreciation
Consumer engagement	
~35% of total revenue over 2019-24	~65% of total revenue over 2019-24

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Change in total revenue dominated by opex impact

Ministerial Direction $2018-19	Share of change due to		2019-24 Draft Decision $2018-19
	Factors outside PWC's control – WACC and tax	Factors within PWC's control – opex, capex, incentive schemes	
$869.5m	+8%	- 27% (opex is 20%)	$705.6m (-19%)

- Opex reduction - $171m in 2019-24
- WACC – complex ups and downs resulting in increase vs fall in other networks (though AER allowed rate is lower than PWC proposed)

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•Ministerial allowance

Significant change from PWC proposal

$2018-19	PWC Proposed		AER Draft decision 2019-24		
2014-19[1]	$m (2018-19)	% change on 2014-19	$	% change on PWC proposed	Nominal price path
$869.5m	$861.5m (ARR)[2]	-0.9%	$705.6m (ARR)[2]	-18.8%	• Tariffs 9.2% lower on 1 July 2023 vs 1 July 2018; av annual decrease of 1.9% • Average residential bill 9.2% lower in 2019-20 then av 1.4% increases for 21-24

1. Ministerial allowance 2. Allowed revenue requirement

$2018-19	2014-19[1]	2019-24		
		PWC Proposal	AER Draft Decision	% change
Opex	$455.9m	$339.3m	$305.9m	-9.8%
Capex	$265.1	$383.0m	$315.6m	-17.6%
RAB - End of current period - End of 2019-24	$966.4m[2]	$1,231.1m	$1,177.8m	-4.4%

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1. Ministerial allowance, adjusted to exclude metering related costs (assumed to make up 3% of opex and capex)
2. RAB value as at 30 June 2019 determined in the AER Draft Decision

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Opex is key driver

- All agree that lack of data meant it difficult to assess level of opex efficiency
- PWC recognised it was inefficient and proposed a 10% reduction on base year
- CCP supports the AER's approach of building up an alternate "bottom up" measure rather than using a top down revealed costs approach
  - Detailed cost category analysis, excessive labour costs, rejection of most step changes, lower estimates of price and output growth, no EBSS
- This led to AER assessing the opex for an "efficient and prudent operator" to be a further reduction of 9.8% - overall 13.8% reduction in base opex
- We recognise that PWC does not have clearly developed pathways to achieve the 10% let alone the 13.8%
  - But this is a reflection of a lack of opex control over many years that consumer have been forced to pay for
  - Agree with AER draft decision including no EBSS
- Opex assumes no productivity growth – hopefully change following current review

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Capex

- Like opex, our approach is to focus on high level trends and rely on the expertise of the AER and its consultants with the repex model and individual project evaluation
  - eg we note the interaction of decisions on Berrimah and Wishart sub-stations
- We welcome the effort PWC is putting into development of risk and asset management practices
- Concern about demand forecasts – reflected in the Draft Report (p. 31)
  - Understand revised forecast will lead to lower customer connections assumption
  - off-grid renewables (Defence Dept; NT 50% renewables by 2030)
- Need comfort that PWC have the resources to complete capex programme plus Government undergrounding project
- Agree with CESS applying 2019-24 – for capital efficiency

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RAB a key issue for consumers

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- WACC at historical low in cycle (AER proposed 5.22% vs PWC proposed 6.62%)
- Given generally long asset lives (>20 yrs) – large risks to consumers once interest rate cycle changes
- Need to have laser like focus on capex at all times

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Tariff Structure Statement

- AER requirement to move towards cost reflective pricing
- Welcome the moves made by PWC to achieve this objective – greater proportion of revenue from fixed+demand charges
- However with the Pricing Order customers consuming <750MWh/yr (all but 200 of the 85,000 customers who consume 35% of grid supplied electricity) will not see these cost reflective price
  - So moves in other DNSPs to have new and upgrading customers facing cost reflective prices is not possible
- Encourage PWC and Jacana to undertake tariff trials to increase consumer knowledge
- Support the large customer tariff changes
  - less complex and more cost reflective tariffs eg removing declining block tariffs

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Work to be Done

- Welcome any feedback from consumers and their representatives on their issues of concern as well as how effectively PWC has engaged with them and how their issues have been addressed in the proposal and subsequently in the revised proposal
- CCP 13 will review PWC's revised proposal
- Comments / suggestions for the CCP can be sent via AERInquiry@aer.gov.au AER reference 60610

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