

Here's how our plans are shaping up

Regulatory Reset
Draft Proposal 2021–2025

energised
2021–2025



We'll deliver a safe, dependable and flexible network while keeping our prices low

Thank you for reading our draft proposal outlining the value and services we'll provide you in 2021–2025. We aim to deliver a safe, dependable and flexible supply of electricity, while keeping our prices among the lowest in the country.

As a business, we take pride in delivering electricity to over 600,000 Victorians. We know how important our performance is to you, so that every day your household and business can go about their activities.

As we look to the future, it's important we keep delivering the services you want. That's why we're asking you to comment on our investment plans. Your feedback has, and will continue to shape the services we provide.

While it's an exciting time, as the electricity industry presents you with more opportunities to take control of your electricity use (including solar and batteries), it's also becoming more complex from our network's perspective. In preparing our network to accommodate this change, we'll be investing in systems that help you make informed energy choices. This sees us leaning more on technology and data than ever before in order to provide you electricity through a smarter network.

As well as facilitating technology and the change that comes with it, we'll also provide you with the safe and dependable service you expect. Your wellbeing, and that of our people, is our number one priority, and as such, we never compromise on safety.

Being part of the CitiPower community means you already receive among the lowest electricity network charges in Australia. We deliver more services to you for each dollar we invest than most other electricity distributors. While our charges only make up 27% of the average residential electricity bill, affordability has continued to be front of our minds in developing this plan. To help, we'll reduce our charges in 2021 by an average of \$25 for residential customers and \$94 for business customers.

We appreciate everyone who has already taken the time to share their views with us. We'll keep listening so we can best meet your needs.

I look forward to hearing your comments.

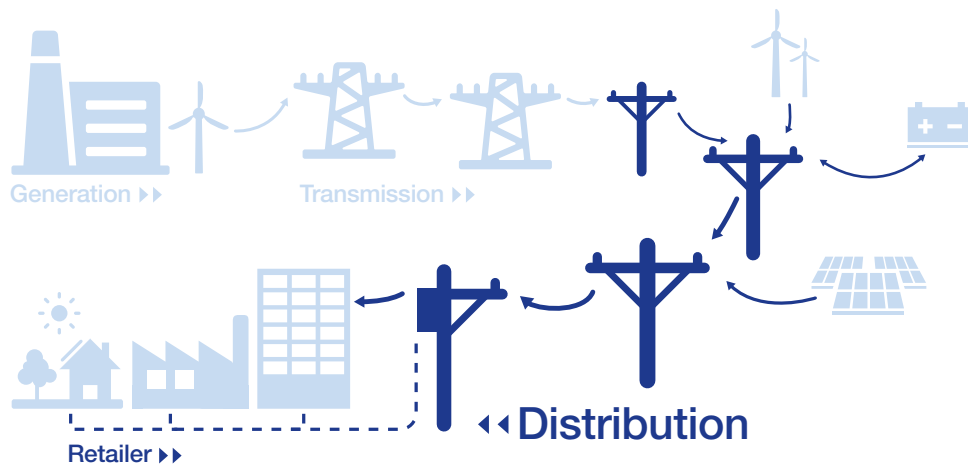


Tim Rourke
Chief Executive Officer



We're part of your community

We own and manage the electricity distribution network that provides power for Melbourne's central business district and inner suburbs. Our network includes more than 58,000 poles and 7,500 kilometres of powerlines.














We manage this part of the process to provide you electricity via your retailer



We serve customers like you, the cafes and bars you visit, major sporting facilities like the Melbourne Cricket Ground, hospitals and water utilities, and your public transport systems. We also support over 25% of Victoria's GDP.

Here's what we've been doing already

Our draft proposal builds on the work we've been doing in recent years. We're proud of our strong reputation for operating a safe and reliable network, while at the same time being one of the most cost-efficient distributors in Australia. Our future investment plans are discussed in the remainder of this document.

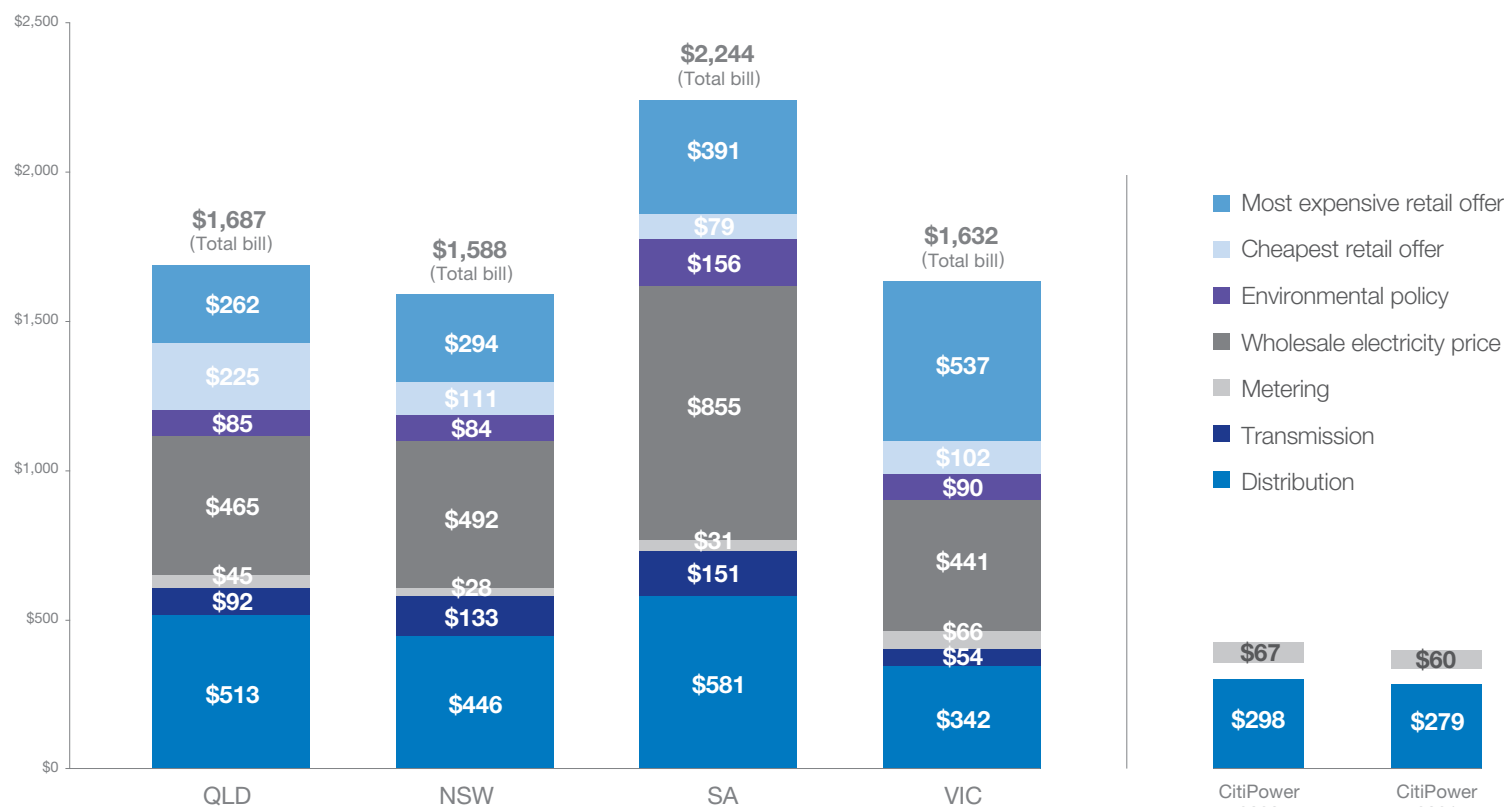
|  Safe and dependable |  Flexible |  Affordable |
|---|---|---|
|  <p>Australia's most reliable network – available for over 99.99% of the year, or just 20 minutes off supply per annum on average for customers.</p> |  <p>Implemented an online portal for new connections, saving you and your electrician time and effort.</p> |  <p>Delivered the second lowest distribution network charges in Australia, at \$291 per annum for average residential customers.</p> |
|  <p>Over \$99 million invested to ensure electricity supply to the CBD is secure</p> |  <p>Supported over 92MW of rooftop solar and 2MW of battery storage.</p> |  <p>Most highly utilised CBD and urban network in the country – we get the most out of our assets, so you pay less.</p> |
|  <p>19% reduction in public safety incidents since 2013. Safety is our number one priority always.</p> |  <p>We use 'smart' meters to identify and respond to safety risks before they occur. We're making the most of your investment.</p> |  <p>One of the top two most cost-efficient distributors in Australia based on AER benchmarking. Providing you value for money.</p> |


You'll see these three themes discussed a lot in this document. These reflect the views and preferences we heard from our stakeholders throughout the engagement process.

Victorian's already benefit from the lowest network charges in Australia.

Based on analysis undertaken by the Australian Energy Market Commission, Victorian network charges will average \$342 per annum in 2019, compared to other states such as NSW where network charges may exceed \$446.

Typical household electricity bill composition by state



Source: Based on typical customer consumption, ranging from 3,865-4,430kWh per annum, as set out in the Australian Energy Market Commission report, *Residential electricity price trends 2018*

Based on typical customer consumption of 4,200kWh per annum

You can help shape your energy future

Our revenues are regulated by the Australian Energy Regulator (AER), and every five years they review our forecast revenue requirement for approval.

This draft proposal sets out the services we'll deliver over the five-year period starting 1 January 2021. We're publishing a draft to get your thoughts on our proposal early. Your feedback will help shape our formal regulatory proposal due to the AER in July 2019.

The feedback you've provided so far has been reflected in our work plans and forecasts. We operate in an ever-changing energy sector, so it's important we continue to plan for the future while still meeting your current expectations.

In addition to the investments we'll make to deliver your preferred services, our draft proposal outlines the expected changes to your electricity bill.

We're also updating our connections policy to ensure our charges remain fair and easy to understand. This policy covers our proposed approach to charging new customers who want to connect to our network. This influences our investment plans, so we're asking for your feedback on this with our draft proposal.

We encourage you, our customers and stakeholders, to review our draft proposal and connections policy and give us your thoughts and feedback.




Visit:

talkingelectricity.com.au/contact-us
to provide feedback to us.

You can submit feedback on our draft proposal and connections policy through the contact form provided on our Talking Electricity website.

We welcome all feedback or questions, no matter how long or short.



What's next?

We'll incorporate your feedback as we continue to develop our regulatory proposal.

We'll also work with key stakeholders through a series of 'deep dive' workshops to discuss our draft proposal in more detail. These workshops will focus on our key investments, and help ensure our proposal meets your needs.

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We want you
to choose
your energy
future



We've asked you what you want

In today's rapidly changing energy market there's never been a more critical time for us to understand and respond to your needs. We want to move beyond simply telling you what we're doing, to ensuring our proposal delivers what you want. This will allow us to anticipate and respond to your changing preferences, support your energy choices, and provide better solutions.

We've been talking to you about the development of our 2021–2025 regulatory proposal since early 2017. Over the last 18 months, we've spoken with 5,000 of our customers who provided valuable insights on their energy needs. We've also worked together with the other Victorian distributors, particularly on reforms to our network charges.

Throughout our engagement activities, we've shared your views with our longstanding Consumer Consultative Committee. This Committee was first established over 10 years ago to provide an independent voice in our decision making process. Similarly, we invited members of the AER's Consumer Challenge Panel, and our Energy Futures Consumer Advisory Panel, to independently review our engagement approach and provide guidance.

You can read more about our stakeholder activities and customer insights on our Talking Electricity website.



We've been talking to you about our regulatory proposal since early 2017

Who we spoke with

- Residential customers
- Small and medium businesses
- Commercial and industrial customers
- Energy industry experts
- Community opinion leaders
- Retailers
- Energy Consumers Australia
- Councils
- Universities
- Demand management proponents



How we engaged them

- Interviews
- Focus groups
- Deliberative forums
- Surveys
- Talking Electricity website
- Public workshops



What we discussed

- Our shared energy future
- Energy values and preferences
- Role of the distributor
- Our value propositions
- Various business options
- Network tariffs
- Demand management opportunities

You've told us your energy future

Our discussions with you so far have focused on our shared energy future. This included your views on the likely take-up of new technologies, the possible impacts of government policy, and expected customer behavioural responses. A snapshot of these views is shown below.



Customers expect to see
more renewables
in their homes or businesses



Around one third
of customers plan to
install solar
during 2021–2025, helped
by government subsidies



The take-up of
batteries
is expected to increase
as rooftop solar grows

Electric vehicles

will eventually be part of our
transport and energy system



As the size of our network grows,
**timely and
efficient**
connections are a must



Customers want
**access to
real-time data**
on their energy use



Customers
want energy to be
affordable



Everyone should have a
**reliable
electricity supply**



Customers want us to
prioritise safety
when planning our asset replacements

Customers are finding
ways to use energy more
**efficiently
to save money**



Around half our customers are interested in
**rebates for reducing
electricity demand**



Customers want
**savings for
shifting use**
to off-peak



What we've heard and what we're doing

We've heard three common themes in our discussions with you. You've told us you want flexibility to choose how you use electricity, a dependable and safe network, and an affordable price. We've used these themes, which reflect your views and preferences, to develop a set of outcomes that our draft proposal will deliver.

These outcomes represent how we'll deliver value to you, and include 'business-as-usual' investment, as well as the investment required to develop a more flexible network that supports your energy choices.

We've heard...


We're doing...



We'd like to know more about your preferences...

1. We'd like to test if we've heard you correctly. Does a safe, dependable, flexible and affordable supply of electricity reflect what you want? Have we missed any key themes that are important to you?

Visit talkingelectricity.com.au/contact-us/ to have your say.



Every day we supply
your household
and business with
electricity to power
your activities

A safe and dependable supply of electricity is critical each and every day.

We all use electricity to keep our food fresh, and light, heat or cool our homes. We all need electricity to operate the plant and equipment at our offices or businesses to create jobs and grow our economy.

As your electricity distributor, we take great pride in the role we play in providing an essential service for our communities. How we manage our poles and wires impacts your lifestyle and the economy, so we follow international best practice. This includes measuring outcomes you value, so you can be confident you'll have electricity when you need it at an affordable price.

Our investment in the period from 2021–2025 to maintain a safe and dependable network represents a major part of our total works. This is because our network is complex and covers such a densely populated area.

An overview of our forecast investment to replace existing assets across our network in the 2021–2025 period is shown in the next column. These investments are further discussed in this section, and include increases to address new safety concerns.

Our investment decisions to replace assets in the next regulatory period are increasingly relying on smart technology and data analytics. For example, we're currently partnering with a number of universities across Australia to identify better ways to manage our assets. This helps us to make data-driven decisions to replace our poles, wires and major electrical plant inside our zone substations, and to identify and resolve safety hazards before they occur.

To ensure we continue to supply your household and business with electricity to power your activities, we commit to providing a:

- safe environment for our customers and workers
- reliable supply of electricity.

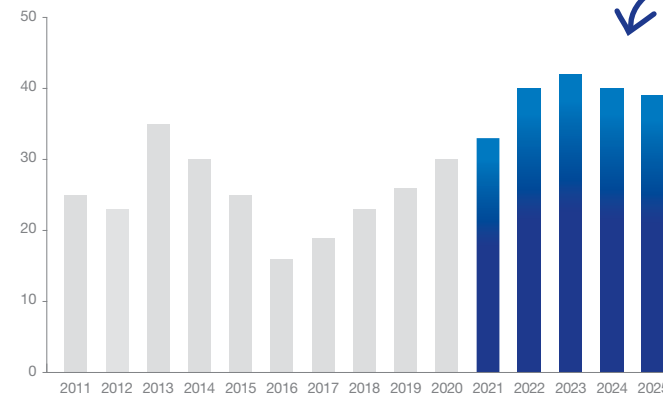
Our network reliability is measured by:

- Frequency and duration of outages across our network (minutes off supply per customer per annum)
- Network resilience in extreme weather (number of faults)

Our network safety is measured by:

- Number of public and workplace safety incidents
- Number of fire starts from our assets
- The condition and health of our assets

Forecast investment to replace existing assets
(\$ million, 2020 dollars)



Our investment is increasing to address new safety concerns, and to maintain reliability as our network ages

We're committed to providing a safe environment for our customers and workers

Your safety, and that of our workers, is our first priority – we never compromise on safety.

Our workers are extremely well trained, and follow best practice safety management to protect us all. This includes a strong culture of reporting all safety incidents (including near misses), no matter how small, so we all continue to learn and improve our processes.

We've also embraced technology to provide better ways to proactively ensure the safety of our workers and community. This follows the increased availability of data about our network since the introduction of smart meters in Victoria in 2009.

In particular, we've established a data analytics team within our business to help further improve the safety of our network. Our innovative use of data analytics provides both a safer and more affordable network.

Notwithstanding our preventative measures, some network assets will still fail on occasion (largely due to extreme conditions) and may pose a safety threat. We undertake a range of activities to reduce the impact should an asset fail. This includes enclosing assets in protective covers and maintaining safe distances between our assets and the community.

A selection of the safety-driven investments included in our draft proposal is shown below:

- \$2 million to remotely test and replace deteriorated 'neutral earthing' at your home and on our network. Deterioration may result in mild tingles when you touch your taps, or in rare circumstances more serious injury.
- \$6 million to test and replace service cables connecting your home to our powerlines. A component of these cables includes a protective covering that can degrade in certain conditions. However, instead of just replacing all service cables, we're using data analytics to select particular at-risk cables.
- \$14 million to continue repairing old underground pits that provide access to our electrical assets in Melbourne's CBD. The condition of some of these pits is deteriorating due to water ingress and heavy traffic.

Another safety program we discussed during our stakeholder forums is relocating selected powerlines around traffic 'black spots'. We haven't included specific investments for this in our draft proposal, but instead, we'll continue to assess the value of any relocations in our day-to-day works.

When developing our investment plans for major plant and equipment, we also place a value (or a benefit) on reducing safety and environmental risks. This approach embeds safe outcomes in all our investment decisions.

Our work with universities helps to improve our network

In partnership with Swinburne University, we're researching new technologies to inspect our assets with non-destructive methods. Non-destructive methods support the integrity of the existing asset during the inspection process, and are expected to provide more accurate information on asset condition.

We're also working with other research partners to leverage data we already collect in managing vegetation around our lines to improve safety outcomes. Our other research projects include termite treatment trials to identify more effective wood pole treatment alternatives.

Identifying and implementing new ways to solve network problems leads to safer, more reliable and affordable networks.

We're committed to providing a reliable supply of electricity

We know from talking to you that network reliability is important. Therefore, we regularly inspect and record the condition of all our assets:

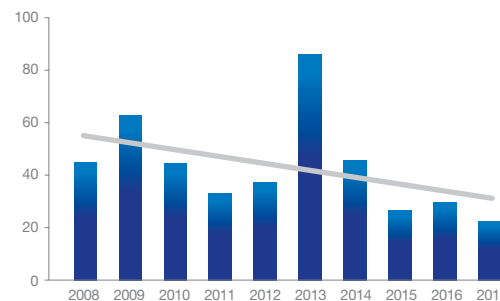
- assets are inspected at least every five years
- for assets in declining condition, more frequent monitoring is scheduled
- if the condition warrants, assets will be removed, repaired or replaced.

We use a range of inspection techniques such as drones, laser technology and traditional field crew inspections. These inspections drive our \$51 million pole and line replacement program over the 2021–2025 period.

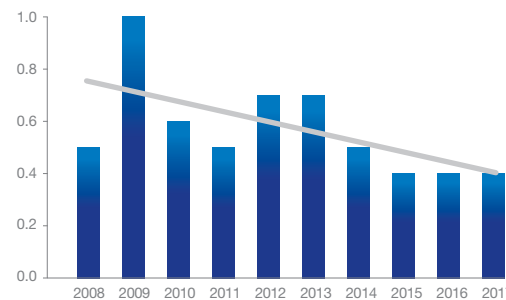
Overall, the investments outlined in this draft proposal are designed to maintain both affordability and the long-term health of our electricity assets. This includes investments needed to maintain current reliability levels on average across our network (we note that factors such as the weather will still drive variances each year).

In practice, however, we'll work to improve reliability where you value the improvement more than the cost to deliver it. As shown, we've been improving our reliability and will strive to maintain this trend. Activities we've undertaken to improve reliability include installing additional switches and monitoring devices. When there is an electricity outage, this equipment helps us restore your supply more quickly by remotely identifying and segmenting fault locations for our field crews to attend.

Unplanned outages a typical customer experiences (minutes)



Unplanned outages a typical customer experiences (number of)



We'd like to know more about your preferences...

2. Our planned investments are designed to maintain reliability for the average customer. We will not receive funding to improve service levels for customers who currently experience lower than average reliability. Are there alternative ways to better support these customers, rather than continuing to make compensation payments for frequent or extended outages?
3. Our use of data analytics supports our risk-based approach to resolving safety outcomes (e.g. only targeting selected assets to be replaced, so as to responsibly balance risk and affordability). Do you support the specific replacement investments we identified?

Visit talkingelectricity.com.au/contact-us/ to have your say.

We're preparing
the network to
be flexible to your
energy needs



You're changing the way you use, store and sell electricity.

Rooftop solar is already well established, and as the price of technology falls, the take-up of batteries for your home is forecast to increase. Likewise, electric vehicles are expected to become increasingly affordable, meaning you may use more electricity in the future.

Electricity demand during peak periods is a key driver of our investment requirements. As part of our stakeholder engagement, we held a forum to explore future electricity scenarios. We asked you about your current and future energy use, and the role of new technologies.

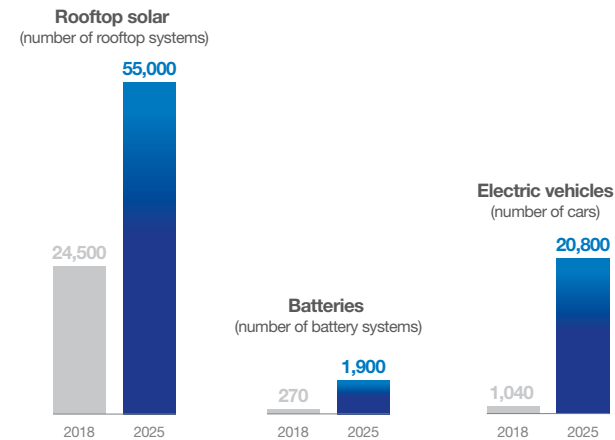
Our forecasts for peak demand from 2021–2025 are shown below.¹ These forecasts are consistent with the scenario you considered most likely, where existing solar and battery trends continue at a similar pace to today. These assumptions are consistent with forecasts provided by the Australian Energy Market Operator (AEMO).²

You also told us we should be taking steps to prepare for a future driven by increased solar, batteries and electric vehicles. These technologies provide you with opportunities to minimise your spend on electricity, for example, by offsetting your usage or feeding surplus electricity you generate back into the network for others to use – and be paid for this. Supporting this, CSIRO forecast that electricity customers will have access to demand response markets worth over \$2.5 billion per annum by 2050.

Over the next regulatory period, we'll invest to allow you to benefit from this transformation. We propose to make it easier for you to:

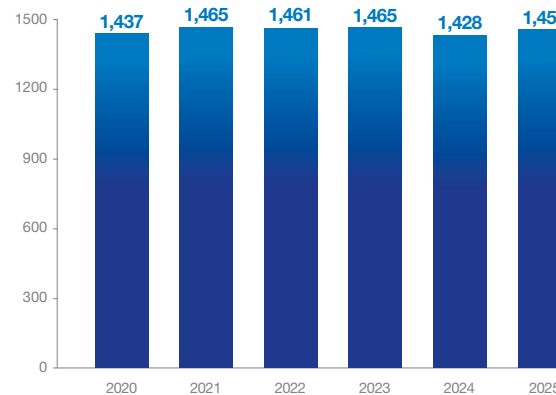
- make new connections to our network
- export solar and use batteries
- use your data to make informed energy choices.

Forecast take-up of new technologies



Use of solar, batteries and electric vehicles will continue to rise

Peak demand forecast (MW)



We expect peak demand to increase by 0.4% each year in 2021–2025

Source: AEMO

¹ These forecasts will be updated for our regulatory proposal to include the most recent data.

² AEMO is an independent body responsible for the administration and operation of the wholesale national electricity market.

We're making it easier for you to export solar and use batteries

When you use solar panels to generate electricity, you may want to export any surplus to your own needs back into the electricity network. This allows you to receive payments for any excess electricity you generate. You could also choose to sell your excess electricity when the network is overloaded, or when the supply of electricity is tight, through the use of batteries.

When multiple customers in the same community or region export electricity at the same time, the amount of electricity pushed into our network may go beyond what it can handle. This is because our network was originally designed to transfer electricity only in a single direction (i.e. from centralised generators to end-use customers). An overload may only occur at limited times during the year, but can cause costly network damage.

Solar and battery use may also result in high voltage levels on our network. We supply electricity to your home or business at around 230V. When solar and battery use increases – for example, as more customers install these systems – we need to manage any corresponding voltage rises, as these can cause wear and tear on your household appliances or cause them to fail.

To avoid damaging our network, or your appliances, one option is to limit customers from exporting their excess solar energy. We recently asked customers if they felt we should limit solar exports and they said 'no'. We don't believe this is the best solution either, because it hampers your ability to take control of your electricity bill – we want you to get the most out of your solar and batteries.

Investing in our network to enable solar and batteries

To give you more choice in how you use, store and sell electricity, we'll invest \$15 million on network improvements. This includes re-balancing the number of customers connected to each network asset, installing devices to manage voltage rises, and installing new assets that can accommodate more exports. This investment is underpinned by our data analytics team – using smart meters, we've been finding the 'hotspots' in our network and determining the lowest cost solution to address them.

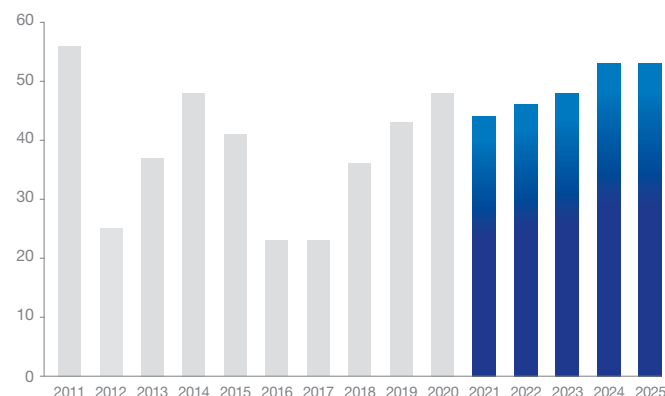
There may be occasions when we still need to limit exports to avoid network damage and maintain the safety of our electricity supply, but our solar enablement investments will allow us to minimise the time of these export limits. In this way we may limit exports for minutes, rather than permanently throughout the full peak period.

The impact of solar and battery growth is included in our forecasts of peak demand on our network. This means solar and batteries are considered as alternatives to constructing more poles and wires. We also manage demand by publishing details of all major investments in advance of any construction activity. This provides an opportunity for stakeholders across our network to propose alternative, lower-cost solutions.

This combination of approaches is the most cost-effective way to accommodate your export needs now and in the future. New standards for solar installations are also helping to reduce the need for network investment.

Our forecast investment to accommodate growth on our network is shown below.

Forecast investment to accommodate growth
(\$ million, 2020 dollars)



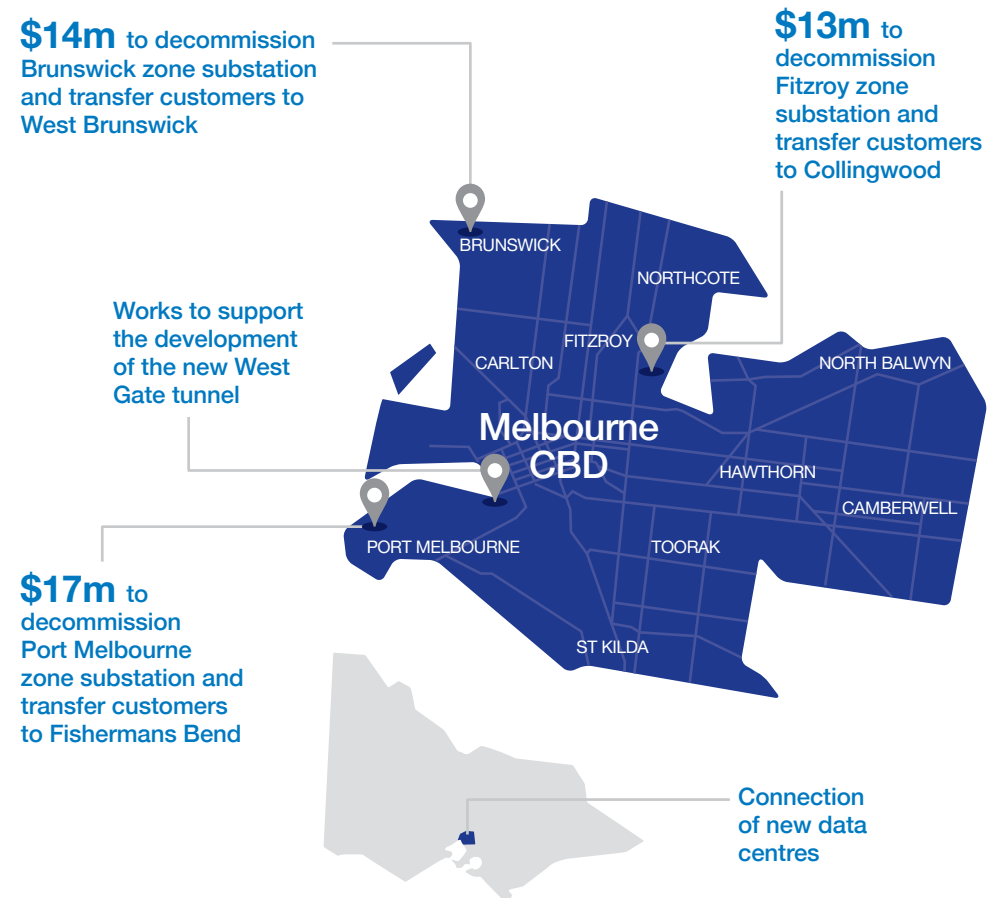
Our investment forecast includes our program to decommission our 80-year old sub-transmission network

We're making it easier for you to connect

Connecting to a network is the first step that you take as an energy customer to receive electricity. Every year, we connect over 4,000 new households, businesses and generators.

We need to ensure our network can accommodate this growth. This includes continuing our program to decommission zone substations connected to our 80 year old sub-transmission network (in the Port Melbourne and Brunswick areas), and to move the supply for existing customers to alternative zone substations. This is cheaper than simply replacing the ageing sub-transmission network and then undertaking separate upgrades to supply new customers.

Our investments also support major infrastructure projects that help grow the Victorian economy. A selection of our key projects is shown.



Connection process and charges

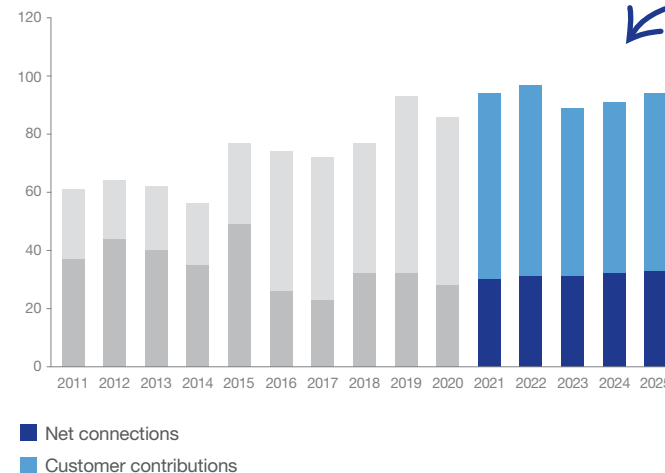
We'll continue to invest in our business processes so we can connect all new customers more easily and quicker than before. For example, we've recently introduced our online eConnect and mySupply platforms to remove the need for paper forms. Putting the connections process online allows us to easily track the progress of your connection request, and ensure we provide accurate cost estimates. Most importantly, it saves time and effort for you or your electrician.

Another focus is continuing to reduce connection timeframes. For large customers, we've committed to complete our construction works within 26 weeks. For the majority of residential customers, we'll connect your house within 10 days.

You also asked us to ensure our connection charges remain fair. That's why we're consulting with you on our connections policy as part of our draft proposal. Our connections policy covers our proposed approach to charging new customers who want to connect to our network. This may include requiring larger new customers to contribute some of the cost of network upgrades needed to support their connection.

Our total forecast connections investment is shown opposite. This chart separately shows the investment funded directly by those customers who make a connections request.

Forecast investment to connect new customers
(\$ million, 2020 dollars)



Our connections investment is increasing with Victoria's economy, particularly as we continue to support major infrastructure programs

We're making it easier for you to use your data to make informed energy choices

The electricity industry is becoming more complicated. You're being asked to choose between hundreds of retail offers, whether to install solar and batteries and what time of day to use electricity to reduce your bill.

Now, more than ever, data on your energy usage can help you make these decisions. You've told us you want better access to this data, and you'd like us to help you make better use of it.

Enabling our customers

To support you in making more informed energy choices, or for you to choose whether you want third parties to use this data to tailor services to your needs, we'll develop a single system or one-stop-shop to access your electricity usage data and connection requests. This will remove the existing need for separate account details across multiple online portals.

Our new system will continue to pre-populate your data into the Victorian Government's retail price comparison website to help you manage your bills. Additionally, it will:

- provide easy access to the status of your connection requests, including through web-chat facilities
- show you that your rooftop solar system is performing well or not
- show you if your appliances are using a lot of electricity
- notify you about electricity outages, and provide a simple way for you to report network faults.

Implementing this system will require an investment of around \$2 million.

More data, more often

New regulations are coming into effect that require us to remotely read your electricity meters every five minutes. This will enable us to provide you with your own electricity use on a five-minute basis so that you can better control how much electricity you use.

Our required investment to meet these new regulations is \$14 million, and will start in 2021. This includes the need for a six-fold increase in the capacity of our communications network. The Australian Energy Market Commission determined that reading meters this frequently will reduce everyone's electricity bills over the longer term.

Keeping your data secure

Unlike in other states, Victorian customers' electricity use is measured by smart meters. These meters have a number of advantages over traditional meters, including:

- automatically notifying us of electricity outages so we can restore your power earlier
- enabling you to view your electricity use in 30-minute intervals (or in the future, five-minute intervals) – this can help you select the best electricity retail offer or understand and manage your household's electricity use
- supporting fairer charges and enabling you to decide when to export excess solar energy or to receive benefits for saving electricity
- allowing us to monitor the quality of electricity supplied to you, which can impact the health of your household appliances and equipment
- providing us with more information about the performance of our assets leading to improved safety outcomes and better targeted asset replacements.

With all this data, which will continue to grow over time, security is clearly important. As recognised by the Australian Cyber Security Centre, malicious cyber activity against Australian organisations and businesses is increasing in frequency, scale, sophistication and severity.

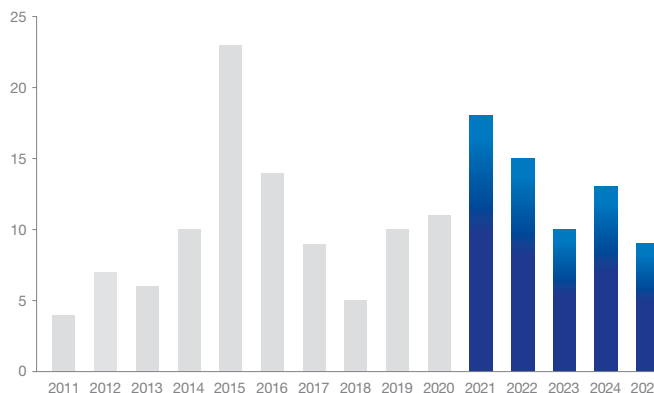
Our draft proposal includes \$8 million to keep pace with our data security needs. We'll use this to put new security measures in place to ensure we can respond quickly if there is a threat to our network.

Our IT investment provides the building blocks for a flexible network

The above investments are all part of our information technology (IT) requirements. These are necessary as we become an increasingly digital network that is better able to service your needs.

Our total IT investment is also driven by the need to periodically upgrade existing business-as-usual systems – from 2023, for example, we'll invest \$7 million to modernise our SAP system that was originally installed in 1996. This system supports our entire business, including managing the network programs and daily corporate functions.

Forecast investment in IT
(\$ million, 2020 dollars)



We'd like to know more about your preferences...

4. We're investing in technology and data services to support your energy choices. How important are these services to you?
5. What other information about your electricity use or our network can we provide to support your energy choices?

Visit talkingelectricity.com.au/contact-us/ to have your say.

The increased investment in 2021 and 2022 is driven by new compliance obligations



We're maintaining
affordability by
keeping our
prices low

We know energy affordability is a major concern for you.

You've told us you expect access to cheap and reliable electricity. As cost of living pressures continue to challenge us all, we'll keep delivering a safe and dependable electricity supply while keeping our prices low.

This proposal allows us to reduce our revenues in 2021. As shown in the table below, this reduction is followed by four years of no real revenue increase. We're interested in your views on this revenue path – an alternative, for example, could be to smooth changes more evenly across the regulatory period.

Our revenues are falling in 2021

| Year | 2021 | 2022 | 2023 | 2024 | 2025 |
|----------------|-------|------|------|------|------|
| Revenue change | -4.6% | 0% | 0% | 0% | 0% |

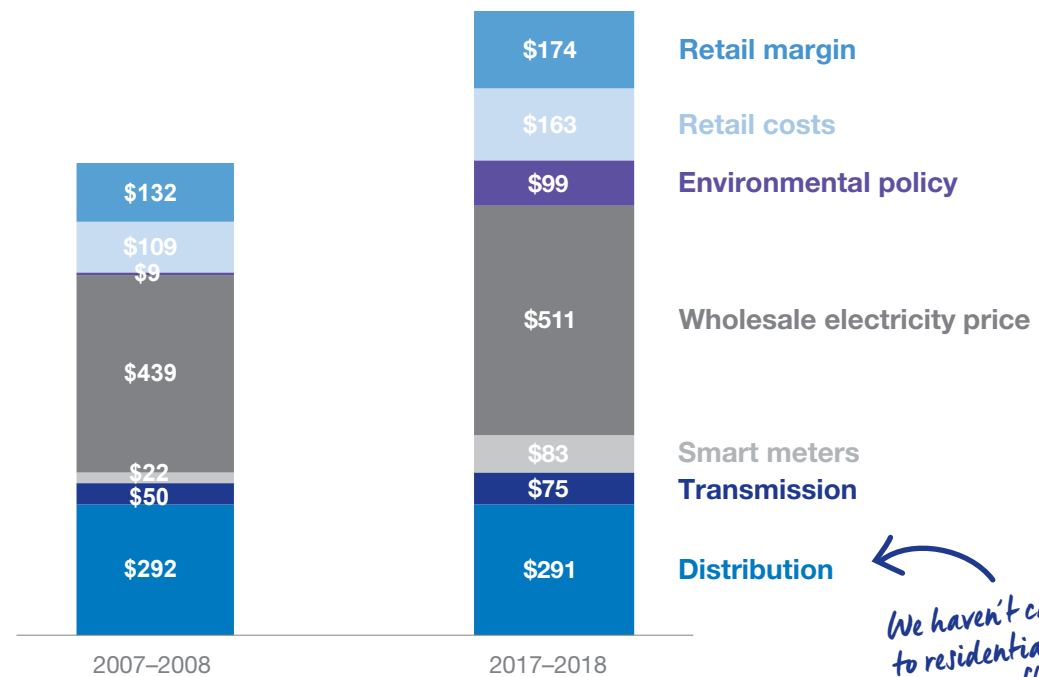
Our revenue changes will contribute to a total reduction in average network charges in 2021 of \$25 for residential customers and \$94 for business customers. Network charges are the component of your electricity bill that we control, and in total, also include the reduction in our metering charges and expected growth in customer numbers.

Our prices have remained stable since 2007

Keeping our prices low continues our trend of real price stability over many years. For example, the Australian Competition and Consumer Commission's recent report on retail electricity prices showed that average network costs in Victoria (excluding metering) have not increased in real terms for over a decade. In 2007–2008, our average network costs were \$292 and have declined in real terms in 2017–2018 to \$291.

Our charges are also among the lowest in Australia.

Average CitiPower household electricity bill composition (2020 dollars)



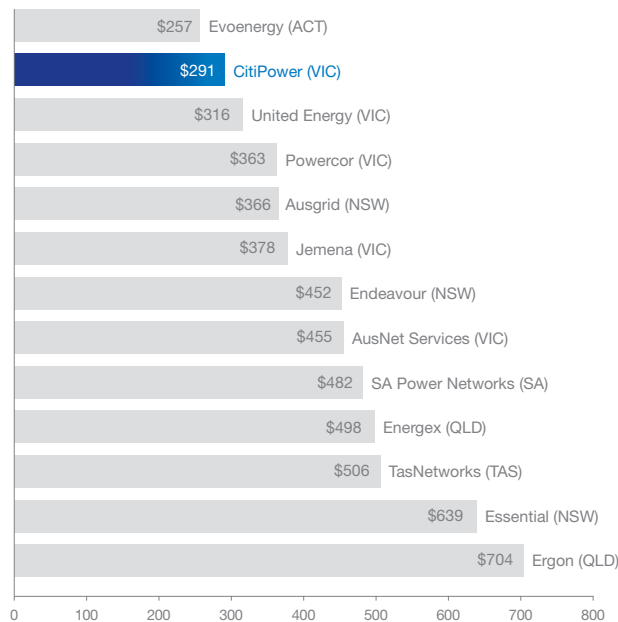
Source: Chart and table adapted from ACCC analysis to reflect our network circumstances on a per customer basis

We haven't contributed to residential bill rises. We're more affordable than we were a decade ago.

We're one of the most cost-efficient distributors in Australia

Our charges are among the lowest in Australia

How we compare – distribution charges across Australia (2020 dollars)

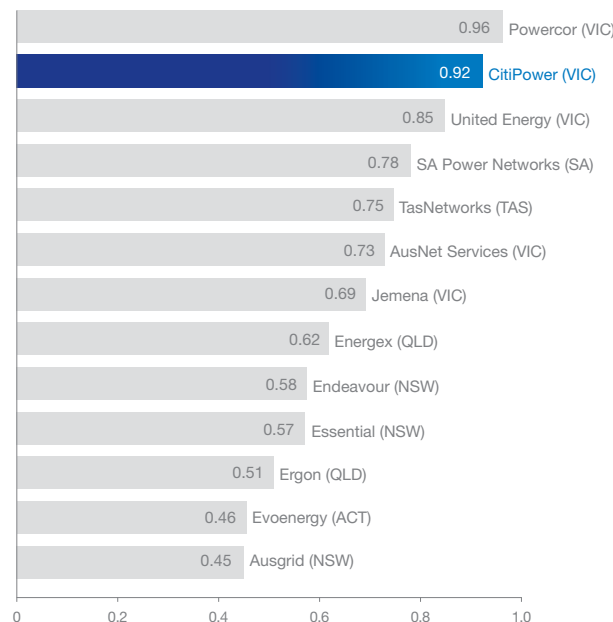


Note: Excludes metering costs

We benchmark better than other distributors

The evolution of new energy markets means we must remain relevant with competitive services. The AER's independent benchmarks show we're among the most cost-efficient distributors.

Operating expenditure productivity index (2006–2017)



Source: AER data

We have an agile employment structure

One of the key ways we deliver you value is through our flexible employment practices. Most of our design and delivery staff are directly employed by us – we're major employers in our communities. However, we also use some external resources to enable us to quickly ramp up or down our workforce to match our capital works program. This means we're not stuck with high fixed costs, or an inability to deliver projects fast enough.

We've also invested in systems to efficiently allocate work to our field teams. This reduces downtime between jobs, and allows us to get to more jobs on time.

We market-test contracts to get better rates

Where our internal workforce can't provide services, we market-test contracts to ensure we get the best deal. This includes our vegetation management program.

When we last renewed our vegetation management contracts, we structured the tender process to ensure as many parties as possible could participate. Our approach has led to ongoing annual savings of around \$1.5 million, which enables us to keep our costs low. At the same time, we're now managing more spans than ever before.

We balance capital and operating investment decisions

We pay close attention to the immediate price impact of all our investment decisions. Operating investments may have immediate price impacts, but provide flexibility to respond to the future state of electricity markets as they evolve.

Alternatively, capital investments can balance affordability concerns. Capital investments generally have only a small impact on our prices because the investment is recovered over the life of the assets, and our assets typically last for a long time. For example, a \$1 million capital investment equates to less than 13 cents per customer.

Incentives

The regulatory framework we operate under provides incentives that allow us to earn extra benefits if we outperform benchmarks the AER sets for us. These benchmarks are continually reviewed by the AER, so our performance must continually improve too.

Ultimately, you benefit from these incentives through lower prices – when we outperform our expenditure targets (i.e. if we come in under budget), you receive approximately 70% of the benefit. For the 2016–2020 period, we expect you'll benefit from around \$210 million in total realised savings.

Our prices are based on well-established approaches

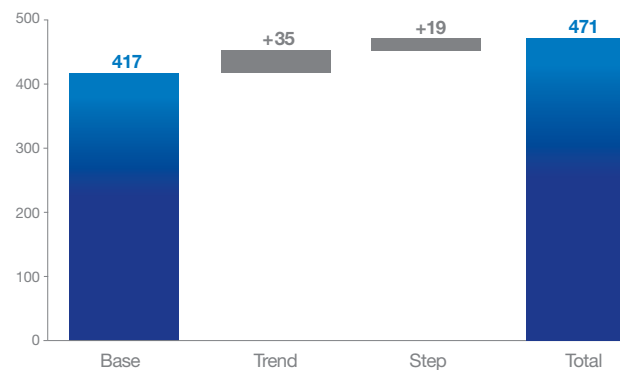
In developing our investment requirements for the period from 2021–2025, we've tried not to reinvent the wheel. Instead, where practical, we've used well-established processes. This includes adopting the approaches already used by the AER when it assesses the efficiency of our forecasts.

Operating expenditure – consistent with the AER approach

We need to maintain our assets and run our business on a day-to-day basis. These costs, for example, cover our ongoing maintenance programs, vegetation management, fault response, our corporate staff and many vital customer support services.

Consistent with the AER's longstanding practice, our operating expenditure forecasts for the 2021–2025 period have been developed using a 'base, trend and step' approach.

Forecast operating expenditure
(\$ million, 2020 dollars)



Representative base year

The costs of running our daily operations for a recent year are a reasonable starting point for forecasting our future expenditure needs – particularly given we benchmark among the best of all distribution networks from an operating cost perspective. When we finalise our operating expenditure forecasts, 2019 will be our most recent 'base' year with audited data.

Forecast trends

Our operating costs take account of expected trends, including likely increases in labour and contract prices. These trends are based on independent benchmarks or known price changes, which show the cost of these services will increase at a rate greater than inflation.

Our operating forecasts are also scaled to reflect growth in the size of our network (e.g. as customer numbers increase, so will our work volumes).

Step changes

We adjust our base year for significant changes we know will occur during the 2021–2025 period. These 'step' changes may increase or decrease our operating costs. Often a step change is needed so we can meet new legislation that changes our operational requirements – we must comply with these obligations. We also include changes where we switch to using operating instead of capital expenditure (e.g. where we start leasing services).

The list of step changes we expect to include in our regulatory proposal is shown opposite. These changes are particularly important for our business, given our lean operating structure – as highlighted in the AER's benchmarking analysis on page 24. That said, we haven't sought to capture all likely cost increases, as we've heard your concerns regarding affordability. Instead, we'll keep costs low by improving our everyday productivity.

Proposed step changes (\$ million, 2020 dollars)

| Proposed step change | Forecast operating investment | Deferred capital investment |
|--|-------------------------------|-----------------------------|
| New regulatory obligations related to market changes | 12.6 | N/A |
| New regulatory obligations related to safety and environment | 1.4 | N/A |
| Expenditure trade-offs | 4.7 | 9.5 |

Rate of return – consistent with the AER approach

We earn a return on the value of our assets. This return is a large driver of the total revenue we receive – equal to approximately 37% – and accordingly, is subject to a rigorous review by the AER.

The AER has recently completed its review of the rate of return. We participated in this review process and have accepted the AER's final decision. At approximately 5.7%, the AER's rate of return is at an historically low level.

Depreciation – consistent with the AER approach

When we build our network – for example, our poles and wires – these assets can last for up to 50 years. Therefore, we only recover a portion of the costs of our assets in any given year.

This approach is consistent with well-established accounting practices. It is also consistent with the AER's methods.

Tax – consistent with the AER approach

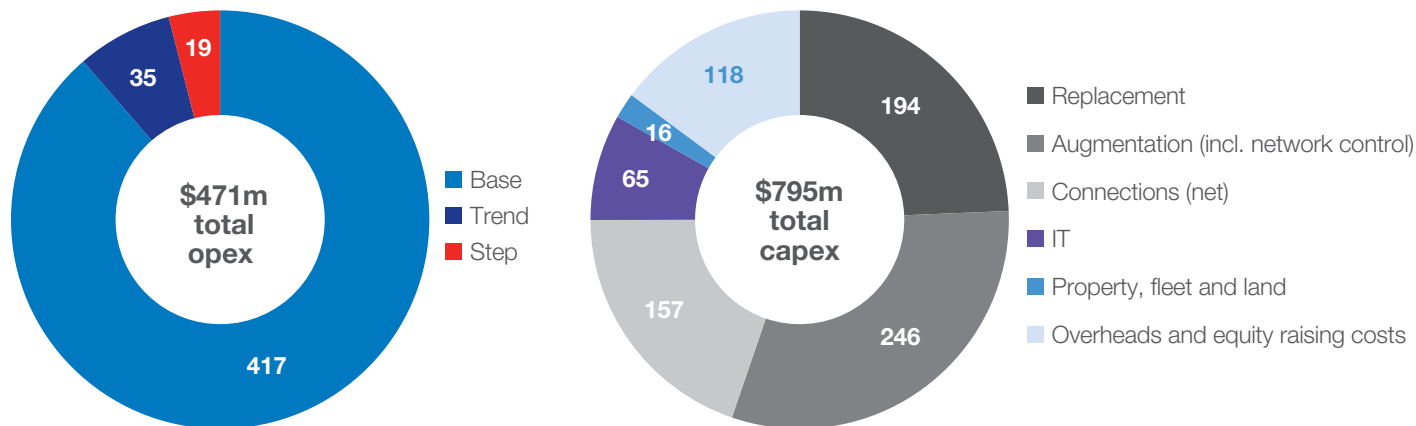
The AER provides an allowance for tax based on a benchmark firm. This recognises that all distributors incur tax liabilities as they operate their networks.

We have applied the AER's taxation approach, as set out in its final report in December 2018 on estimating corporate tax costs for regulated energy networks.

Our total investment forecast is prudent and efficient, and will keep our prices low

Our total investment forecast discussed in this draft proposal is used to set the total revenue allowance we propose to recover from our customers. A summary of this investment is provided below.

Forecast operating and capital investment for 2021–2025
(\$ million, 2020 dollars)



We'd like to know more about your preferences...

6. We've heard from you that affordability is a primary concern, and this has been reflected in our capital and operating investment forecasts. Have we struck the right balance between flexibility, safety, dependability and affordability?

Visit talkingelectricity.com.au/contact-us/ to have your say.

The background image shows a long wooden pier extending into a body of water at sunset. The sky is a mix of deep blue and orange, with scattered clouds. The pier is lit with warm yellow lights, and a small building with a sign that says "Pier Hotel" is visible on the pier. A large, semi-transparent blue circle is overlaid on the left side of the image, partially obscuring the pier and the sky. The text "We're supporting your energy choices through fair and simple charges" is written in white, sans-serif font across the upper right portion of the image, enclosed in large, light blue quotation marks.

We're supporting
your energy choices
through fair and
simple charges

We've designed our price structures to be fair and easily understood

Our aim is to set simple and fair price structures for electricity, so we've been working with the other Victorian networks to design consistent price structures for residential, and small and medium business customers throughout the state. We've also held two separate customer forums, but we want to hear from more of you before settling on the final price structure for our network.

Based on your feedback so far, we've narrowed the price structure options for residential, and small and medium business customers to those set out below.

Our aim is to set simple and fair price structures

| Price structure | Description |
|---------------------|--|
| Time of use | The price of the electricity changes throughout the day. It is higher at peak times and lower at other times. |
| Peak usage packages | The charge for your package would be the same each month based on your level of electricity use at peak times. |
| Demand | Your monthly charge would be based on your maximum electricity demand at peak times for that month. |
| Status quo | Your price structure would not change. Most customers are currently charged a fixed daily rate plus a charge for electricity use that varies with how much you use each day. |

We believe these new price structures are fair because:

- you can make savings if you're able to change the time you use electricity (e.g. by setting your dishwasher and washing machine timers to operate outside peak times, or even using a battery to store electricity for later)
- customers who use a lot of electricity at peak times pay for the costs they impose on the network – this is fairer than charging other customers the same amount when their electricity use has less impact on the network
- by encouraging you to change the time you use electricity, we can build in less capacity to the overall network and lower everyone's charges.

We're also interested in your views on how quickly we should move towards these pricing structures. Each of our customers is assigned a pricing structure by a retail electricity business. The sooner customers are assigned to a new pricing structure that provides an incentive to move usage away from peak times, the sooner network cost savings will be realised. However, this may come at the expense of some individuals in the short term. The pace of change will depend on whether all customers are assigned to a new pricing structure by default (unless they opt out), or whether new structures only apply to customers who opt in.

We've published a consultation paper with more detail on our price structure options. This paper is available on our Talking Electricity website.

Large business and industrial customers

We'll continue to adopt a 12-month rolling kVA demand charge structure for large businesses and industrial customers, where demand is measured in 15-minute intervals. Our commercial and industrial customers have been charged based on their demand for a number of years, so most understand this pricing structure well.

Following in-depth interviews with our larger customers, pricing options that reward customers for reducing demand at network peak times are being considered. Options include rebates or replacing the current fixed charge with a network peak pricing signal.

We've also heard that measuring demand over 30-minute intervals would allow some large customers to better manage their demand charges. Although this would lower bills for some large customers, it will increase them for others (as our total revenue is fixed). We're interested in hearing from more of you on this issue.

We charge you for what you use

We offer services that are complementary to our role of ensuring a safe and reliable electricity supply. These services include those related to smart meters or street lighting, and responding to requests from customers who require new or additional work (e.g. connecting a new home).

For these services, we have either an ongoing annual charge or one-off fees for customer-requested services. The full list of proposed fees and charges for the 2021–2025 period will be published in our regulatory proposal.

Metering

We own and operate all smart meters and the metering communications infrastructure for residential and small business customers. The cost of managing the meters is recovered from all customers.

Our metering charges are expected to fall during 2021–2025. In 2021, for example, we'll reduce our charges by around 10%.

Ancillary network services

Ancillary network services include all requests from customers who require work on the network, such as turning electricity on and off, or connecting a new home. Customers who request the service pay the cost of providing that service. There are approximately 20 services we offer upon request. Our fees for ancillary network services during 2021–2025 will be based on the expected costs of providing that service.

Street lighting

We maintain and repair street lights that are directly connected to our network (more than 90% of all street lights). The lights themselves may be installed and operated by local councils or VicRoads.

We charge the councils and VicRoads for maintaining each light. These are based on actual costs, where the cost of maintaining energy-efficient lights is lower compared to older light types. We expect the overall cost of maintaining street lights to fall during 2021–2025, as during this period most existing lights will be replaced with efficient lights.

We'd like to know more about your preferences...

7. Which pricing structure best balances affordability, fairness and simplicity?
8. Do you think all customers should be assigned to new price structures by default (unless they opt out), or should they only apply to customers who opt in?
9. Would you be willing to change the way or time you use electricity every day if you could receive a saving from doing so?

Visit talkingelectricity.com.au/contact-us/ to have your say.



Help shape your energy future

You can submit feedback on our draft proposal and connections policy through the contact form provided on our Talking Electricity website. We welcome all feedback or questions, no matter how long or short.

Visit:

talkingelectricity.com.au/contact-us
to provide feedback to us.