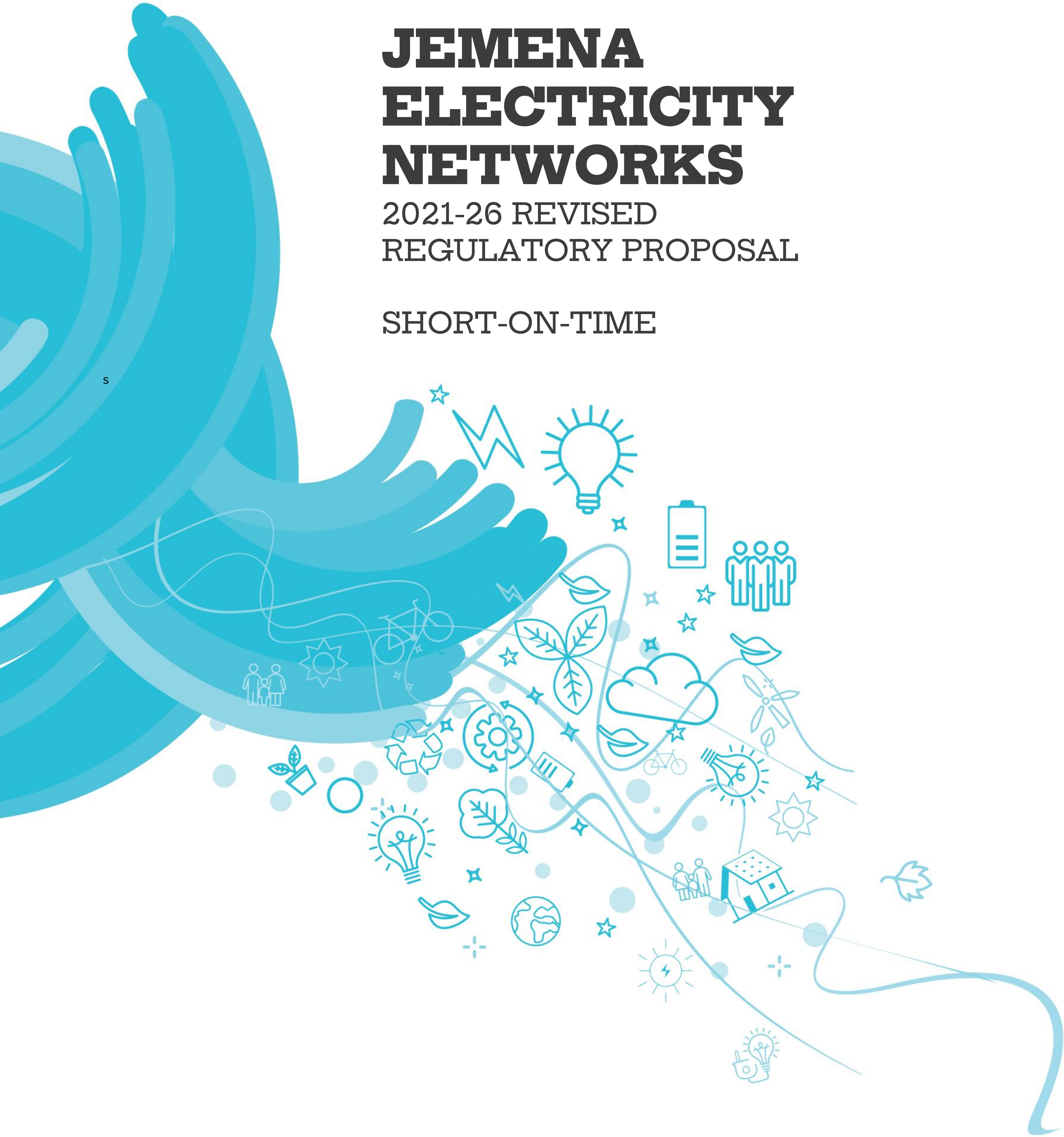
JEMENA ELECTRICITY NETWORKS

2021-26 REVISED REGULATORY PROPOSAL

SHORT-ON-TIME



DECEMBER 2020

Overview

Every five years, the Australian Energy Regulator (**AER**) undertakes an electricity distribution price review (**price review**) to determine the revenue which our business can recover for the services it provides. The review involves a comprehensive assessment of our plans and consideration of our customers' preferences. Given the nature and extent of the review, multiple submissions are made by stakeholders and us to inform the AER in making its decision.

This document—Jemena Electricity Networks (Vic) Ltd's (**JEN**) revised regulatory proposal (**revised proposal**)—outlines the revenue we require to deliver the services our customers expect over the 2021-26 regulatory control period (**next regulatory period**). It is an update to our initial proposal of 31 January 2020 (**initial proposal**), focusing on providing updated or new information and addressing material issues outlined in the AER 2021-26 draft decision on our initial proposal(**draft decision**). It also examines and incorporates the effects of changes arising since the submission of our initial proposal, such as the COVID-19 pandemic, updates from our customers and changes to legal and regulatory requirements.

To the extent that our initial proposal has not been updated, amended or otherwise changed by this document, it remains applicable (and for those elements should be read together with this document). For simplicity and ease of understanding, we have not restated those elements in this document.

Table OV.1 sets out a summary of the standard control services and smart metering services revenue we require to provide the electricity distribution services to our customers safely, efficiently, and to a level expected of us.

Table OV.1: standard control services and smart metering services smoothed revenue forecasts [5-year totals] – ($Nominal, $M)

Service Type	Initial Proposal	Draft Decision	Revised Proposal
Standard control services	1,379.6	1,273.3	1,305.0
Smart metering services	128.2	112.1	112.9
Total	**1,507.8**	**1,385.3**	**1,417.9**

The revised proposal revenue amount of $1,418M ($nominal) is 6 per cent lower than our initial proposal amount of $1,508M ($nominal). The revenue now being proposed is greater than the $1,385M ($nominal) approved in the AER's draft decision by 2.3 per cent. In this revised proposal, we outline the reasons why the revenue assessment in the draft decision is insufficient and why the revenue we seek in the revised proposal is the minimum necessary to provide our services safely and efficiently.

Our customers' preferences

In developing our initial proposal, we set out to make our customers the centre of our plan. We did this by involving our customers in the development of our plan and making sure that we reflected their preferences in every aspect of our initial proposal. By reaching out widely, we were able to capture the broadest range of voices possible. Given the insights gained and success of this approach when developing our initial proposal, we have re-engaged with a number of our key stakeholders, including our People's Panel and Customer Council when developing this revised proposal.

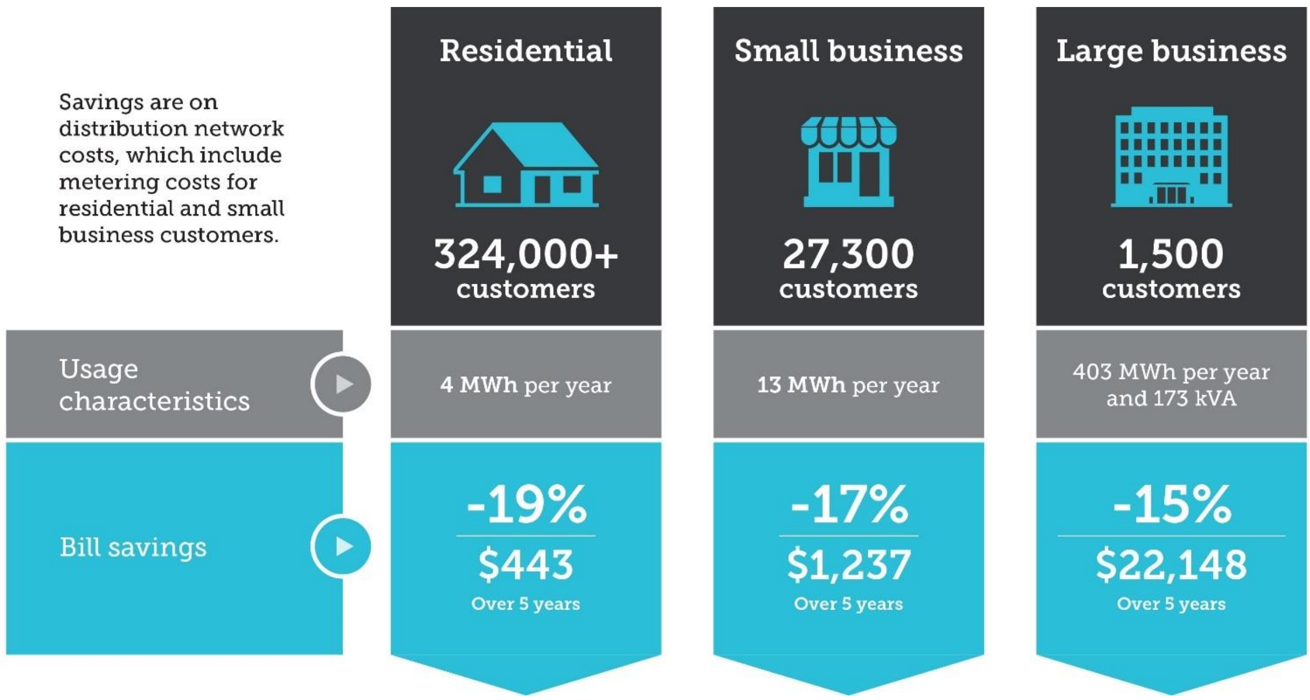
Through our Customer Council, we obtained comprehensive feedback on the draft decision and our initial proposal. We have also sought the views of our People's Panel to understand what has changed for them since we last met, whether their preferences have changed as a result, as well as to discuss some of the more material issues raised by the AER in the draft decision.

Our People's Panel members—representing the voice of our broader customer base—affirmed their preferences, and particularly emphasised their desire for affordable electricity. Our revised proposal responds to the feedback we've heard by:

- providing even greater bill savings than our initial proposal for all of our customers
- offering a range of network tariffs that give our customers more choices, empowering them to manage their electricity usage in a way that better suits them
- reflecting the efficient expenditure required to maintain the current reliability of our services over the long-term
- incorporating our Future Grid program to facilitate the efficient connection of a growing amount of Distributed Energy Resources (**DER**) to our network.

The bill savings for our customers are outlined in Figure OV.1 below, with more than five per cent extra savings across each customer type compared to our initial proposal.

Figure OV.1: Bill savings our revised proposal will deliver for customers ($2021)



The AER's draft decision

On 30 September, the AER released its draft decision relating to our initial proposal. The draft decision is a formal draft of the decision that will set out the revenues and prices the AER considers are prudent and efficient for us to provide our services in the long-term interests of customers. The AER's draft decision considered that our smoothed revenues for standard control services should be $1,273M (nominal) for the next regulatory period.

Similarly, for our smart metering services we proposed $128M (nominal) of smoothed revenue for the next regulatory period, however, the draft decision considered $112M (nominal) of smoothed revenue is required.

In making its draft decision, the AER has outlined its reasoning and invited JEN and other stakeholders to make submissions to better inform its final decision. We have prepared this revised proposal to inform the AER's final decision and demonstrate why our revised proposal revenue requirement is in the long-term interests of our customers.

What has changed since submitting our initial proposal?

There have been several changes since submitting our initial proposal in January 2020 which impact our forecast expenditures, and therefore, our revenue requirements. Changes include movements in the risk free rate and the AER's consultation on forecast inflation. Additionally, the COVID-19 pandemic has impacted on the way our society interacts and changed the way our customers use and rely on our electricity network.

In preparing this revised proposal, we have undertaken a comprehensive analysis of the impacts of the pandemic on JEN and is services, including on our capital and operating expenditures, and adopted a balanced approach when factoring these changes into our revised proposal. We elaborate on the pandemic, its economic impacts and our revised proposal's response to it in our full proposal.

We have also continued to focus on the efficient deployment of Rapid Earth Fault Current Limiter (**REFCL**) devices to meet our bushfire mitigation obligations. As indicated in our initial proposal, we have refined our program and reduced our forecast expenditure required to achieve compliance in the Coolaroo area. Our revised proposal also incorporates expenditure required to comply with bushfire mitigation obligations in the Kalkallo area, in light of changes outlined by Energy Safe Victoria (**ESV**).

These changes are new, and aside from the refinement of our REFCL program, were not contemplated when we developed our initial proposal. Given this, we consider it is prudent to raise these issues in this revised proposal, so that these matters are appropriately assessed and considered by the AER to afford JEN a reasonable opportunity to recover its efficient costs related to these changes.

Ensuring we have sufficient revenue to deliver services

JEN must recover its efficient costs through regulated revenue to provide standard control services and smart metering services in line with our customers' preferences and in accordance with our regulatory obligations.

Application of benchmarking techniques to operating expenditure

We have examined the draft decision in detail and how the AER's assessment tools have been applied. For our base year operating expenditure, we have significant concerns with the approach the AER has adopted to determine an alternative operating expenditure base year amount, including:

- the deterministic application of benchmarking techniques to assess base year operating expenditure efficiency, despite there being known shortcomings associated with these benchmarking techniques
- making no adjustment to account for differences in capitalisation policies between Distribution Network Service Providers (**DNSP**s)
- making reductions to our newly expensed corporate overheads, when these expenses were not subject to a similar assessment methodology under their former classification as capital expenditure
- the existence and acknowledgement of significant errors between 2014 and 2018 by AER's consultant about the calculation of output weights as part of this analysis.

These concerns are material, and similar concerns have been raised by other stakeholders and industry participants previously. Left unaddressed, we consider the AER's approach to determining an alternative operating expenditure base year amount will not provide JEN with a sufficient revenue allowance for the next regulatory period and could have long term consequences to our customers.

Inflation Forecast

We note that the AER has recently made its draft decision on forecasting inflation[1] and is scheduled to release its final position paper after submission of this revised proposal. We have provided our views on this

1 AER, *Draft position, Regulatory treatment of inflation,* October 2020.

consultation through a separate submission to the AER and have summarised our submission in Attachment 03-01. We note that, although we cannot incorporate the outcomes of the inflation forecasting final decision into this revised proposal, there is sufficient time for the AER to include it in JEN's price reset final decision.

Our revised proposal

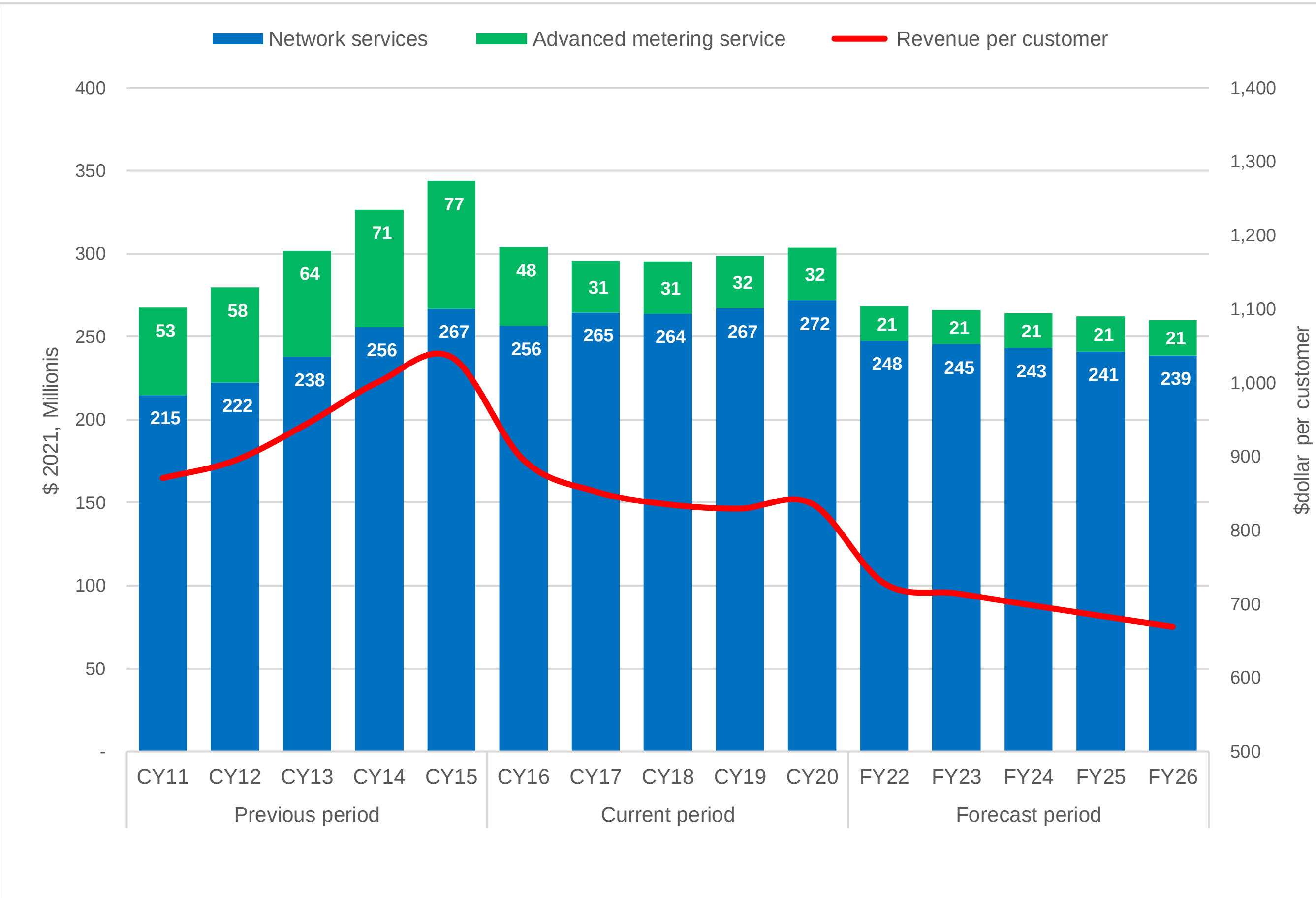
We have considered a broad range of factors when thinking about how we operate and invest in the future, and have reflected these in our revised proposal. We have also addressed other key areas of the draft decision in which the AER sought further information.

Our revised proposal revenue forecast reflects the updates we have made to our key drivers of building block revenue, most notably:

- a revised operating expenditure forecast which incorporates changes to our base year, step changes, forecast output growth and real labour price escalation
- a revised capital expenditure forecast which incorporates updates to our REFCL program, real price escalation and responding to the COVID-19 pandemic
- updates to the rate of return to account for market movements.

Our revised proposal continues the long-term trend of falling network prices for our customers. As can be observed in Figure OV.2, our revenues are forecast to reduce substantially at the start of the next regulatory period and then decline at a slower rate, despite our network and customer base growing—meaning that our customers will continue to benefit through lower bills over time. The revenue per customer is declining at an even faster rate when the revenue reductions are spread across a growing customer base.

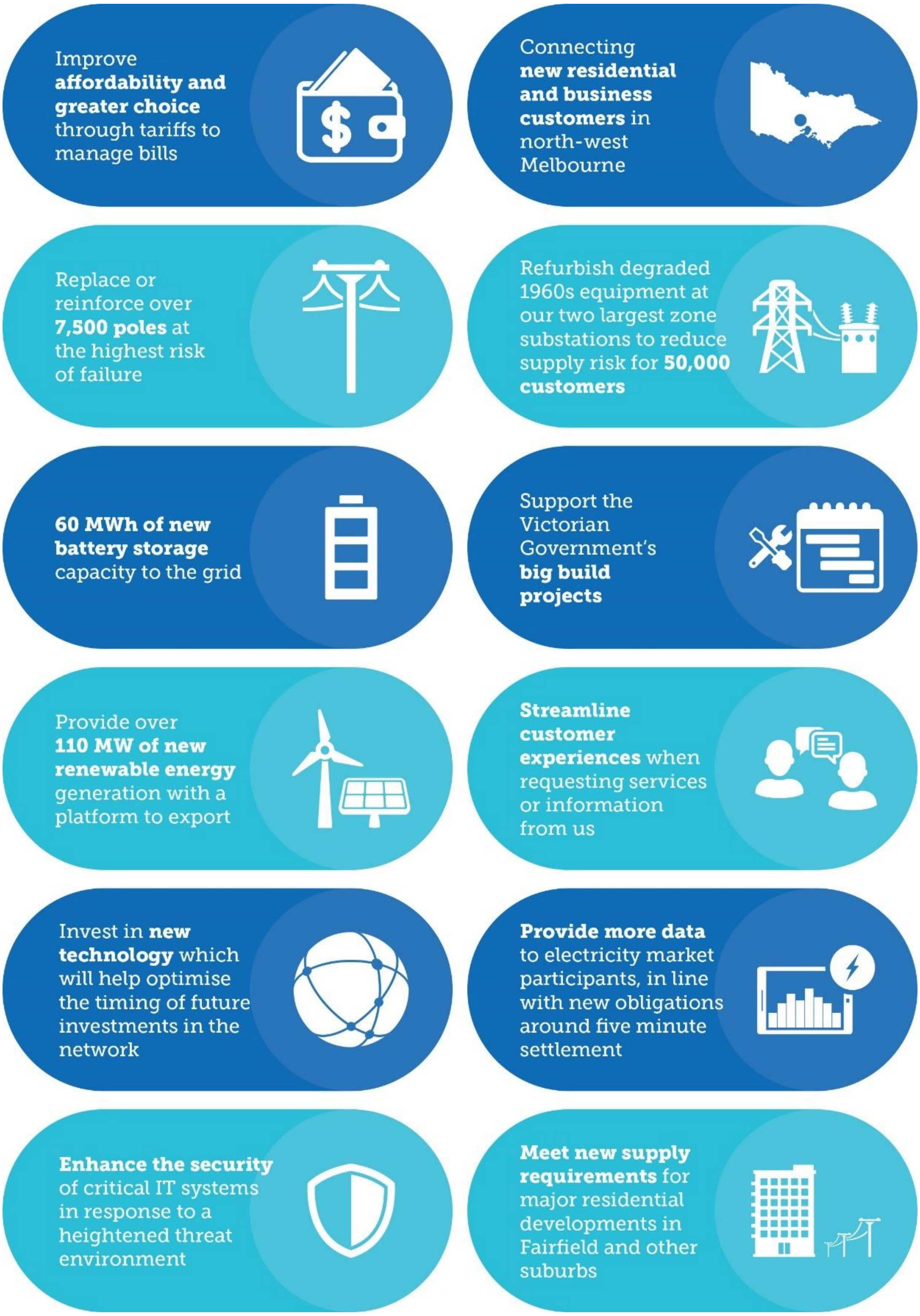
Figure OV.2: Long term revenue requirements ($2021, $M)



What our revised proposal delivers for customers

Through our revised proposal, we can deliver on the commitments we have made to our customers to provide safe and reliable electricity distribution services, efficiently, affordably and sustainably. Figure OV.3 outlines the initiatives and benefits that our revised proposal allows us to deliver.

Figure OV.3: What our revised proposal delivers for our customers



Our revised proposal identifies several risks

Our proposal also identifies several risks, including revenue sufficiency, to ensure we can deliver safe and reliable distribution services to our customers. We outline these risks in Figure OV.4 below.

Figure OV.4: Risks of our proposal to our customers