



# Yarra Trams

**CP RRP BUS 9.02 - Yarra Trams - Dec2020**

**Revised regulatory proposal 2021–2026**



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# 1 Summary

## 1.1 Summary of our revised proposal

In our revised proposal, we repropose the incremental operating expenditure related to the relocation of our assets on Yarra Trams poles, with the following changes from the original proposal:

- we are proposing the expenditure as a category specific forecast, rather than a step change. This addresses the AER's and stakeholders' concerns that the cost of the program may be locked into the base year expenditure for the 2026–2031 regulatory period
- we have updated the volume of works based on confirmed work program provided by Yarra Trams, refer CP RRP ATT53. This includes a detailed list of Yarra Trams planned poles interventions for each year of the 2021–2026 regulatory period (and beyond)
- we have recalculated our unit rate based on a larger number of historical works, which has reduced the unit rate to \$14,808.

The volume of pole relocation works by Yarra Trams for the 2021–2026 represents a fundamental change in our operating environment outside of our control, which necessitates increased expenditure during 2021–2026 to meet the National Electricity Objective (NEO).

A summary of the Yarra Trams category specific forecast is set out in table 1 below.

Table 1 Summary of our proposed Yarra Trams category specific incremental expenditure, \$ million 2021

	Original proposal	Draft determination	Revised proposal
Incremental operating expenditure	12.7	-	4.8

Source: CitiPower

# 2 Background

## 2.1 Our original proposal for a Yarra Trams step change

In our original proposal we proposed a step change for the relocation of our assets on poles owned by Yarra Trams. Yarra Trams are embarking on a ten-year program of substantial tram track renewals and upgrades. As part of the program, Yarra Trams will be relocating or replacing some of their electricity poles that hold our pole-top assets and conductors.

To maintain reliability and safety of electricity supply to customers affected by the proposed Yarra Trams pole relocations, we will be required to relocate our existing assets onto the new or relocated Yarra Trams poles. Relocation of assets on poles forms part of our maintenance and repair operating expenditure. The proposed relocation program will therefore result in a material increase in our operating expenditure not captured in the 2019 base year.

Table 2 below summarises the original proposal Yarra Trams pole relocation step change expenditure.

Table 2 Original proposal step changes, \$ million 2021

Step change	2021/22	2022/23	2023/24	2024/25	2025/26	Total
Yarra Trams step change	2.8	2.8	2.9	2.9	3.0	14.4

Source: CitiPower

In a subsequent information request response, we had updated the forecast volumes of pole relocations in the step change model, resulting in the expenditure amount being reduced to \$12.7 million (\$2021).

## 2.2 The draft determination

In the draft determination, the AER did not accept our Yarra Trams step change. A summary of the AER's reasons for not accepting the step change is set out below:

- this is a single cost category variation and if included as a step change, it would result in a permanent increase to the base after the 2021–2026 regulatory period. It would be inappropriate to allow this as a step change as there is uncertainty of tram track works that Yarra Trams plan to conduct in the 2026–2031 period
- unforeseen increases in expenditure related to certain programs can often be funded as the cost of other programs and projects in the base year decline
- the expected increase in renewal and upgrade works by Yarra Trams and the corresponding impact for CitiPower is not a new or change in regulatory obligations nor is the proposal considering an efficient capital/operating expenditure trade-off.

The AER also expressed concerns about the efficiency of our blended unit rate.

# 3 Revised proposal

## 3.1 Updated Yarra Trams category specific forecast

### 3.1.1 Updated pole relocation volumes

Our revised proposal for incremental operating expenditure related to the relocation of our assets on Yarra Trams poles is based on an updated volume of pole relocation works. The volumes were provided to us in an official letter from Yarra Trams, refer CP RRP ATT53. This includes a detailed list of Yarra Trams planned poles interventions for each year of the 2021–2026 regulatory period (and beyond).

The table below summarises the volume of pole relocations Yarra Trams is planning on carrying out during the 2021–2026 regulatory period, for which we have pole top assets requiring relocation.

Table 3 Planned number of pole relocations works to be undertaken over 2021–2026

Forecast	2021/22	2022/23	2023/24	2024/25	2025/26	Total
Pole relocation volumes	179	110	204	122	107	722

Source: CP RRP ATT53 and CP RRP MOD 9.03

The average annual planned works represent a 123% increase on the volume of works undertaken in our 2019 base year. This represents a fundamental change in our operating environment outside of our control, which necessitates increased expenditure during 2021–2026 to meet the National Electricity Objective (NEO).

### 3.1.2 Updated unit rate

In the draft determination, the AER expressed doubt over the efficiency of our blended unit rate for the relocation works. We are confident our unit rates reflect the cost of an efficient and prudent service provider, for several reasons:

- we are the second most efficient distributor in Australia, behind Powercor that we also own and operate. Our operating expenditure efficiency has been well documented and evidenced through years of AER benchmarking reports and is well accepted as such by our customers and stakeholders. Our unit rates reflect the achieved efficiencies across the board
- we are subject to an incentive framework to which we have responded and continue to respond
- our private ownership structure promotes efficient expenditure
- we have the lowest operating expenditure per customer while continuing to provide a safe and dependable network that is available 99.99% of the time
- a large proportion of our operating expenditure is outsourced to external contractors who benefit from economies of scale
- our labour costs are efficient and competitively priced, and our corporate and field staff are strategically located across the network to minimise travel times and response times in emergency situations.

At the time of the original proposal, our unit rate was based on the number of jobs available for year to date in 2019. We have since updated our blended unit rate to include all jobs during 2019 and 2018, which has resulted in a lower unit rate due to inclusion of some lower complexity jobs. We believe the updated unit rate better reflects the full scale of job complexity and is more appropriate for forecasting future expenditure. Our updated unit rate is included in CP RRP MOD 9.03.

### 3.1.3 Revised proposal Yarra trams category specific forecast

The table below shows the forecast value of our category specific forecast for incremental operating expenditure related to Yarra Trams pole relocation works for each year in the 2021-2026 regulatory period.

Table 4 Summary of Yarra Trams category specific forecast, \$ million 2021

Forecast	2021/22	2022/23	2023/24	2024/25	2025/26	Total
Yarra Trams category specific forecast	1.5	0.4	1.9	0.6	0.4	4.8

Source: CP RRP MOD 9.03

### 3.1.4 Alternative option to relocating our assets on Yarra Trams poles

The only alternative to relocating our assets on Yarra Trams poles is to install a new distribution pole or underground the assets. However, in most cases where we hold our assets on Yarra Tram poles there are physical restrictions to having a distribution pole in the same space, leaving undergrounding as the most likely solution.

Based on previous works, we estimate the unit cost of moving assets underground to be around four times the unit cost of the asset relocation. This would result in a total capital cost of approximately \$40 million compared with the operating expenditure solution of \$4.8 million. However, at a high-level, the benefits of undergrounding our assets (i.e. more supply reliability or safety) would be less than four times the value of customer benefits under asset relocation. This is particularly because our reliability performance on our network is already very high, particularly in Melbourne's CBD. Additionally, if undergrounded, there is a corresponding large cost on customers to install their own underground service connections as a result.

As such, we consider the relocation of our pole top assets onto new or relocated Yarra Trams poles is an efficient operating/capital expenditure trade-off. The capital solution is higher cost without corresponding benefit, while there are significant complications of installing parallel poles due to the congested nature of infrastructure in the CitiPower network.

## 3.2 Relationship with the operating expenditure base and rate of change

The Rules require the AER to accept forecast operating expenditure where it reasonably reflects the prudent and efficient costs of achieving the operating expenditure objectives, and a realistic expectation of the demand forecast and cost inputs.

We do not consider the operating expenditure base and rate of change provide reasonable opportunity to recover our efficient costs associated with the Yarra Trams pole relocation program for the following reasons:

- our base operating expenditure is highly efficient as demonstrated by the AER's own benchmarking and we have no capacity to absorb these additional costs
- the rate of change being applied is the lowest in history, including a 0.5% productivity adjustment (equivalent to approximately \$6 million), nil real price growth for non-labour inputs and the lowest real labour price forecasts and output growth forecasts in over 15 years
- there are no commensurate reductions in cost pressures foreseeable in the 2021–2026 regulatory period This is not surprising as in our experience, the cost burden from obligations and regulations under which we operate only tends to increase, not decrease
- further there is no express materiality threshold under the Rules for the purposes of assessing whether operating expenditure should be included in the forecast. A materiality threshold is particularly irrelevant in our circumstances where our base operating expenditure is highly efficient, the rate of change is the lowest

in history and the impact of COVID-19 will result in higher costs for our operations due to changed work practices enduring beyond the next few years.

Please refer to CP RRP BUS 9.06 for more detail on our concerns with the AER's approach to considering incremental operating expenditure costs to be captured in the operating expenditure base and rate of change.