

27th November 2014

CAUTION NEEDED TO AVOID ELECTRICITY CUSTOMER IMPACTS

Unsustainable funding cuts to electricity networks proposed by the Australian Energy Regulator threaten to undermine reliability, safety and efficiency outcomes for customers.

Energy Networks Association Chief Executive Officer, John Bradley, said the network sector recognized the price pressures on electricity customers and the need to deliver cost savings and efficient performance. Network businesses proposed real capital expenditure reductions of over 30% compared to the last regulatory period. The AER has largely accepted TasNetworks Tasmanian transmission proposal.

Mr Bradley said the AER has proposed real reductions to current operating expenditures totaling \$2.7 billion or 35% over the next five years for electricity transmission and distribution network businesses in NSW and ACT.

“Customers have been fed up with electricity price increases and do expect to see network costs falling but we also need to avoid impacts on other customer priorities.

“In NSW and ACT, the AER would cut distribution operating expenditure to a level not seen in 10 to 13 years – it seems implausible that this can be achieved without customer impacts.

“If implemented, these funding cuts put at risk key consumer outcomes relating to safety, maintenance and outage response times.

“While consumers should expect a strong regulatory regime which drives real efficiency benefits, unsustainable funding cuts would inevitably be service reductions in disguise.

“It would be a high risk approach to an essential service,” Mr Bradley said.

Mr Bradley said the draft decisions threaten to change the risk profile of network operations and service delivery, and deliver short term price reductions at the expense of ongoing service outcomes for consumers.

“In some distribution businesses, the proposed decision would require the removal of thousands of staff, less vegetation management, slower responses to outages and less frequent inspections and maintenance.

“The AER is not a technical or safety regulator and it’s not clear the due diligence has been done to assure consumers that network safety, public safety, outage response times and customer service will be maintained.

Mr Bradley noted that the effect of operating expenditure cuts would be greater for distribution businesses where staff redundancies are required and effectively backdated. In one case, this could mean an effective operating expenditure reduction of 60% below the regulatory proposal in the four years from 1 July 2015.

“These are the first draft decisions under a new regulatory framework using a new benchmarking technique so it is important not to lose sight of the potential customer impacts,” Mr Bradley said.

Under the *National Electricity Rules*, the AER was required to release its first-ever annual benchmarking report for the Australian distribution industry on 30 September 2014, so it would be available well before the first draft determination.

“The benchmarking analysis has only been released publicly now and seems to have been applied as a blunt tool to support retrospective cuts of up to 42% in distribution operating expenditure.”

Mr Bradley said the ENA and its members will seek an urgent briefing with the AER to discuss concerns about the outputs and use of the benchmarking analysis.

“Energy networks support the appropriate use of benchmarking by the AER which recognises differences in data sources and network circumstances..

“Benchmarking should not be used simplistically and the AER consultant report rightly notes that the Australian data alone produced model estimates that are “relatively unstable and unreliable’.”

“Given the scale of operating expenditure reductions, it would be important to understand how the model has used international data primarily from New Zealand and Ontario to inform conclusions about the efficiency of Australian networks,” Mr Bradley said.

Mr Bradley said it was important the final regulatory outcome encouraged investor confidence in stable, evidence-based regulation.

“Australian energy consumers rely on future investment to ensure new customers can be connected and assets can be replaced to maintain security and reliability,” Mr Bradley said.

He said electricity consumers would ultimately pay more for electricity if networks were prevented by the AER from prudent funding of operations, maintenance and reinvestment.

“Consumers don’t benefit from underinvestment and extreme cutbacks in maintenance, vegetation management or inspections.

“We have seen underinvestment in reliability in some States result in rushed and heavy-handed interventions by State governments mandating expensive reliability standards.

“Consumers end up paying more under this kind of ‘roller-coaster’ regulation where underspending is followed by higher cost catchup spending and political intervention.

“The ENA looks forward to more balanced final decisions that are in the long-term interests of electricity consumers,” Mr Bradley said.

ENDS.

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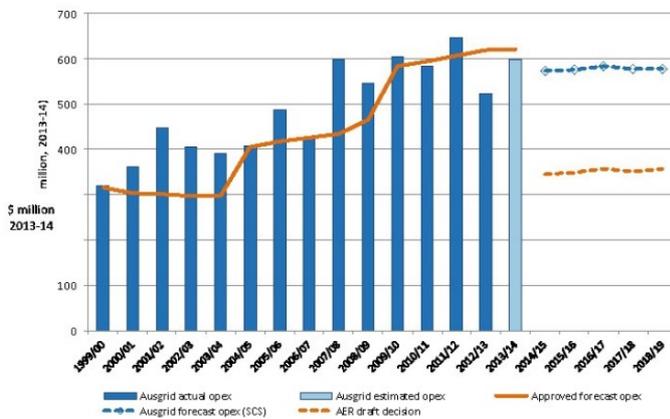
ENA is the peak national body for Australia’s energy networks; and represents gas distribution and electricity network businesses on economic, technical, environment and safety regulation as well as national energy policy issues.

AER CHARTS COMPARING OPERATING EXPENDITURE TO HISTORIC LEVELS

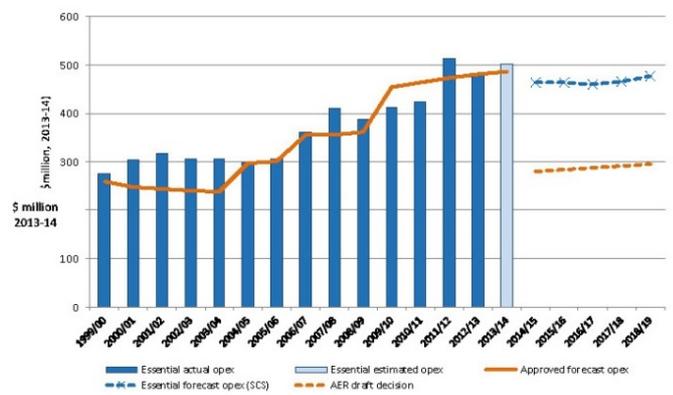
The charts below demonstrate that under the AER draft decision, the annual operating expenditure would be reduced to:

- A level not seen since 2001 in the case of Ausgrid and Essential Energy;
- A level not seen since 2003 in the case of Endeavour Energy; and
- Lower than any year since 2004/05 in the case of ActewAGL.

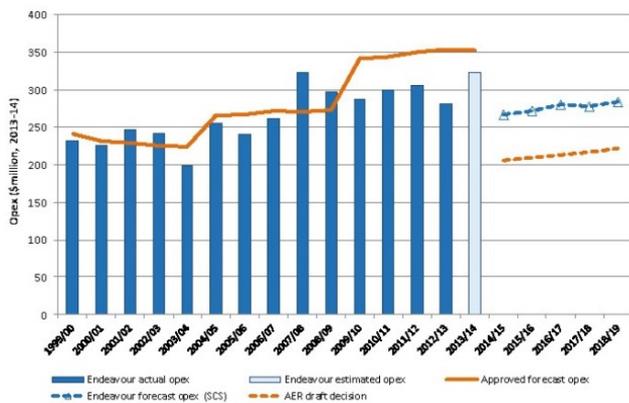
AER draft decision compared to Ausgrid's past and proposed opex (\$million, 2013-14)



AER draft decision compared to Essential Energy's past and proposed opex (\$million, 2013-14)



AER draft decision compared to Endeavour Energy's past and proposed opex (\$million, 2013-14)



AER draft decision compared to ActewAGL's past and proposed opex (\$million, 2013-14)



Source: AER Draft Decision Fact Sheets released 27 November 2014