



New Reg: AusNet Services Trial
Insights Report 2 – Negotiations Round 1

23 May 2019

Australian Energy Regulator

FINAL REPORT



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I. INTRODUCTION

CEPA has been engaged by the Australian Energy Regulator (AER) to undertake an evaluation of AusNet Services’ trial of the New Reg process.

Our evaluation framework, dated 29 November 2018, provides further information on our overall approach to evaluating New Reg.¹ This Insights Report is the second in a series of three before we provide the AER with both an Interim Evaluation Report and a Final Evaluation Report. This second Insights Report covers the initial negotiation phase and publication of the Customer Forum’s Interim Engagement Report² and AusNet Services’ Draft Regulatory Proposal.³ The activities and deliverables in this phase, which corresponds with steps 3, 6, 7, 8 and 9 of the New Reg Process,⁴ are set out in the figure below.

Figure 1.1: Second Insights Report’s coverage



Source: CEPA. Note: We have used different colours to represent parties’ involvement: The Customer Forum = Green; AER = Gold; AusNet = Blue.

This Insights Report relies on and should be read in conjunction with the Second Monitoring Report prepared by Farrier Swier Consulting Pty Ltd, dated 16 April 2019.⁵ The Second Monitoring Report covered activities from the scope of agreement to the initial negotiations.

We note that the Customer Forum and AusNet Services have not reached an initial position on a number of areas in the scope for negotiations. The Customer Forum has positioned the Interim Engagement Report as a consultative document rather than as the Draft Engagement Report as specified in the Memorandum of Understanding (MOU).⁶ This reflects the fact that AusNet Services is also using the Draft as a consultative document rather than an actual preliminary submission. This has changed the scope of insights originally envisaged for this stage of the New Reg Trial on how it is progressing against its objectives.

¹ CEPA (2018), *New Reg Trial Evaluation Framework*, November. Available here: <https://www.aer.gov.au/networks-pipelines/guidelines-schemes-models-reviews/consultation-on-the-new-reg-process>

² Customer Forum (2019), *Interim Engagement Report*, February.

³ AusNet Services (2019), *Draft Electricity Distribution Regulatory Proposal: 1 January 2021 to 31 December 2025*, February.

⁴ Energy Consumers Australia, AER and Energy Networks Australia (2018), *New Reg: Towards Consumer-Centric Energy Network Regulation: Directions Paper*, March.

⁵ Farrier Swier (2019), *New Reg: AusNet Services Trial – Stage 2: Monitoring report on scope of agreement and initial negotiations, 15 March* (‘Monitoring Report 2’).

⁶ AusNet Services, Customer Forum and AER (2018), *Memorandum of Understanding*, June.



1.1. SUMMARY OF INSIGHTS

In the table below, we provide a summary of our insights against the relevant steps of the New Reg process set out in the Directions Paper. We set out further detail on each of the insights in Section 2. Our insights should be read noting that they are a snapshot based on the initial negotiating positions and accompanying justification. All the insights will be reviewed, and updated accordingly, as the trial progresses.

Table 1.1: Summary of Insights

New Reg process step	Insights
1. A network business may propose to the AER to undertake an Early Engagement Process to develop its regulatory proposal.	Covered in Insights Report 1.
2. If a network business decides to pursue the Early Engagement Process, it would submit an Early Engagement Plan to the AER. This would draw on informal discussions and consultation with the AER, the network business' existing consumer relationships and Energy Consumers Australia (ECA). The Plan outlines the process the business intends to undertake to develop its regulatory proposal, including:	Covered in Insights Report 1 and Step 6.
a. establishment of a consumer representative group (Customer Forum) which the network would resource and fund	
b. high-level scope of matters proposed to be considered within the Early Engagement Process	
c. process of dialogue and engagement that will be followed by the network business and Customer Forum	
d. role and expectations of the AER to support the Early Engagement Process.	
3. The Customer Forum should:	Insight 2.1. The Customer Forum appears to be providing a good conduit for consumers' perspectives. The Customer Forum has had a positive impact on AusNet Services' customer engagement and identified areas/ processes where AusNet Services could improve its services. The Customer Forum has achieved this by working with AusNet Services to engage with a range of different types of customers in different locations. ⁷
a. represent, 'bring' the perspectives of, and act on behalf of all consumer voices (large and small), having regard to the long term interests of current and future consumers	

⁷ The Customer Forum noted they have expanded the range and type of customers than AusNet Services has engaged with in the past.



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New Reg process step	Insights
<p>b. be fully independent of the network business</p>	<p>Insight 2.2. The Customer Forum continues to appear to be acting independently of AusNet Services, and AER Staff are comfortable with the Customer Forum’s independence. This is supported by the Customer Forum and AusNet Services commitment to publish material from and minutes of their meetings, and the Customer Forum and AusNet Services publishing their initial positions/ considerations for consultation.</p>
<p>c. have the skills and expertise to serve the role of being a credible counterparty to the network business</p>	<p>Insight 2.3. The Customer Forum has focused its engagement (to date) on identifying and seeking commitments from AusNet Services on customer experience outcomes. It has also challenged AusNet Services to set out its works program better to demonstrate customer benefits. The Forum has utilised the skill set of its members to form these positions and influence AusNet Services Regulatory Proposal.</p> <p>Insight 2.4. The Customer Forum has relied on AER Staff for a technical view on the efficiency of some of AusNet Services’ proposed expenditure (in addition to requesting that AusNet Services engage technical support to provide it with an opinion on specific areas of AusNet Services’ proposal). Given Insight 2.3, this has meant the Customer Forum’s negotiated positions in the Initial Engagement Report have tended to focus on customer needs and desired outcomes rather than on the efficient level of expenditure the network operator should be allowed to deliver on these customer preferences and requirements.</p> <p>Insight 2.5. Where the balance of focus and skill set of the Customer Forum should be in future New Reg processes may be an issue that stakeholders wish to consider when initially defining the scope of the negotiations and membership of the Customer Forum.</p>
<p>d. operate in an open and engaging way to establish and maintain its legitimacy with consumers and the wider community.</p>	<p>Insight 2.6. The wider community in AusNet Services’ distribution area provided a mix of views in response to a survey. While there was no specific question in the survey on whether the Customer Forum was operating in an open and engaging way, both customers, one of the three advocates, and one (of one) community group considered that the Customer Forum was able to understand customers’ expectations, preferences and concerns. Also supporting an open and transparent process, as noted in Insight 2.2, is the publication of Customer Forum and AusNet Services meeting minutes and the Interim Engagement Report/ Draft Regulatory Proposal document for consultation.</p>
<p>4. The AER will decide whether or not it accepts the proposed Early Engagement Plan. The AER may propose amendments to the Plan. If the AER accepts the Plan, it commits itself to be deeply involved in the Early Engagement Process.</p>	<p>Covered in Insights Report 1.</p>
<p>a. This commitment is formalised through an ‘Engagement Agreement’ entered into by the business, the AER and the Customer Forum.</p>	



New Reg process step	Insights
<p>b. The Engagement Agreement sets out the roles and expectations of each of the parties, including the scope, funding arrangements, anticipated timelines, ‘off-ramps’ or termination conditions, and arrangements for a jointly conducted ex post review.</p>	
<p>5. It is anticipated that the early phases of engagement between the network business and Customer Forum will involve induction, training, and information sharing. The AER will be closely involved in providing background information including on network performance comparisons and previous related decisions, and guidance on AER assessment approaches and its statutory roles and responsibilities in revenue determination processes. Both the business and the Forum will do this in a way that does not require Forum members to have energy industry or regulatory expertise.</p>	<p>Covered in Insights Report 1.</p>
<p>6. The next step involves the business and Customer Forum scoping in detail the matters to be considered in the Early Engagement Process. This should also set out how the parties intend to collect information on the perspectives of customers (for example, through customer research or direct engagement) to inform their consideration of these matters. The scope of matters to be considered must be agreed between the business and Customer Forum, and accepted by the AER—although the AER may be more closely involved in the scoping phase for the purpose of a trial.</p>	<p>Insight 2.7. The Customer Forum and AusNet Services consider that the scope of matters they are negotiating is appropriate. However, AER Staff noted that the monitoring/ evaluation should consider whether the expanded scope of matters (to those AER Staff considered were out of scope) was appropriate given the timelines of the trial.⁸</p> <p>Insight 2.8. While the Customer Forum has been able to rely on AER Staff for guidance on what is or isn’t consistent with how the regulatory framework currently functions, the Customer Forum set out a few positions in the Interim Engagement Report that AER Staff consider are potentially inconsistent with the framework (e.g. in relation to innovation and the CRM proposal). The positions were not wrong <i>per se</i>; however, it appeared that the Customer Forum, in forming these positions, either did not appreciate the technical interactions between different elements of the framework or what is feasible under the current regulatory framework. (We note that some of these issues relate to out of scope matters, please also refer to Insight 2.12.) The former could indicate that more (or more timely) regulatory technical support needs to be provided to the Customer Forum, and/ or additional experience/ skill set be incorporated in the Customer Forum’s membership, in future New Reg processes. The latter may provide an interesting insight into the appropriateness of the regulatory framework, given new information on customer preferences, and will be considered in our evaluation.</p>
<p>a. Ideally the business and Customer Forum can agree to the proposal as a whole—and that it fully reflects consumer perspectives and preferences wherever relevant. It is envisaged that the Early Engagement Process will, in principle, deal with any matter that may arise in a network business’ regulatory proposal. However, for reasons of practicality or due to regulatory constraints, certain matters may be taken ‘off the table’. For example, at least for a trial, some aspects of the proposal may be out of the business’ control due to government regulations or reliability standards, or are subject to a binding AER guideline.</p>	
<p>7. The Early Engagement Plan will specify how the Early Engagement Process will be carried out. Central to the Early Engagement Process is the</p>	<p>Insight 2.9. The Customer Forum noted that agreeing expenditure levels was difficult given the moving nature of AusNet Services’ forecasts. The Customer Forum</p>

⁸ Monitoring Report 2, page 12.





New Reg process step	Insights
<p>idea of creating a ‘dynamic conversation’ between the network business and Customer Forum, supported by the AER, to achieve outcomes in the long term interests of consumers. These discussions should be structured with the aim of reaching agreements in a timely way. The AER needs to be assured that it has sufficient visibility during the Early Engagement Process that it can indicate that something will not be acceptable before it is submitted.</p>	<p>indicated that it may have left numbers out of its Interim Engagement Report if it had to do it again. AusNet Services noted that estimates will move around as the network is trying to establish expenditure estimates 18 months or more before they are due to be incurred, and some estimates will not be finalised until close to the submission of its Regulatory Proposal. This raises questions to explore on whether the phasing of the New Reg process as laid out in the MOU is appropriate.</p> <p>Insight 2.10. The Customer Forum and AusNet Services originally envisaged that the Draft Engagement Report and Draft Regulatory Proposal would set out both parties’ initial positions, and this was specified in the MOU. However, the Customer Forum has decided to treat the Draft Engagement Report as an interim one for consultative purposes. This indicates that the MOU could have provided greater flexibility for what the Draft Engagement Report needed to cover.⁹</p> <p>Insight 2.11. While bearing in mind that this is the first trial of New Reg and therefore no precedent has been established for what AER Staff are seeking in terms of justification for the positions reached, the publications of the reports have been important for AER Staff to provide their views on how the Customer Forum and AusNet Services have set out their positions and associated justification.</p>
<p>a. Throughout the engagement process, the AER will contribute to the process of reaching agreement by providing information and explaining issues through ‘advice notes’ and/or presentations that communicate the ‘boundaries’ of the rules, and what it may consider as an acceptable regulatory outcome—consistent with AER guideline approaches. The AER may also identify aspects of a proposal that in its view would most benefit from consumer perspectives, including through customer research and wider stakeholder consultation.</p>	<p>Insight 2.12. The Customer Forum and AusNet Services are satisfied with the advice AER Staff have been providing. However, related to Insight 2.8, AER Staff noted that a number of the issues it has raised during the course of the negotiation process were related to matters outside the agreed Scope of Negotiation. AER Staff had not provided guidance notes for these matters. AER Staff have provided the Customer Forum with their views on the Interim Engagement Report and Draft Regulatory Proposal in Guidance Note 9 and continue to work with the Customer Forum on these points.</p>
<p>b. The Customer Forum should be resourced to communicate directly with end-customers, customer representatives, and other engagement channels and forums the network uses for its business-as-usual engagement, to elicit and understand their preferences, to carry out customer research (or help shape the business’ research program), and to communicate issues and trade-offs back to customers.</p>	<p>Insight 2.13. The Customer Forum has had sufficient resourcing to carry out its scope of work. However, it has noted that more administrative support may have made its role easier. Securing this type of support during the early stages of a New Reg process may be something that needs to be considered in future.</p>
<p>8. At the conclusion of the Early Engagement Process the parties submit an Engagement Report setting</p>	<p>Insight 2.14. Based on the Interim Engagement Report, we consider that the Customer Forum provided</p>

⁹ We understand that AusNet Services and the Customer Forum asked for the inclusion of the Draft Engagement Report stage in the MOU.





New Reg process step	Insights
<p>out the process followed and outcomes from the engagement. The Engagement Report is a critical input to the AER's subsequent assessment of the regulatory proposal submitted by the network business, contributes to learning and improvement for future applications of the New Reg process, and supports accountability of the Customer Forum to the end-use consumers.</p>	<p>justification to support some but not all of the initial positions it reached/ did not reach. We also note that it was not clear for some matters what position the Customer Forum had reached. To help achieve the objectives set out in the MOU, the Customer Forum, in justifying its final positions, needs to provide further linkages between its positions, customers' preferences it has gathered during the negotiation process, and the achievement of the NEO. This will assist the AER in making its determination on whether the positions adopted by the Customer Forum contribute to the achievement of the NEO.¹⁰</p>
<p>a. The Engagement Report includes the scope of matters considered and, for each matter, the agreement that has been reached or, in the event of disagreement, the positions of the relevant parties.</p>	<p>Insight 2.15. Interim Engagement Report was, to a large extent, <i>structured</i> like a negotiation on each building block, i.e., assessing items under the operating expenditure (opex) block, the augmentation expenditure (augex) block, the replacement expenditure (repex) block, etc. However, the Customer Forum, as noted in Insights 2.3, 2.4 and 2.5, has focused more on determining appropriate customer experience and outputs/ outcomes which don't necessarily correspond neatly with individual building blocks.</p>
<p>b. For the matters which have been agreed between the parties, the Engagement Report should explain why these agreements reached are consistent with, or best reflect, consumer perspectives and preferences—referencing any customer research or consultation undertaken during the process.</p>	<p>We consider that more flexibility in terms of the structure of the report might be appropriate given how the Customer Forum approached its role (and how future Customer Forum may approach their roles). For example, the Customer Forum could set out the service outcomes required (in line with customer preferences), while leaving the assessment of the prudence and efficiency of specific expenditure items to the AER.¹¹ We will consider this issue further in future evaluation reports.</p>
<p>c. For aspects of a proposal for which the business and Customer Forum could not reach agreement, the Engagement Report should identify and explain the reasons these issues were left unresolved. This provides transparency and a useful starting point for the AER's subsequent assessment of the regulatory proposal.</p>	<p>Insight 2.16. When read independently, we do not consider that the Draft Regulatory Proposal and the Interim Engagement Report always give the same impression of the positions reached by each party. Alternative procedural or other mechanisms for documenting agreements may be worth consideration to ensure that discrepancies, or perceived discrepancies, are dealt with.</p>
<p>9. If the network business and its Customer Forum can reach agreement on some or all aspects of the regulatory proposal, there is an expectation that the Engagement Report would evidence how the agreement reflected consumers' preferences, citing relevant customer research and results of consumer engagement. Provided the Engagement Report accompanies or is included in the network business' revenue proposal the AER must have regard to it.¹²</p>	

¹⁰ As well as improving the overall outcomes of the regulatory review process with a view to promoting the long-term interests of consumers of electricity, the New Reg trial also has the objective of improving the speed and reducing the cost of the regulatory review process.

¹¹ For example, the Customer Forum was asked to provide its position on the prudence of opex step changes that were part of mandatory requirements imposed on AusNet Services. While this would not take up much of its negotiating time, it is not clear the value in it providing opinions on these items.

¹² Clauses 6.10.1(b)(1), 6.11.1(b)(1), 6A.12.1(a1)(1) & 6A.13.1(a1)(1) of the National Electricity Rules.





2. OUR INITIAL INSIGHTS

In this section we set out our second set of insights on the New Reg process.

2.1. STEP 3: BRINGING CUSTOMERS' PERSPECTIVES AND PREFERENCES

Insight 2.1

The Customer Forum appears to be providing a good conduit for consumers' perspectives. The Customer Forum has had a positive impact on AusNet Services' customer engagement and identified areas/ processes where AusNet Services could improve its services. The Customer Forum has achieved this by working with AusNet Services to engage with a range of different types of customers in different locations.¹³

AusNet Services' decision to undertake the New Reg trial and engage the Customer Forum appears to have had a significant impact on AusNet Services' customer engagement. The Customer Forum noted in its Interim Engagement Report that it believed it had identified inadequacies in AusNet Services' customer research and understanding in a number of areas.¹⁴ In order to improve this, and provide it with better information on AusNet Services' customers' preferences, the Customer Forum encouraged and worked with AusNet Services to carry out engagement/ research targeting:

- smaller communities; and
- businesses.

This research has brought AusNet Services' attention to service issues for different locations/ customers groups in its service area.¹⁵ The Customer Forum's customer engagement has also highlighted differences in how AusNet Services dealt with various customers (see for example Customer Forum, 2019, Appendix E4). The Customer Forum appears to have been successful in identifying issues in AusNet Services' processes that could affect all of AusNet Services' customers.

The Customer Forum is yet to agree with AusNet Services on how services to some specific groups of customers (for example, the dairy farmers in Gippsland)¹⁶ could be improved and how this should be funded, however, it has agreed some broader customer experience and hardship arrangements.^{17,18}

¹³ The Customer Forum noted they have expanded the range and type of customers than AusNet Services has engaged with in the past.

¹⁴ Customer Forum (2019), page 11.

¹⁵ Customer Forum (2019), Appendix E.

¹⁶ See Customer Forum (2019), Appendix E2.

¹⁷ Customer Forum (2019), section 9.

¹⁸ It is well known that customers experience different levels of services depending on their location, which is why in addition to average service quality metrics incentives (i.e. STPIS) there are schemes such as the Guaranteed Service Level (GSL) payments in place for worst served customers.



Insight 2.2

The Customer Forum continues to appear to be acting independently of AusNet Services, and AER staff are comfortable with the Customer Forum's independence. This is supported by the Customer Forum and AusNet Services commitment to publish material from and minutes of their meetings, and the Customer Forum and AusNet Services publishing their initial positions/ considerations for consultation.

In line with Insight 4 from our first Insights Report, the Customer Forum appears to be acting independently of AusNet Services. For example, the Customer Forum:

- has challenged AusNet Services on its processes and customer service levels;
- challenged AER Staff on its assumptions and models; and
- used its customer engagement to identify concerns with AusNet Services' customer engagement and quality of service.¹⁹

AER Staff, the Customer Forum, and AusNet Services assessed that the Customer Forum had been acting independently.²⁰ We also note that the Customer Forum and AusNet Services have committed to publishing minutes from their meetings and are consulting on their initial positions.

We note, however, that the publication of the Interim Engagement Report and the Draft Regulatory Proposal were delayed from late 2018 to February 2019. This delay cut into the public consultation time for the Draft Regulatory Proposal and Interim Engagement Report. The delay resulted from AusNet Services' board concerns with some of the language and content of the case studies in the Interim Engagement Report. These concerns were primarily around the Board being satisfied that *"the actions described by the company [AusNet Services' management] to address customer concerns were comprehensive"*²¹ and that the Customer Forum acknowledged that AusNet Services' regulatory obligations were met. Both parties stated that the scope of negotiations and the negotiated positions were unchanged from what was agreed by late 2018 to the publication in February.²²

The Customer Forum believed that the lessons from this delay included the need for the DNSP's board to be firmly linked into the negotiation process to avoid misalignment developing and making the Customer Forum aware of the Board's reasonable sensitivity to language.²³

Insight 2.3

The Customer Forum has focused its engagement (to date) on identifying and seeking commitments from AusNet Services on customer experience outcomes. It has also challenged AusNet Services to set out its works program better to demonstrate customer benefits. The Forum has utilised the skill set of its members to form these positions and influence AusNet Services Regulatory Proposal.

¹⁹ Customer Forum (2019), page 11.

²⁰ Monitoring Report 2, page 17.

²¹ Monitoring Report 2, page 18.

²² Monitoring Report 2, page 18.

²³ Monitoring Report 2, page 18.



Insight 2.4

The Customer Forum has relied on AER Staff for a technical view on the efficiency of some of AusNet Services' proposed expenditure (in addition to requesting that AusNet Services engage technical support to provide it with an opinion on specific areas of AusNet Services' proposal). Given Insight 2.3, this has meant the Customer Forum's negotiated positions in the Initial Engagement Report have tended to focus on customer needs and desired outcomes rather than on the efficient level of expenditure the network operator should be allowed to deliver on these customer preferences and requirements.

Insight 2.5

Where the balance of focus and skill set of the Customer Forum should be in future New Reg processes, may be an issue that stakeholders wish to consider when initially defining the scope of the negotiations and membership of the Customer Forum.

The Customer Forum, AusNet Services, and AER staff considered that the Customer Forum has a good mix of skills. This skill set has enabled the Customer Forum to challenge AusNet Services on:

- customer engagement;
- business practices;
- options analysis; and
- customer experience.

We believe, that this is evidenced in how it:

- reshaped AusNet Services' engagement programme;
- negotiated customer outcomes such as the customer service incentive scheme (CSIS),²⁴ the Community Liaison Officer and a Commercial and Industrial Liaison Manager, and more general improvements in AusNet Services customer engagement programme;
- challenged some of AusNet Services business processes, e.g., how it assesses and pays Guaranteed Service Levels (GSLs), and how it presents cost-benefit information on its repex options;²⁵ and
- has helped AusNet Services identify issues in its GSLs processes.

The Customer Forum positions reflect its view that its role was more of a qualitative challenger/ negotiator rather than being an economic one.²⁶ However, AER staff consider that this may undersell the role they believe the Customer Forum is playing.

The Customer Forum has relied on AER Staff guidance notes and AusNet Services for technical assistance. We understand that the Customer Forum has also sought support from AER Staff on a few matters. The Customer Forum's reliance on AER Staff advice on technical issues will be considered further as the trial progresses.

²⁴ AER Staff consider that this may be categorised under the Small Scale Incentive Scheme (SSIS).

²⁵ The Customer Forum also appears to be successful at challenging AusNet Services on its process and practices (like an independent Non-Executive Director, but from the perspective of customers). We note that Ofwat has placed a significant emphasis on unlisted company's boards to meet principles and regulatory requirements of a listed company to help ensure that companies take greater ownership of and accountability for delivery to customers. Ofwat (2014), *Board leadership, transparency and governance – principles*, January.

²⁶ Monitoring Report 2, page 27.

**Insight 2.6**

The wider community in AusNet Services distribution area provided a mix of views in response to a survey. While there was no specific question in the survey on whether the Customer Forum was operating in an open and engaging way, both customers, one of the three advocates, and one (of one) community group considered that the Customer Forum was able to understand customers' expectations, preferences and concerns.

Also supporting an open and transparent process, as noted in Insight 2.2, is the publication of Customer Forum and AusNet Services meeting minutes and the Interim Engagement Report and Draft Regulatory Proposal for consultation.

2.2. STEP 6: SCOPE OF NEGOTIATIONS**Insight 2.7**

The Customer Forum and AusNet Services consider that the scope of matters they are negotiating is appropriate. However, AER Staff noted that the monitoring/ evaluation should consider whether the expanded scope of matters (to those AER Staff considered were out of scope) was appropriate given the timelines of the trial.²⁷

Insight 2.8

While the Customer Forum has been able to rely on AER Staff for guidance on what is or isn't consistent with how the regulatory framework currently functions, the Customer Forum set out a few positions in the Interim Engagement Report that AER Staff considers are potentially inconsistent with the framework (e.g. in relation to innovation and the CRM proposal). The positions were not wrong *per se*; however, it appeared that the Customer Forum, in forming these positions, either did not appreciate the technical interactions between different elements of the framework or what is feasible under the current regulatory framework. (We note that some of these issues relate to out of scope matters, please also refer to Insight 2.12.) The former could indicate that more (or more timely) regulatory technical support needs to be provided to the Customer Forum, and/ or additional experience/ skill set be incorporated in the Customer Forum's membership, in future New Reg processes. The latter may provide an interesting insight into the appropriateness of the regulatory framework, given new information on customer preferences, and will be considered in our evaluation.

As noted in the first Insights Report, the Customer Forum and AusNet Services valued the flexibility to discuss matters outside those categorised as 'in scope' (AER staff assisted). These 'out of scope' matters fall into two categories, 'out of scope and AusNet Services and Customer Forum have agreed to negotiate on' or 'out of scope'.²⁸ The Customer Forum noted that once recruited it made sense for them to be able to consider the best scope to utilise their skill sets.²⁹

AER Staff questioned whether the wider scope of matters that the Customer Forum and AusNet Services chose to consider may have drawn resources away from matters that were in scope.³⁰ The Customer Forum and AusNet Services did not share these concerns.

However, we note that:

- AER Staff are concerned that the Customer Forum's position on an innovation allowance for AusNet services is not aligned with the regulatory framework. This related to an 'out of scope'

²⁷ Monitoring Report 2, page 12.

²⁸ This is based on AER Staff categorisation. See Monitoring Report 2, page 10.

²⁹ Monitoring Report 2, page 12.

³⁰ Monitoring Report 2, page 12.



matter for which AER Staff had not anticipated providing assistance on. In particular, the Customer Forum proposed that AusNet Services construct an innovation budget based on a modest per customer contribution.³¹ However, AER Staff considered that the AER could not approve a general innovation allowance that is not linked to a specific activity or objective.³² We note that the Customer Forum has requested AusNet Services to refine the list of innovation projects that it wishes to pursue, based on a set of principles provided by the Customer Forum. These include the principle that the projects should directly benefit and result in improved service to customers.³³

- The Customer Forum in principle position on the CRM system may not take account of the technical interactions between the expenditure and other elements in the regulatory framework. Specifically, whether the CRM would be partially (or fully) funded under the CSIS.

These examples, and the general widening of the negotiations to out of scope matters, may indicate:

- that more, or more timely, regulatory technical support may need to be provided to the Customer Forum, and/ or additional experience/ skill set be incorporated in the Customer Forum's membership, in future New Reg processes; and/or
- that the regulatory framework needs to evolve, given new information on customer preferences. This will be considered in our evaluation.

In regard to the latter, the Customer Forum has noted it is not certain the current framework automatically ensures a satisfactory level of service.³⁴ Please also refer to Insight 2.12.

2.3. STEP 7: THE 'DYNAMIC CONVERSATION'

Insight 2.9

The Customer Forum noted that agreeing expenditure levels was difficult given the moving nature of AusNet Services' forecasts. The Customer Forum indicated that it may have left numbers out of its Interim Engagement Report if it had to do it again. AusNet Services noted that estimates will move around as the network is trying to establish expenditure estimates 18 months or more before they are due to be incurred, and some estimates will not be finalised until close to the submission of its Regulatory Proposal. This raises questions to explore on whether the phasing of the New Reg process as laid out in the MOU is appropriate.

Insight 2.10

The Customer Forum and AusNet Services originally envisaged that the Draft Engagement Report and Draft Regulatory Proposal would set out both parties' initial positions, and this was specified in the MOU. However, the Customer Forum has decided to treat the Draft Engagement Report as an interim one for consultative purposes. This indicates that the MOU could have provided greater flexibility for what the Draft Engagement Report needed to cover.³⁵

³¹ Customer Forum (2019), page 34.

³² AER Staff Guidance Note 9, page 20.

³³ Customer Forum (2019), page 34.

³⁴ Customer Forum (2019), page 12.

³⁵ We understand that AusNet Services and the Customer Forum asked for the inclusion of the Draft Engagement Report stage in the MOU.



Insight 2.11

While bearing in mind that this is the first trial of New Reg and therefore no precedent has been established for what AER Staff are seeking in terms of justification for the positions reached, the publications of the reports have been important for AER Staff to provide their views on how the Customer Forum and AusNet Services have set out their positions and associated justification.

The MOU states that the Draft Engagement Report would set out the Customer Forum's initial positions (i.e., the extent of agreement or disagreement between the parties).³⁶ However, the Customer Forum noted that AusNet Services was still to finalise its costs and,³⁷ in addition, the Customer Forum was also awaiting further advice from AusNet Services on a number of issues.³⁸ Therefore, the Customer Forum had not been able to reach an initial position on some matters.

The Customer Forum noted that the changing expenditure estimates impacted its ability to fully consider the cost/ quality trade-offs and it noted that this made it difficult to achieve the Interim Engagement Report milestone. The Customer Forum considered that in hindsight it would have excluded numbers from the Interim Engagement Report.

In its interview for the Monitoring Report, the Customer Forum stated that a two-stage engagement with customers may have been better, where it assessed the need, before presenting options that were costed out in more detail.³⁹ This may be an approach to consider in future New Reg processes.

Insight 2.12

The Customer Forum and AusNet Services are satisfied with the advice AER Staff have been providing. However, related to Insight 2.8, AER Staff noted that a number of the issues it has raised during the course of the negotiation process were related to matters outside the agreed Scope of Negotiation. AER Staff had not provided guidance notes for these matters. AER Staff have provided the Customer Forum with their views on the Interim Engagement Report and Draft Regulatory Proposal in Guidance Note 9 and continue to work with the Customer Forum on these points.

Insight 2.13

The Customer Forum has had sufficient resourcing to carry out its scope of work. However, it has noted that more administrative support may have made its role easier.⁴⁰ Securing this type of support during the early stages of a New Reg process may be something that needs to be considered in future.

³⁶ MOU, Clause 5(d).

³⁷ The Victorian Government's Solar House program, announced in August 2018, heavily impacted AusNet Services' expenditure forecasts, particularly its DER estimates.

³⁸ Customer Forum (2019), page iii.

³⁹ This is based on our notes from the Customer Forum interview, as part of the monitoring process, held on 28 February 2019.

⁴⁰ Monitoring Report 2, page 14.



2.4. STEP 8 AND 9: SETTING OUT NEGOTIATING POSITIONS

Insight 2.14

Based on the Interim Engagement Report, we consider that the Customer Forum provided justification to support some but not all of the initial positions it reached/ did not reach. We also note that it was not clear for some matters what position the Customer Forum had reached. To help achieve the objectives set out in the MOU, the Customer Forum, in justifying its final positions, needs to provide further linkages between its positions, customers' preferences it has gathered during the negotiation process, and the achievement of the NEO.⁴¹ This will assist the AER in making its determination on whether the positions adopted by the Customer Forum contribute to the achievement of the NEO.⁴²

Insight 2.15

Interim Engagement Report was, to a large extent, *structured* like a negotiation on each building block, i.e., assessing items under the operating expenditure (opex) block, the augmentation expenditure (augex) block, the replacement expenditure (repex) block, etc. However, the Customer Forum, as noted in Insights 2.3, 2.4 and 2.5, has focused more on determining appropriate customer experience and outputs/ outcomes which don't necessarily correspond neatly with individual building blocks.

We consider that more flexibility in terms of the structure of the report might be appropriate given how the Customer Forum approached its role (and how future Customer Forum may approach their roles). For example, the Customer Forum could set out the service outcomes required (in line with customer preferences), while leaving the assessment of the prudence and efficiency of specific expenditure items to the AER. We will consider this issue further in future evaluation reports.

At a high level, the scope of matters covered in the Interim Engagement Report appeared appropriate. The Customer Forum has been able to provide views/ opinions on all the matters it is negotiating with AusNet Services and, to some extent, it has been able to reference customers' preferences in relation to each of its positions. However, and perhaps due to the interim nature of the report, the Customer Forum's level of justifications for its positions, including how it has considered both current and future consumers, has varied across the matters for agreement.

While AER Staff noted that the Interim Engagement Report

“summarises the research and engagement undertaken by the Forum and that this document has been targeted at facilitating consultation with customers and advocates, rather than at addressing the requirements of the AER to support the reset process”⁴³

AER Staff considered that the Customer Forum, in its Interim Engagement Report, has not fulfilled all of the requirements set out in the MOU. Namely, it did not structure its report around answering the following points:

- *Matters in scope and considered by the Forum*
- *Areas of agreement and disagreement with AusNet Services*

⁴¹ We believe our view is consistent with AER Staff views set out in the AER Staff Guidance Note 9.

⁴² As well as improving the overall outcomes of the regulatory review process with a view to promoting the long-term interests of consumers of electricity, the New Reg trial also has the objective of improving the speed and reducing the cost of the regulatory review process.

⁴³ Monitoring Report 2, page 27.



- *How these positions are in the interests of consumers*⁴⁴

In addition, we also could not always determine, from the Interim Engagement Report, what the Customer Forum's positions were. For example, in regard to metering, the Customer Forum notes that:

*"Given the annual average metering charge is decreasing and customer benefits are increasing, the Customer Forum believes AusNet Services proposal represents value for money and will be enhanced through improved communication of metering benefits to customers."*⁴⁵

While the Customer Forum indicates an agreement with AusNet Services' proposal, it is not clear what it is agreeing to. For example, is the Customer Forum agreeing to the costs of AusNet Services metering communication programme? And/ or that AusNet Services proposed reductions are prudent and efficient?

In our opinion, the Customer Forum is likely providing useful information on customers preferences and desired outcomes/ outputs, which is in line with the trial objective of improving the overall outcomes of the regulatory review process with a view to promoting the long-term interests of consumers of electricity. However, the New Reg trial also has the objective of improving the speed and reducing the cost of the regulatory review process. The more justification the Customer Forum can provide for its positions the more likely it is that the latter objective for the New Reg trial is achieved, in particular, in making it easier for the AER to determine that the Customer Forum's final negotiated positions achieve the NEO.

Additional questions that have arisen from our review of the available material, are:

- Is it sufficient, for some matters, that the Customer Forum justify its positions from demand-side based outcomes/ outputs on consumer preferences only and leave the analysis of 'prudency and efficiency' of the inputs to the AER?
- How can the Customer Forum prioritise and assess issues on which it is best placed to provide input? For example, the Customer Forum spent time considering and arriving at positions on expenditure items that AusNet Services considered were mandatory and stated it was up to the AER to determine if the expenditure was efficient; and the Customer Forum indicated that it considers that 1.5% productivity is appropriate for AusNet Services but it provided no evidence that would assist the AER in making a determination on this outside of its National Electricity Market (NEM) wide approach.⁴⁶
- Should future Engagement Reports be structured differently to align with the Customer Forum's expected role in each negotiation? The Interim Engagement Report was, to a large extent, laid out like a negotiation on each building block, i.e. assessing items under the operating expenditure (opex) block, the augmentation expenditure (augex) block, the replacement expenditure (repex) block, etc. While we understand that this was partly specified by AER Staff, and it was how matters were presented to it, the Customer Forum has focused more on determining customer experience and outputs/ outcomes, which may involve a number of interactions across the building blocks.

We will seek to evaluate these questions as the trial progresses.

⁴⁴ Monitoring Report 2, page 27.

⁴⁵ Customer Forum (2019), page 40.

⁴⁶ We note that AER Staff, in Guidance Note 9, consider that AusNet Services commitment to applying the AER's estimate means it does not need to revisit AusNet Services' proposal.

**Insight 2.16**

When read independently, we do not consider that the Draft Regulatory Proposal and the Interim Engagement Report always give the same impression of the positions reached by each party. Alternative procedural or other mechanisms for documenting agreements may be worth consideration to ensure that discrepancies, or perceived discrepancies, are dealt with.

The Customer Forum and AusNet Services are satisfied that AusNet Services' Draft Regulatory Proposal represent the Customer Forum's agreed position. However, our reading of the Draft Regulatory Proposal indicates that, in places, the Customer Forum's position may be misrepresented. For example, AusNet Services stated that:

"The Customer Forum supported in principle:

>> a Customer Relationship Management (CRM) system costing \$2.29 million (\$2020), which will deliver outcomes valued by customers; and

>> an Outage Management System costing \$0.25 million (\$2020)."⁴⁷

This could be interpreted as the Customer Forum agreeing to the amounts proposed. However, the Customer Forum agreed in principle to the need for the CRM but stated that the AER needs to review the expenditure:

"Accordingly, the Customer Forum supported, in principle, AusNet Services' proposed investment in the Customer Relationship Management and Outage Management systems. The Customer Forum concluded the proposed budget and scope for these projects was outside its expertise. It further concluded that the AER would be better equipped to analyse these aspects of the proposals."⁴⁸

Another example is metering (an out of scope matter). The Customer Forum notes that it is not satisfied that the 4G expenditure upgrade is appropriate,⁴⁹ however AusNet Services' Draft Regulatory Proposal only states the Customer Forum view as:

"The Customer Forum believes AusNet Services' proposal represents value for money given the annual average metering charge is falling and customer benefits are increasing. The Customer Forum also considers that improved communication of metering benefits to customers (as shown in Chapter 5) is required."⁵⁰

While these discrepancies may be unintended, if a reader were only to read the Draft Regulatory Proposal they may come away with a different view of the Customer Forum's positions than if they had only read the Interim Engagement Report.

This suggests that alternative procedural or other mechanisms for documenting agreements may be worth consideration. This will be explored in the final evaluation report when the trial has been completed and the outcomes delivered can be analysed more fully.

⁴⁷ AusNet Services (2019), page 53.

⁴⁸ Customer Forum (2019), page 21.

⁴⁹ Customer Forum (2019), page 39.

⁵⁰ AusNet Services (2019), page 80.



FINAL REPORT

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