2023-27 Revenue Proposal

Revenue Proposal Reference Group (RPRG)

10 December 2020

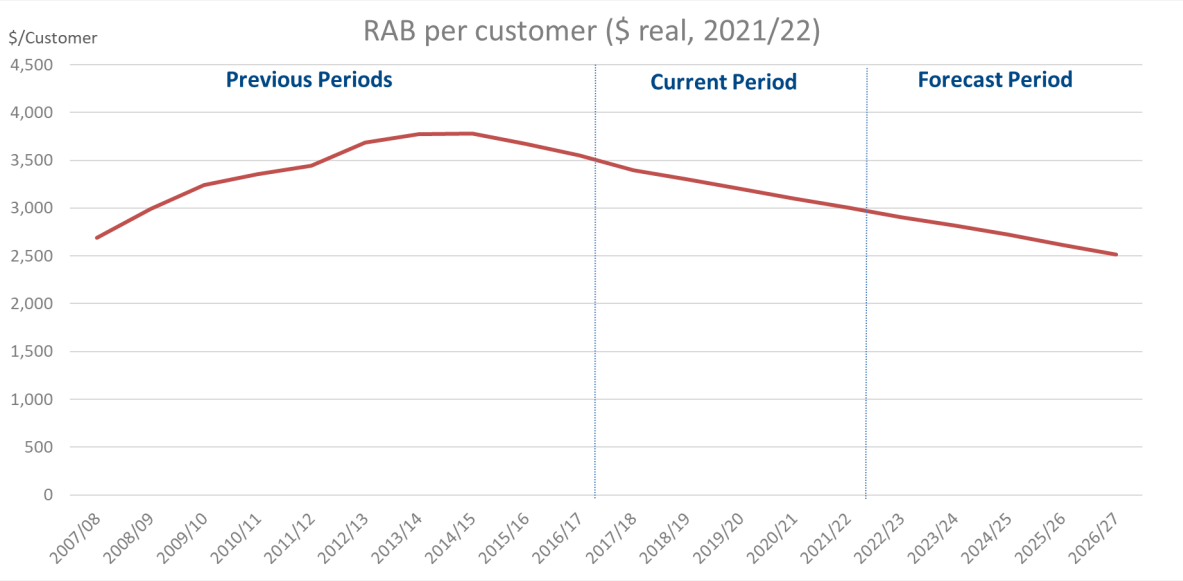
Introduction and progress update

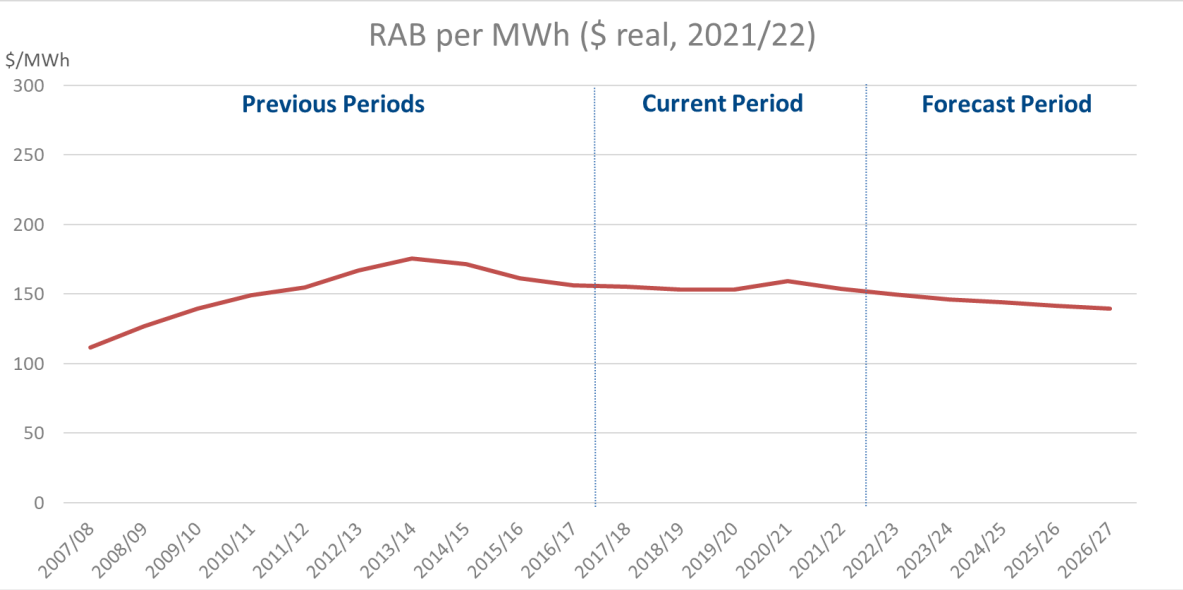
Actions from previous RPRG/CP meetings

Action	Response
Powerlink to indicate what the $ impact on electricity prices would be for customers should contingent projects go ahead.	• As a 'rule of thumb', for every $100m of contingent project capital expenditure, the indicative impact on the transmission component of electricity bills is 60c per year for the average residential customer[1] and $1 per year for a small business customer[2].
Powerlink to respond to whether levels of repex reduce the need for opex, and how does IT capex investment impact opex.	• The opex requirement for a particular asset class is generally proportional to the average age of assets within each class. If no new assets are added due to augmentation, and the rate of reinvestment only maintains the average age of assets within each class, then the opex requirement would remain relatively constant. Reinvestments in an asset class that hold the average age of the asset class relatively steady are unlikely to bring about a reduction in total opex for the asset class. • IT capex impacts opex two ways: o it supports process efficiency improvements by replacing legacy systems with contemporary ones that provide for more seamless data integration, management of process flows etc; and o the cost of IT ownership is reduced through consolidation of applications, databases, platforms etc. The cost to patch or update systems is also reduced as there are fewer customisations. More modern systems have fewer vulnerabilities than older systems and vendor support is cheaper than for legacy systems.
Can Powerlink demonstrate some additional metrics e.g. RAB/customer and RAB/MWh.	• See graphs on the following slide.

[1] *based on the Queensland Competition Authority's (QCA) annual Tariff 11 (residential) median energy usage of 4,061kWh p.a.*
[2] *based on the QCA's annual Tariff 20 (small business) median energy usage of 6,831kWh p.a.*

RAB metrics





- Our RAB has been declining in real terms over the current period and is forecast to decline in both real and nominal terms in the next period.
- RAB per customer has declined at a rate of 3% p.a. over the current period, and is forecast to continue to decline at a rate of 3% p.a. in the next regulatory period.
- RAB per MWh has remained relatively flat during the current period, and is forecast to decline at a rate of 2% p.a. in the next regulatory period.

Update on key outstanding matters

Contingent reinvestments

After considering feedback, we have decided not to pursue contingent reinvestment projects in our Revenue Proposal.

- Our draft Revenue Proposal included proposed contingent reinvestment projects where future reinvestment needs were related to future ISP needs and were not sufficiently certain in terms of cost and/or timing.
- We received feedback from customers, the AER and the CCP that expressed concern about the use of the contingent project framework for reinvestments, including that:
  - contingent reinvestments may undermine the incentives based regulatory framework;
  - a condition based trigger cannot be objectively verified (as required by the Rules); and
  - a condition based trigger is not an exogenous event, beyond the influence of the TNSP.
- As a result of this feedback we have decided not to pursue contingent reinvestments in the Revenue Proposal.
- This decision will not result in a change to the capital expenditure forecast (of $865.3m) presented to the Customer Panel on 26 November 2020. The forecast included additional ex-ante capital expenditure to provide for targeted life extension of the assets that were the subject of the proposed contingent reinvestment (approximately $21m).
- This inclusion was made in anticipation of formalising a decision to remove contingent reinvestment.

RAB transfers

We are investigating potential asset transfers into the RAB of up to approximately $50m ($21/22, real).

- The Rules allow for the value of assets that previously provided non-prescribed transmission services to be transferred into the RAB, where they subsequently provide prescribed transmission services.
- We are investigating potential additions to the RAB up to an estimated value of $50m.

Indicative impact	Latest forecast (presented to Customer Panel 26/11)	With $50m transfer	Change
RAB – change over 2023-27 regulatory period	↓ $766m (real, 2021/22)	↓ $727m (real, 2021/22)	↑ $39m
	↓ $40m (nominal)	↑ $5m (nominal)	↑ $45m
MAR – 2023-27 regulatory period (5-year total)	$3,336.4m (real, 2021/22)	$3,351.8m (real, 2021/22)	↑ $15.4m
Transmission price in first year (2022/23) of the next regulatory period			
Residential (per annum)[1]	↓ $14.30 (nominal)	↓ $13.80 (nominal)	↑ 50c
Small business (per annum)[2]	↓ $24.20 (nominal)	↓ $23.30 (nominal)	↑ 90c

[1] *based on the Queensland Competition Authority's (QCA) annual Tariff 11 (residential) median energy usage of 4,061kWh p.a.*
[2] *based on the QCA's annual Tariff 20 (small business) median energy usage of 6,831kWh p.a.*

This information is indicative only and does not reflect Powerlink's final Revenue Proposal position.

Shared Assets

At this stage, we do not anticipate an adjustment to our Maximum Allowed Revenue (MAR) for shared assets.

- Shared assets are assets that:
  - are used to provide both prescribed and non-regulated services, or services that are not transmission services; and
  - sit entirely within the Regulatory Asset Base (RAB).

- Where Shared Asset Unregulated Revenues (SAUR) are greater than 1% of smoothed MAR (approximately $7m p.a. for Powerlink), the AER may reduce the MAR by 10% of the SAUR.

- Our current forecast of net revenues for shared assets indicates that the 1% MAR materiality threshold would not be exceeded in any year of the next regulatory period and therefore, no adjustment will be made to Powerlink's MAR – we are still working through this to finalise our assessment of potential shared assets.

This information is indicative only and does not reflect Powerlink's final Revenue Proposal position.

Benchmarking

Benchmarking – overview

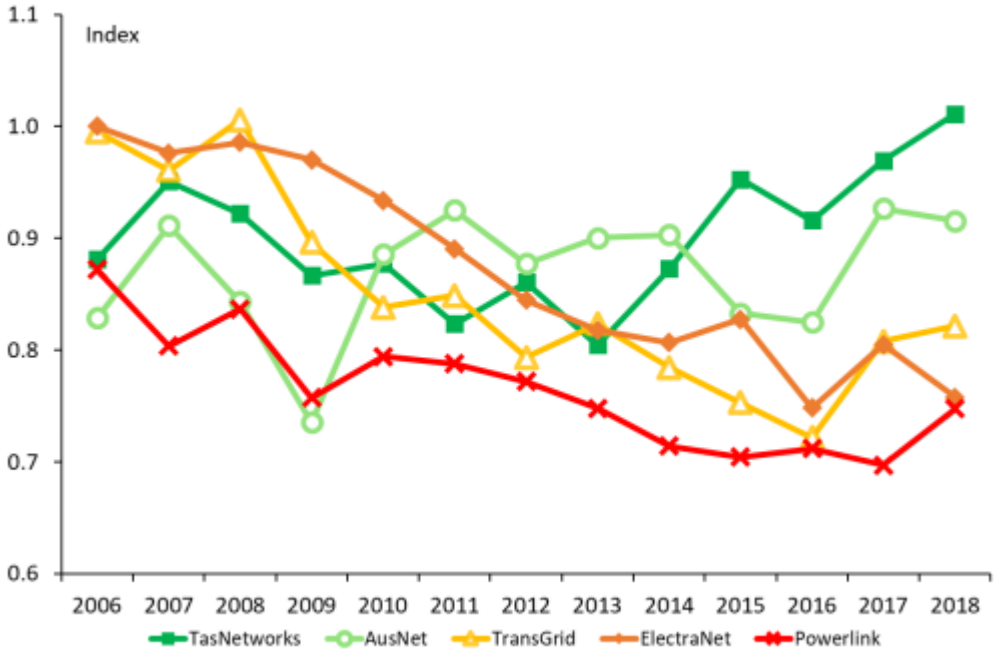
Econometric benchmarking of TNSPs is not well developed, even internationally. Australia is further limited by the small sample size of only five TNSPs.

- The AER published its 2020 Annual Benchmarking Report for electricity TNSPs on 27 November 2020. This includes TNSP data to 30 June 2019.
- AER must have regard to the most recent annual benchmarking report when assessing whether operating and capital expenditure forecasts provided by a TNSP within its Revenue Proposal represent efficient expenditure.
- The 2020 Annual Benchmarking Report has updated the weightings applied to the non-reliability output measures (maximum demand, energy transported, number of customers and circuit kilometres) to correct for an earlier error.
- The effect of this has been to lower the relative performance of AusNet Services and TransGrid and to increase the relative performance of TasNetworks and ElectraNet. Powerlink has remained relatively unchanged.
- There were other, less significant, changes to the weight given to energy not supplied, updated VCR values and the method for calculating the productivity indices.

Benchmarking – 2019 vs 2020

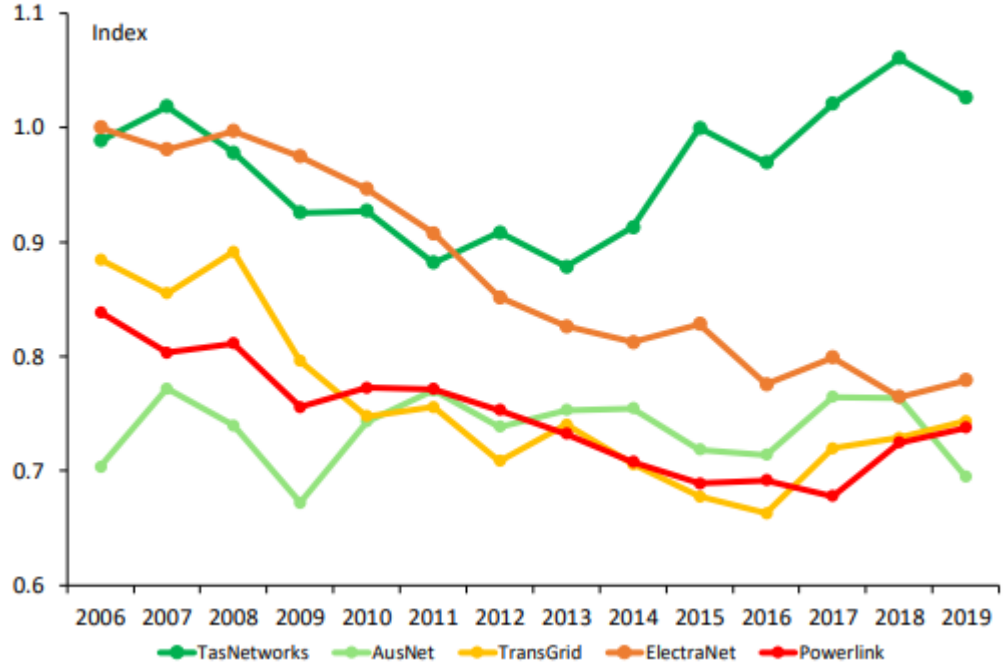
The effect of the change in weightings confirms benchmarking results for TNSPs cannot be used deterministically.

Figure 4.1 Electricity transmission MTFP indexes by TNSP, 2006–2018



Source: 2019 Annual Benchmarking Report, AER

Figure 4.1 Electricity transmission MTFP indexes by TNSP, 2006–2019



Source: 2020 Annual Benchmarking Report, AER

- Weighting change has not significantly impacted individual trends, but has impacted relative rankings.

Benchmarking – implications for the Revenue Proposal

- Powerlink and TransGrid are the only two TNSPs to have improved their MTFP performance in each of the last two years. The AER notes that this 'can be linked to improvement in opex efficiency levels.'

- We engaged HoustonKemp to provide advice on the 2020 Annual Benchmarking Report and the efficiency of our proposed opex base year (2018/19). This included analysis of our historical opex over time and compared to other TNSPs.

- We have provided the Customer Panel, the AER and the AER's Consumer Challenge Panel with a copy of HoustonKemp's report in advance of the lodgement of the Revenue Proposal. This was to help customers and the AER consider the efficiency of our base year as part of our goal to achieve 'capable of acceptance'.

- HoustonKemp considered three different tiers of measures:
    - Multilateral Total Factor Productivity (MTFP), capital Multilateral Partial Factor Productivity (MPFP) and opex MPFP, both in absolute and trend terms;
    - Partial Performance Indicator (PPI) measures such as total cost per end user, total cost per circuit km, total cost per MVA of maximum demand and total cost per MWh of energy transported; and
    - Opex category analysis measures such as corporate overheads per end user, network overheads per end user and maintenance costs per circuit km.

Benchmarking – HoustonKemp conclusions

HoustonKemp found we are operating relatively efficiently when compared to our peers and there is nothing to indicate our proposed 2018/19 base year opex is "materially inefficient" [1].

- The AER's most recent benchmarking results, both in absolute and trend terms, shows that we have been responding to the incentives in the regulatory framework and are operating relatively efficiently when compared to our peers.

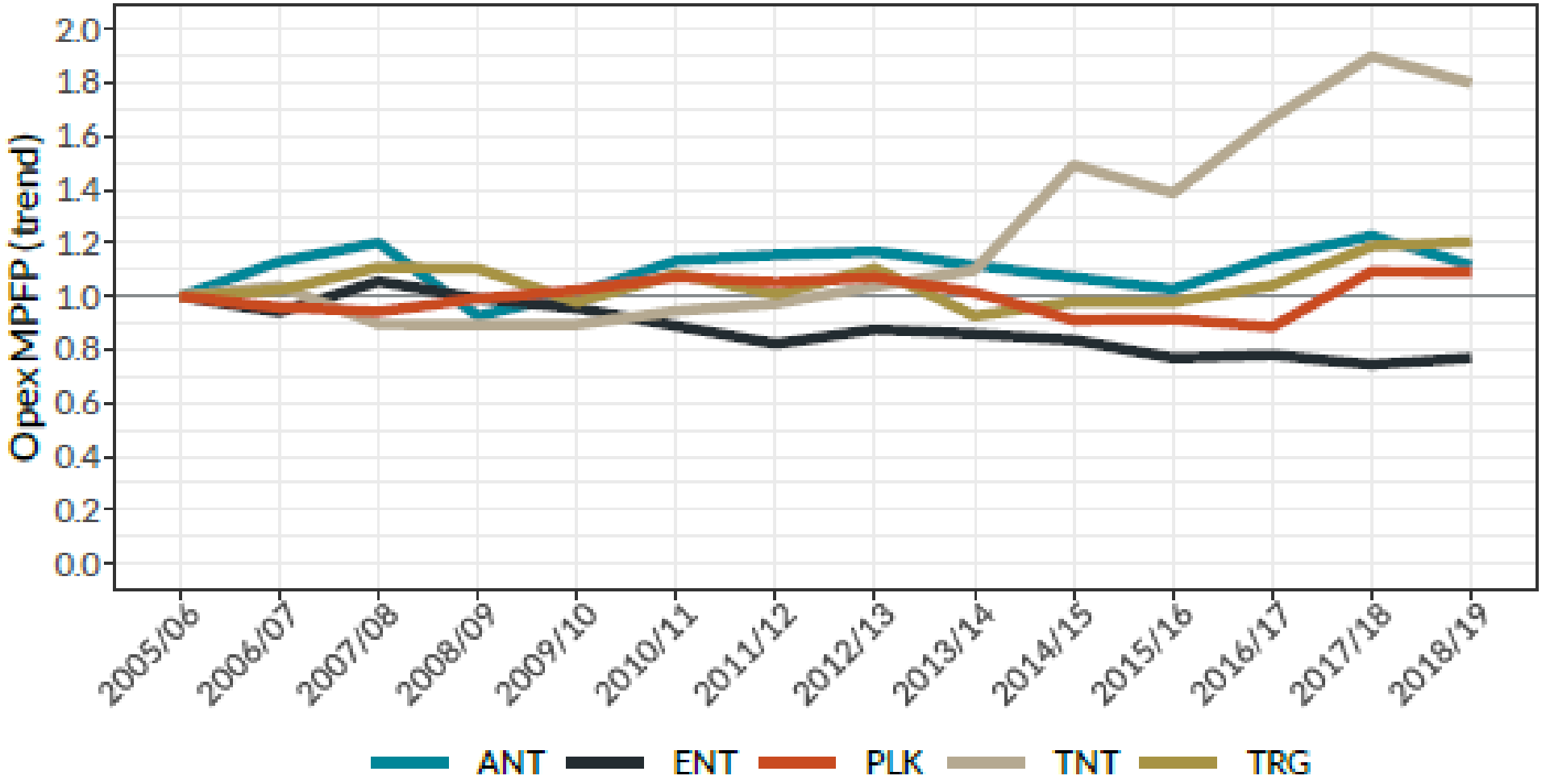
- Our relative benchmarking performance in 2018/19 (our proposed opex base year) is consistent with our relative performance in 2014/15, which the AER previously considered to represent an efficient base year for the current regulatory period.

- Category analysis of our opex over time and against our peers indicates that our opex performance across major opex categories has been improving over time and is consistent with the key characteristics of our network relative to other stand-alone TNSPs.

[1] Note: use of the term "materially inefficient" reflects terminology used by the AER.

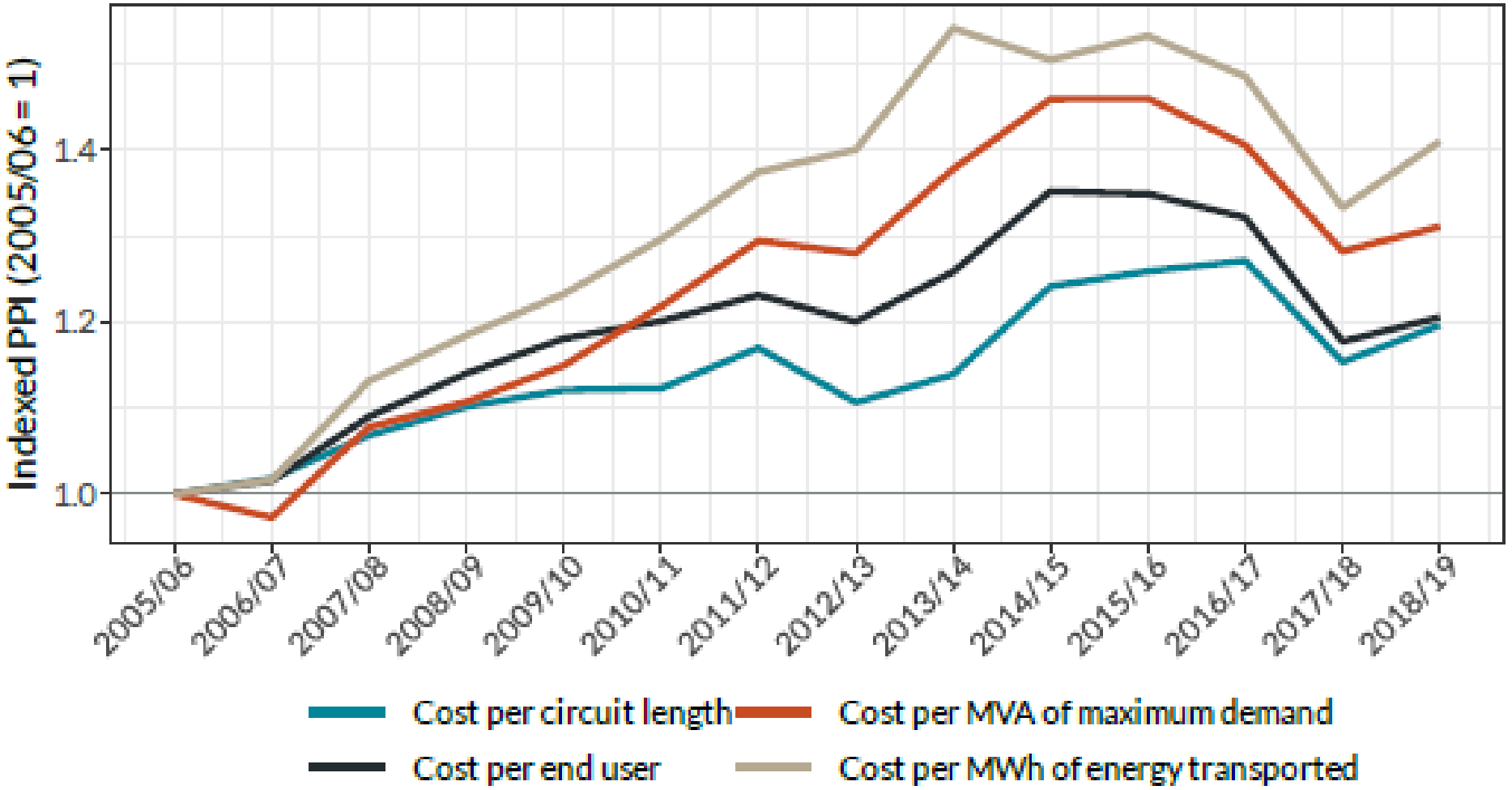
Opex MPFP trend

HoustonKemp found our opex MPFP performance is consistent with other TNSPs and has improved over time.

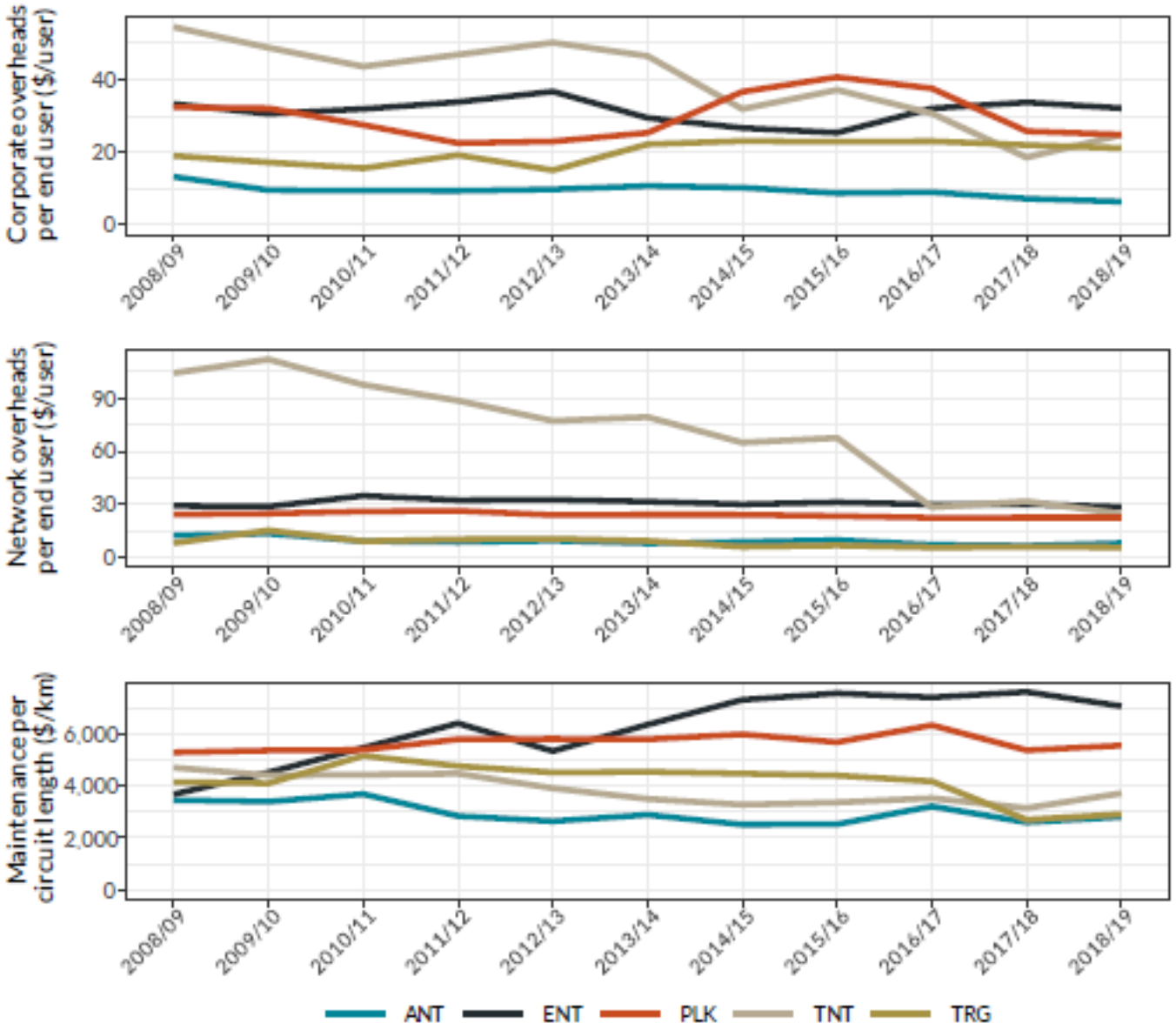


Partial Performance Indicator (PPI) over time

HoustonKemp found our PPI results are consistent with our network characteristics and there is nothing that would suggest our 2018/19 outturn opex is "materially inefficient".



Opex category analysis



Corporate and network overheads per end user

- HoustonKemp found that:
  - Overheads per customer are lower than they were in 2008/09.
  - The increase in 2015/16 reflects our organisational restructure costs.

Maintenance per circuit length

- HoustonKemp found that maintenance costs are approximately 5% higher in real terms than in 2008/09, consistent with the increasing age of our network over time.

Engagement

Evaluation of Engagement Approach

Success of engagement approach is whether we meet our overarching objective:

To deliver a Revenue Proposal that is capable of acceptance by our customers, the Australian Energy Regulator and Powerlink.

Engagement KPIs

KPI	Target
Effectiveness and quality of information provided to stakeholders	70% of participants rated the information provided relevant and accessible
Satisfaction level of stakeholders with engagement activities	An overall satisfaction rating of 7/10 for engagement activities
Stakeholders were engaged at appropriate level on the IAP2 spectrum	Identified that majority of stakeholders had appropriate level of influence on Powerlink decision-making
Impact of engagement on Powerlink decision making and quality of feedback/input received	Ability to demonstrate what changed as a result of engagement.
Timely delivery of engagement program	Engagement program delivered on-schedule.
Improvement in social licence to operate score and reputation scores	Improvement on 2018 social licence to operate and reputation scores, and positive verbatim feedback regarding Revenue Determination process engagement.

Evaluation of Engagement Approach

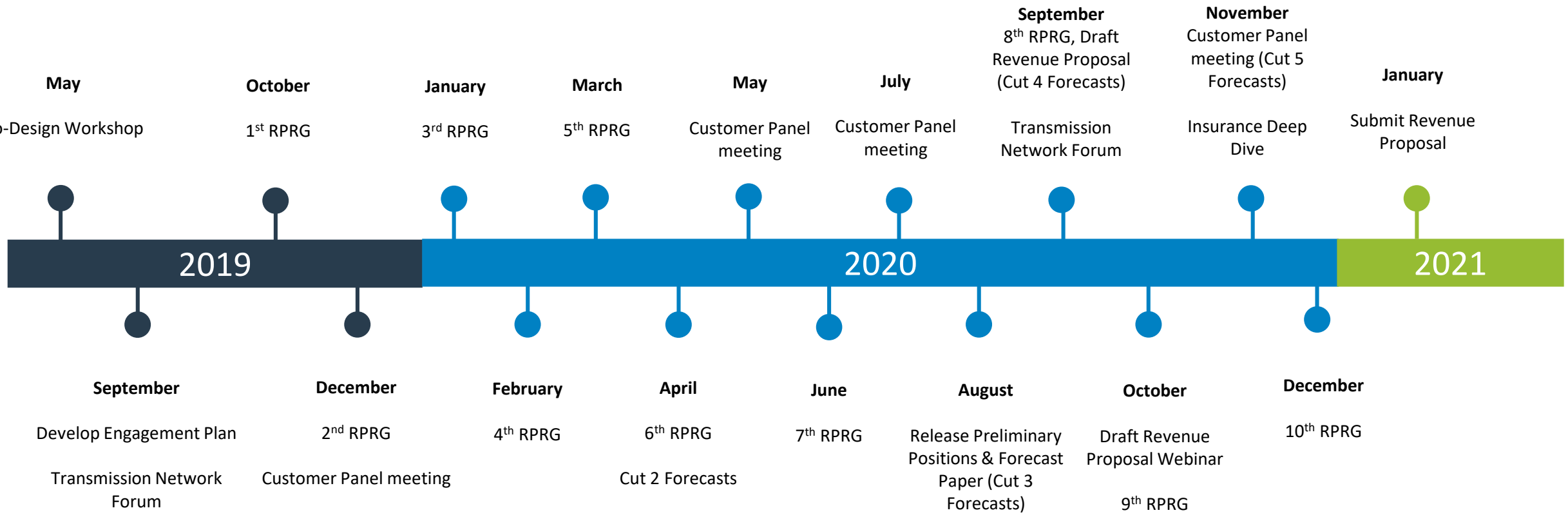
Formal evaluation techniques

- Customer Panel meeting without Powerlink representatives
- Dedicated session with RPRG
- Submissions on Draft Revenue Proposal
- Quantitative Customer Panel Survey
- Satisfaction surveys after key engagement activities (e.g. Transmission Network Forum)
- Stakeholder Perception Survey (wider stakeholder view)
- Energy Charter Independent Accountability Panel Report

Informal evaluation techniques

- Regular Customer Panel agenda item to discuss and pivot engagement approach
- Regular ‘check-in’ conversations with Customer Panel representatives

Engagement timeline



Ten Revenue Proposal Reference Group (RPRG) meetings held

Four Customer Panel meetings held

Evaluation of Engagement Approach

We understand a Customer Panel meeting (without Powerlink representatives) is being held on 11 December 2020 to discuss engagement and capable of acceptance criteria.

From an RPRG perspective:

- How would you describe Powerlink's engagement approach for its 2023-27 Revenue Proposal?
- Was engagement scope clear and appropriate?
- Did the information presented by Powerlink allow you to appropriately participate in engagement activities?
- Did you feel like customer feedback influenced the 2023-27 Revenue Proposal?

Next steps – Revenue Proposal and RPRG