

20 October 2021



Dr Kris Funston  
Executive General Manager, Network Regulation  
Australian Energy Regulator  
GPO Box 3131  
Canberra, ACT, 2601

Dear Dr Funston,

## **DRAFT BETTER RESETS HANDBOOK – TOWARD CONSUMER CENTRIC NETWORK PROPOSALS**

Endeavour Energy appreciates the opportunity to provide feedback on the AER's draft Better Resets Handbook (the Handbook) that seeks to formalise a more customer-centric approach to regulatory determinations. This Handbook follows a period of increased focus on, and investment in, customer engagement following the 2013 Better Regulation reforms culminating in the 'New Reg' trial.

The objective of the Handbook is to incentivise networks to develop quality regulatory proposals through genuine engagement with customers. The benefits of engagement include an improved understanding of customers, reputational benefits and a targeted and proportionate review of a regulatory proposal. The Handbook promotes the pursuit of these benefits by providing a clear account of the AER's expectations on what constitutes good engagement and outcomes for key topics.

We are supportive of the draft Handbook and the AER's intention. It codifies many existing regulatory interpretations and practices and more clearly establishes what is expected of networks in developing a regulatory proposal. The shift towards a more customer centric approach to regulation is a welcome one and something that should be encouraged further.

The targeted review stream promoted by the Handbook involves a more intensive process pre-lodgement as opposed to the traditional propose-respond model prescribed in the Rules. It would be duplicative and resource intensive for networks and stakeholders to invest in extensive pre-lodgement engagement only for the proposal to then be subjected to a detailed technical review. If the AER's assessment approach builds off the outcomes of pre-lodgement engagement then networks and stakeholders will see the value in investing their time and resources in the process.

While standard assessment techniques may remain necessary where the customer engagement is poor, or fails to resolve a substantive number of matters, we consider the ideal should be an expedited formal review process where a proposal is well-justified and the product of a genuine and thorough engagement process.

It is also worth noting that the regulatory framework is complex and ever expanding. There are numerous requirements a regulatory proposal and supporting documentation must satisfy between the Rules, technical standards, industry notes, AER Guidelines and guidance notes (notwithstanding other Federal and Jurisdictional legislation). This Handbook provides a useful synthesis of how the AER applies these instruments and its judgement in practice when completing its regulatory task.

As noted by the AER, the Handbook works within the regulatory framework and in no way replaces or obviates any of the AER's or network's obligations in the regulatory determination process. It is important it be made clear that the Handbook is not a determinative instrument but rather is a set of expectations that seek to promote the more efficient application of the Rules. These expectations may

continue to evolve and whilst regulatory certainty is valuable there will need to be a flexible and pragmatic approach in applying the Handbook.

Our primary feedback is therefore as follows:

1. **Broader trade-offs / focus on outputs** – input directions are valued but delivering outputs that advance the long-term interests of customers should remain the primary factor in determining whether a targeted review applies. We accept that a prescriptive or formulaic approach to the factors outlined in sections 4-8 would be counter-productive and misaligned with the intent of the Handbook. We presume the AER will apply the Handbook in a flexible and pragmatic manner whereby breaches of less material input factors are weighed appropriately against output related factors.
2. **Application to 2024-29 resets** – the Framework and Approach (F&A) process is suited to a network formally signalling its intent to access a targeted review and for the AER to provide its initial view. The AER's criteria to decide whether to apply a targeted review should be focussed on the willingness and capacity of networks and interested stakeholders to participate in the process and the quality of the network's engagement plans and activities.

We consider the Handbook should apply to the 2024-29 determination process and accept a less formal approach is appropriate to trial and refine the targeted review process before it is resourced and scaled accordingly. However, it is important that networks unable to participate in the targeted process are not subject to a disproportionate level of scrutiny. In time all networks should be able to aspire to and access a targeted review (to varying degrees).

3. **Role of the CCP** – we support the AER's suggested role for the CCP and note that many networks are now actively seeking the independent views of customers and customer representatives in preparing their regulatory proposal. Prior to the publication of the Draft Handbook, we had committed to developing our 2024-29 proposal through a co-design process. To do this we have established a Regulatory Reference Group (RRG) reflective of diverse perspectives to help shape, challenge and review our engagement activities and proposal content.

In circumstances where networks follow an approach of this kind, we would expect the CCP to provide an additional perspective that focusses on the process followed, the effectiveness of the network's engagement activities and extent to which the feedback received has been incorporated into a proposal by a network rather than the content itself. It may be necessary for the AER to provide direction to the CCP on a case-by-case basis as to the appropriate scope of its review and participation in the determination process. The CCP may also need to be appointed earlier to support the targeted review stream or where there is extensive pre-lodgement engagement to be observed.

4. **Incentives** – we consider the AER generally applies a targeted assessment approach with regards to opex and depreciation currently. Whilst the Handbook should still address these key topic areas, it is the capex assessment process that particularly provides an opportunity to reduce regulatory costs through establishing clearer engagement expectations and regulatory precedents.

We would encourage the AER to review the requirements of the Regulatory Information Notice (RIN) that accompanies a proposal (Reset RIN) and whether it can be rationalised where a targeted review is adopted. We also wish to emphasise the importance of AER experts supporting and participating in pre-lodgement engagement activities. This will help focus the efforts of networks, customers and stakeholders.

We provide a response to the draft Handbook questions in the attached Appendix for further consideration. If you have any queries or wish to discuss our submission further please contact myself on (02) 9853 5195 or Colin Crisafulli, Manager Network Regulation at Endeavour Energy on (02) 9853 6017 or via email at [colin.crisafulli@endeavourenergy.com.au](mailto:colin.crisafulli@endeavourenergy.com.au).

Yours sincerely,

A handwritten signature in black ink, appearing to be 'FM', followed by a period.

**Françoise Merit**  
**Chief Financial Officer**

## Appendix – Response to questions

### 1. Do you consider the Handbook as set out will achieve the AER's aim of incentivising proposals that reflect consumer preferences and are capable of acceptance?

#### a) If yes to 1, what do you see as the main benefits of the Handbook? Are they the same as those set out in this document or do you consider there are additional benefits which are not listed?

Yes, we are of the view that the Handbook will better promote the long-term interests of customers, incentivise improved customer engagement and increase the efficiency of the regulatory determination process.

In essence, the Handbook is about assessing whether a quality engagement process was conducted in support of a proposal and that it had a clear and tangible impact on the proposal. Sections 5-8 establish tests by which the extent to which consumer views shaped key elements of the proposal can be determined.

The Handbook, while useful in this regard, is ultimately an exercise of trust between the AER, networks and stakeholders participating in the regulatory process. Ideally, there would be stronger assurance as to the weighting of the factors and exactly what a targeted review will entail. For instance, the points in section 5.2.6 are appropriate but relatively brief. It remains unclear what level of detail this kind of assessment will involve and what checks and balances will apply to prevent a targeted review from transitioning into a traditional assessment (where this may be unwarranted).

This is not to suggest that a binding or prescriptive Handbook is the solution, such an approach would be counter-productive and out of step with the intent of this initiative. Instead, this Handbook will need to be applied in good faith by all parties in a flexible and pragmatic manner. We therefore accept that the factors outlined in sections 4-8 can not be itemised and weighted in a formulaic manner to determine exactly how targeted and proportionate an AER review should be.

However, we would suggest that sections 4.3.2, 5.2.5 and 6.2.6 be given primacy as they more directly relate to the overall outcomes a proposal delivers and whether the proposal advances the long-term interests of customers. A regulatory proposal should deliver value to customers against a number of key outputs. For instance:

- **Service quality:** the extent to which the proposal supports service outcomes that customers value. This could be with respect to reliability, resilience, customer support/service, outage management, access (i.e. connection processes and terms). It is obviously critical that cost reductions are achieved without compromising service quality (at a minimum) and ideally whilst improving service outcomes. Conversely, there may be instances of consumer support for increased costs to support certain service outcomes.
- **Affordability:** a critical proof point may be whether a proposal delivers an overall revenue outcome that contributes positively to customer affordability (over the long term) such as no real price increases. This could allow for trade-offs between expenditure, WACC, depreciation rates, etc. For instance, if there is an increase in expenditure that is more than offset by reductions in other building blocks it may still be the case that the proposal delivers an outcome that is supportable by customers. We were therefore heartened to hear an AER Board member emphasise at the workshop on 6 October that the “total package matters” in addition to the assessment of individual building blocks.
- **Sustainability:** this is a difficult component to define but a proposal should support positive long-term outcomes for customers. This could go to measures of interest such as RAB per customer which essentially is a proxy of future affordability. As above, it is important expenditure reductions are achieved via sustainable efficiency gains rather than inefficient deferrals that create future price shocks. It is also important that networks innovate in order to provide an efficient service in the future (i.e. so the efficiency frontier continues to move rather

than stagnate), especially in response to increasingly clear calls from customers that we do so.

- Incentives: a proposal should provide customers with an incentive to consume and manage their energy more efficiently in order to reduce their bill and in turn future network costs (i.e. cost-reflective tariffs). A proposal should also set benchmarks that provide networks with an ongoing incentive to continually search for the optimal balance between cost and service quality. An aspect of this balance is innovation which is important to discovering and/or maintaining an appropriate balance in the future as new technology and/or processes are integrated.

We consider prioritising key outputs is uncontroversial and in most instances there should be no conflict between the overall outcomes of a proposal and the other input factors discussed in sections 5-8.

For instance, with respect to expenditure (sections 5 and 6) a reasonable forecast is taken to be in line with or below historical trends and/or AER top down analysis (e.g. repex model), or otherwise explainable by bottom up category analysis. This is an appropriate approach to assessing expenditure proposals and it is likely that the long-term interests of customers will be served by steady or reducing expenditure allowances. However, there may be instances where individual factors within the Handbook are not satisfied at the expense of others, yet a proportionate and targeted review may remain appropriate. Take a scenario where:

- an overall capex proposal is in line with, or below, historical expenditure;
- at a category level there are new and/or increased expenditure programs which may be supported by a mixture of technical/engineering detail or consumer support (by way of example increases in DER hosting); and
- these increases are completely (or more than) offset by reductions in other categories of expenditure or building blocks and/or deliver an outcome desired by customers (for instance improved ability to export).

In this case we would expect the Handbook to support a proportionate assessment approach and it appears to be the intent per section 5.2.6. In finalising and applying the Handbook we consider a balance between certainty and transparency whilst allowing for nuance and trade-offs to promote outcomes that advance the long term interests of customers will be critical.

**b) If no to 1, what are your reasons for this? Further, what changes do you consider could be made to the Handbook to achieve the aim of incentivising proposals that reflect consumer preferences and are capable of acceptance?**

Per the above response, we consider the Handbook will support improved regulatory outcomes if applied by the AER, networks and stakeholders in good faith and with a focus on outcomes. In our response to questions 4 and 7 below we provide suggestions for further improvements.

**2. Do you agree with the proposed targeted review stream and that this a positive change to how we regulate networks? Please include reasons for your views in the answer provided.**

Yes, the regulatory framework has a clear objective but a complex set of Rules and Guidelines to achieve this outcome. It can be difficult for all parties to understand what constitutes a 'good' regulatory proposal and how the AER should exercise its discretion. This Handbook is a simple and transparent account of the AER's regulatory task and its expectations.

Further, there is an increasing focus on pre-lodgement engagement activities in support of regulatory proposals. This can be an intensive process for networks, stakeholders and the AER. It is important that the outcomes of these engagement activities are given effect (to the greatest extent possible under the regulatory framework) in order for this approach to be a productive and worthwhile use of effort and

resources, and ultimately to encourage and incentivise truly customer-focused engagement. It would be duplicative, exhaustive and discouraging for all parties to engage in both extensive pre-lodgement engagement and post-lodgement technical review, particularly where there is conflicting outcomes from these activities.

A targeted review stream will allow the AER to build on the outcomes of pre-lodgement engagement and thereby validate the usefulness and credibility of this exercise by networks and stakeholders. This will better manage the expectations of all parties and minimise the costs and administrative burden of regulation.

**3. Do you consider the Handbook will improve the level of consumer engagement undertaken by network businesses and result in consumer preferences being better reflected in proposals? Please include reasons for your views in the answer provided.**

Yes, as noted above the Handbook provides clearer expectations as to what constitutes good engagement, and the clear preference for quality and sincerity of engagement expressed by the draft Handbook should diffuse an “arms race” approach to engagement that may not meaningfully reflect better outcomes. It also provides a tangible and clear role for engagement in the regulatory determination process that can reduce the costs associated with a traditional regulatory assessment.

As a result, it should assist in focussing engagement activities on key matters and provide greater assurance that the outcomes of engagement will be given effect to by the AER. On the latter it also provides greater insight as to the extent to which the AER can adopt the outcomes of engagement activities and how these will be balanced with its regulatory task of setting a prudent and efficient expenditure and revenue allowances.

Endeavour Energy notes the importance of having DNSPs and their representative reset committees “on the same page” with regards to the meaning of the handbook, because this will enable focused and collaborative work towards proposal development. (Please see below response to Q. 8).

**4. Are the incentives offered by the Handbook sufficient for network businesses to seek access to the targeted review stream process? If you do not consider the incentives are sufficient, then what additional incentives do you think could be provided within the current regulatory framework?**

As aforementioned, a higher level of assurance from the AER as to what a targeted review will entail would be ideal. However, we accept it is difficult for the Handbook to provide this level of assurance without becoming a legalistic and prescriptive document. Instead, the application of the Handbook will be context dependent and most likely refined and calibrated on a continual basis.

We would recommend the requirements of the Reset RIN, particularly Schedule 1 of the Reset RIN, are reduced where the AER intends to apply a targeted review. The requirements of the RIN are extensive and a significant burden on networks. In our view, much of this information (especially that required by Schedule 1) plays no or little role in the AER’s assessment of a proposal. Instead, proposal attachments, meetings with AER staff and consultants and responses to specific post-lodgement questions play a more integral role.

Given this, the requirements of Schedule 1 of the RIN should be tailored to the areas of targeted assessment (where these are known). This could be in the RIN issued to the network itself or through the AER flagging areas of intended non-enforcement of particular RIN components.

Similarly, an early indication of whether the AER considers a network qualifies for a targeted review and their ability to participate in and support pre-lodgement engagement will be important. This will enable networks to focus on preparing supporting documentation on areas of interest to the AER and stakeholders. It will also assist networks and stakeholders focus their pre-lodgement engagement activities and submissions.

- 5. The targeted review stream is a new process which we expect to refine and improve as we learn from each iterative application. Therefore our preference would be to first apply the targeted review stream process to a limited number of network businesses. This approach would allow us to better manage the risks of introducing a new process, maximise learnings and manage resourcing constraints. What approach or criteria should we use to determine which network businesses should be selected?**

Ordinarily, we consider the Framework and Approach (F&A) process provides the ideal opportunity for networks to flag their intention to access the targeted review stream. The AER could also set out in the Final F&A an early indication of whether it intends to support the pre-lodgement engagement activities required in support of a targeted review and the criteria against which this decision will be made subsequently.

However, for the first application of the Handbook we accept that a less formal, trial-based approach is suitable. We would expect the upcoming 2024-29 determinations to provide an opportunity to test the Handbook on a select basis to allow for learnings and improvements to be made before scaling its application. We would expect after this initial period that all networks would have the opportunity to access a targeted review (as should be the aspiration) and that the AER and stakeholders will be resourced and supported accordingly to enable this.

In terms of the criteria to decide whether a network should be selected, it could include:

- The network has established (or will) a panel/working group/committee/etc of customers and/or customer representatives that are suitably resourced and qualified (or will be supported on the latter) to participate in extensive pre-lodgement engagement and deliver an independent customer report.
- Interest from both the network and key stakeholders that will be relied upon to support pre-lodgement engagement to access a targeted review process.
- Evidence of a genuine and well-defined customer engagement plan from the network (developed in consultation with customers) that aligns with the AER's consumer engagement expectations. This may also include a commitment from senior management and/or Board members representatives of the network to resource and participate in engagement activities in support of a targeted review outcome.

It will be difficult for the criteria to cover the matters covered in sections 5-8 of the Handbook pre-lodgement of a proposal. This is because networks will apply to access the targeted review scheme at the very early stages of a determination process. Given this, early expenditure forecasts and positions are likely to be unreliable and/or not yet engaged on with customers.

This means networks and customers and stakeholders will engage on expenditure forecasts and key positions with an intention to pursue a targeted review. The AER will only be required to decide whether a network can access a targeted review after its formal submission. However, the AER's participation in pre-lodgement engagement will be critical in supporting a network's ability to access a targeted review.

This means that a commitment is required from the AER to support the pursuit of a targeted review prior (or in parallel) to positions and forecasts being developed in consultation with customers and stakeholders. The AER's criteria of whether to apply a targeted review should therefore initially be focussed on section 4 of the Handbook before it can formally be made on the basis of sections 4-8 post lodgement.

**6. Do you agree with the approach to commence the full application of the targeted review stream process to the revenue proposals due in January 2023?**

- a) **We would be open to considering applying of the targeted review stream process partially to a proposal which is submitted before January 2023. This would allow us to test the process before it is fully applied. Would you be supportive of this approach? Please include reasons for your views in the answer provided.**
- b) **For stakeholders that answered yes to 6(a), what approach or criteria should we use to determine which network business' proposal should be considered for a partial application?**

Yes, we support the application of the targeted review stream to revenue proposals due in January 2023. Although we note question 5 gives the impression this will be on a select basis rather than available to all networks. We have no comment as to whether the Handbook should apply to Transmission networks submitting proposals prior to January 2023 as this is a matter for these networks and their customers to comment on.

**7. Do you agree with the expectations for the topics set out in sections 4 to 8 of this document? If not, what changes do you consider need to be made to the expectations? Please include your reasons for any proposed changes.**

We support the AER outlining its expectations and it is important to ensure that regulatory precedents continue to be regarded and applied, even in the context of strong engagement outcomes. The AER must continue to satisfy its obligations under the Rules and sections 4-8 provide transparency as to how the AER will do so.

However, it is important that the Handbook complements and synthesises the existing Rules and various AER guidelines, instruments and guidance notes<sup>1</sup>. Given this, we provide the following comments for the AER's consideration on potential changes:

- Section 5.2.1.1: it is unclear what the third dot point relating the incentives adds to the AER's top-down assessment of the total capex forecast. Whilst networks should engage on incentive schemes the outcomes from the existing period are a mechanistic application of an approved incentive scheme.

Any engagement should focus on matters of judgement (such as adjustments to actual capex) and even then the link to forecast capex is unclear. The CESS operates on a more discrete basis relative to the EBSS or STPIS. The CESS incentivises efficient reductions in capex within a period which benefit customers through reduced RAB growth. An efficient capex allowance is set each period for the network to then out-perform given capex is not set on a recurrent basis.

It would be worth clarifying this point to make it clear that the CESS reward/payment itself is not contingent on customer engagement per se. Instead, we assume the intent is for networks to properly account for any sources of material underspend to provide customers (and the AER) assurance that the CESS is only rewarding efficient reductions in capex rather than happenstance deferrals.

- Section 5.2.4: we support consideration being given to the sustainability of a proposal with reference to RAB per customer. However, we suggest this be consolidated with section 5.2.5 as it relates to an output of a proposal and likely to overlap with the feedback networks receive from customers on the implications of the proposed capex including short term and long term trade-offs.

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<sup>1</sup> We note with the exception of the *Consumer Engagement Guideline for Network Service Providers* which the Handbook is intended to replace.



It is worth noting that as an outcome, RAB/customer may be difficult to manage in times of renewal. The assumption of repex being recurrent is only somewhat appropriate given the lumpy nature of asset age profiles historically. This can result in peaks and troughs in replacement profiles which in turn can impact RAB/customer. The latter can be difficult to manage outside of accelerating depreciation which impacts short time affordability.

- Section 6.2.3: we agree with the majority of positions the AER set out on opex trend factors. We acknowledge that these positions do not prevent a network from proposing an alternative, however the risk of not being able to access targeted review on the basis of doing would be disproportionate and potentially create perverse incentives. We therefore suggest the following factors are considered further:

- ‘adopting AEMO’s forecasts of consumption and demand’: A network is required to satisfy the operating expenditure criteria which include a *‘realistic expectation of the demand forecast and cost inputs required to achieve the operating expenditure objectives’*.

The AEMO forecast may be at a more aggregated network level or apply different assumptions, for instance to forecast spot loads, where networks will have more accurate information. Networks often prepare detailed forecasts at a Bulk Supply Point and Zone Substation level, required by the Reset RIN (rather than simply providing AEMO’s forecast) and have these forecasts verified independently.

Given this, the Handbook should not simply prescribe the AEMO forecast be used. Instead, it could reference a realistic or independently verified forecast is used and/or reasonable explanations exist for differences between the network forecast and AEMO’s.

- ‘forecasting customer number growth consistent with the historic trend’: for similar reasons to the above a specific approach to forecasting customer growth need not be embedded as the starting point. A historic trend may not be appropriate where better forecasting information (such as State and/or developer based housing forecasts) or expert advice is available.
  - ‘forecasting zero real non-labour price growth’: in practice this is likely to remain the default approach given the difficulties in applying material price growth to capex forecasts. If forecasting non-labour price growth becomes a material issue in the future and can be modelled simply by a network they should not be discouraged from proposing a non-zero value (including negative).
- Section 8.2.2 and 8.2.4: it may be necessary to broaden the language used to more explicitly include retailers following the expansion NER cl 6.18.5(i). Whilst we intend to engage extensively with end-use customers and their representatives the structure of each tariff must be capable of being understood by end-use customers or be capable of being incorporated by retailers in contract terms offered to those customers.

We also note there may be a tension between progressing tariff reform per 8.2.1 and 8.2.4 that suggests reducing customer choice may be a key consideration in the targeted review of a Tariff Structure Statement (TSS).

## **8. Is there any further clarification or issues which the Handbook should set out?**

For clarity the AER should consider adopting language that more clearly differentiates between end-use customers and stakeholders who represent end-use customers (or a subset of). We note the reference to “pre-lodgement engagement with consumers”, in Figure 1 (p.8) of Section 3 and advise this phrasing may cause confusion as to the exact requirement of the early engagement. The AER could consider amending this language, or clarify that in the parlance of the report, “consumer” means stakeholder / advocate, whereas “customer” means what DNSP’s commonly refer to as an “end-use

consumer". This clarification would be of benefit to all parties. We highlight that 4.3 (Breadth and Depth) refers further to consumer engagement but makes no reference to engagement with customers. This is a further example of how a clarification of this terminology would be desirable.

Section 3.2.2 states that independent consumer reports can provide views on technical issues but does not offer clarity on the extent to which this is considered reasonable or necessary to the AER's assessment. This statement appears somewhat at odds with earlier advice regarding the reporting role being focused on engagement quality and outcomes, and we believe further clarification on this aspect will be useful for all parties.

It may also be worth noting that the Handbook does not in any way limit the scope of a network's engagement activities. Instead, it provides useful guidance on key topic areas that commonly are the focus of a proposal. However, other building block and determination topic areas may also be considered for targeted vs detailed review based on the quality of a network's engagement.

For instance, cost pass-throughs, contingent projects, connection policies, Alternate Control Services (ACS) like Public Lighting, etc. may be areas of interest for certain networks or their customers in certain circumstances. Whilst these topics are not explicitly addressed within this draft Handbook we would expect the AER to take a similar approach to assessing them.