Key topics nominated by the CAP – As discussed at Meeting held on 27 October 2022

	Issue	CAP input	ElectraNet input

1	**Price impact / Contingent Projects**
	• Higher interest rates and inflation have increased required revenue beyond AER Draft Decision expenditure cuts
	
	NOTE: as ElectraNet can't influence the Rate of Return, which is the biggest driver of the revenue increase, little can be done by ElectraNet or the CAP to influence price
		• ElectraNet to consider options to mitigate the impact for customers such as:
		  o Innovations to reduce capex costs without reducing the quality of supply
		  o Whether a more rigorous target can be set on opex productivity
		  o Is there a transition possibility where the full rate of return impact is not applied up front but is delayed?
		• Need to consider regional businesses' sensitivity to reliable supply – consistency of supply can be more important than price relief.
		• While related, the impact of contingent projects needs to be considered separately.
		• Important for ElectraNet to acknowledge and reflect a really clear understanding of the impact increased revenue will have on customers. Needs to be addressed in RRP as a really tough issue for many customers.
		• The CAP will look for ElectraNet to take leadership for exploring potential for innovation in ways that drive down cost without lost reliability in years to come – what might be possible to maintain reliability and reduce costs? There is not necessarily a straight line relationship between cost and reliability – it can be bent.
		• The DMIAM is worth exploring.
		• ElectraNet should be open to raising affordability concerns with SA Government and AER to explore actions to reduce the adverse impacts of increasing power costs for customers.
		• Important to bear in mind that the transmission component of residential power bills is ~11% compared with Federal Budget projection of 56% bill increases. Other elements are driving up costs, primarily higher gas prices driven by global events.
		• Capex deferral may only create further risk and cost so needs to be carefully considered.
			• ElectraNet does not consider further reductions in expenditure programs to be acceptable:
			  o Reducing capex beyond the current level would lead to unacceptable risk to ElectraNet and customers in the short to medium term (safety, fire, supply interruption). Material new capex requirements have already arisen since ElectraNet's Revenue Proposal that will need to be absorbed within the AER capex allowance.
			  o A stricter opex productivity target would have little impact on price but would force ElectraNet to reduce maintenance or other expenditure. This too would lead to unacceptable risks in the short to medium term.
			• ElectraNet will continue to pursue capex and opex efficiencies wherever possible, incentivised by the EBSS and CESS, and pursue innovations through the NCIPAP and DMIAM measures.
			• The Rate of Return is set by the AER under the Rules, with the relevant instrument to be updated in December. There is no scope for ElectraNet to vary from this or influence prevailing market rates.
			• ElectraNet recognises and shares the concern of customers over the affordability of electricity in the context of rising energy costs, and remains committed to driving down its costs, exploring innovations and playing its broader role in enabling the energy transition to cleaner and more affordable energy.

	Issue	CAP input	ElectraNet input

2	**Capital Expenditure Sharing Scheme (CESS)**
	• Some SA-NSW interconnector project (PEC) capex was delayed into next regulatory period
	• ElectraNet reprioritised previously deferred capital projects to 'fill the gap' left by this deferral
	• ElectraNet's reprioritisation means that there is no windfall gain from the PEC capex deferral
	• ElectraNet strongly believes that AER Guideline conditions for making a capex deferral adjustment have not been met
		• Given timing there was limited opportunity for engagement on this topic with the previous CAP.
		• This warrants consideration by the new CAP prior to the Revised Revenue Proposal being lodged.
		• CAP sought and obtained additional information to enable it to identify next steps for engagement, including ElectraNet's letter of May 2022 on which it consulted with the previous CAP and a further response to the AER of August 2022 on this issue.
		• Understand delay of PEC but don't want windfall gain. ElectraNet said it brought projects back so that there is no CESS gain, nor loss.
		• There ought to be a clear statement from the CAP of its position here.
		• The information provided by ElectraNet was helpful, though the tables were not as clear as they could have been. However, on balance ElectraNet's position is accepted that the relevant projects were largely considered by the CAP and the AER in the previous revenue reset process.
		• Key question is whether the projects brought back are legitimate under CESS rules and if so, ElectraNet should not carry much of a CESS penalty or gain.
		• The CAP concluded that ElectraNet should not be subject to a windfall gain or penalty and that the penalty of ~$2-3m that results with no PEC capex deferral adjustment is the right outcome.
			• ElectraNet agrees no windfall gain should occur under the CESS due to the deferral of Project EnergyConnect.
			• No windfall gain will occur as ElectraNet has efficiently reprioritised its capital program by bringing forward previously deferred expenditure to offset the deferral.
			  ○ The bulk of these projects (over 80%) were presented in our Revenue Proposal for the current period and have been scrutinised previously by customers.
			• There is therefore no need for a deferral adjustment, which would only impose a windfall penalty on ElectraNet (of over $20m).
			  ○ The risk for customers is that imposing a windfall penalty would discourage network businesses from efficiently prioritising their capital programs in future. It would also leave a revenue shortfall for ElectraNet, putting pressure on expenditure elsewhere and increasing risk.
			• The removal of the deferral adjustment leaves ElectraNet a small underlying penalty (~$2-3m).
			• It is in the interests of customers that the signals sent to ElectraNet and other TNSPs drive efficient investment decisions.
			• ElectraNet has addressed the AER's concern that customers did not have an opportunity to scrutinise the projects brought forward, showing that the majority of the delayed projects brought back had been considered by the CAP and the AER in the previous revenue reset process five years ago.
			• ElectraNet has continued to engage on this with the AER, and there is growing shared understanding of the matter.

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3	**Insurance costs** • AER cut ElectraNet's proposed step change by ~$15m over the regulatory period • This cut will be reduced in Final Decision following conversation between ElectraNet and AER staff once ElectraNet's higher FY23 insurance costs are considered *NOTE: under the cost pass through mechanism if insurance costs exceed forecasts materially the extra can be 'passed through' to customers.*	• Insurance and cyber security were subject to detailed consumer scrutiny by the previous CAP. This built a shared understanding of the risk balance. • The AER Draft Decision focused on the prudent cost, so the CAP is comfortable with the AER and ElectraNet coming to an outcome. • The CAP sought and obtained information on the costs of insurance to date in the current regulatory period relative to the 1% pass through threshold. • The CAP has been through risk sharing and other aspects a year ago and needn't review again. • It's about getting the right level of coverage and doing so at the best possible price. CAP member organisations face similar challenges in relation to insurance.	• ElectraNet will shortly submit a cost pass through application for FY23, which will provide the missing information about current year costs and restore most of the original forecast. • ElectraNet is not seeing a need to expand its insurance cover or increase the forecast based on the latest information. • ElectraNet does not agree in principle with the 'scale factor' reduction made by the AER (of around $6m) but proposes to accept this in the Revised Revenue Proposal.
4	**Cyber step change** • ElectraNet proposed an opex increase to fund cost of improving cyber security • AER's advisor considered cost increase excessive • AEMO is soon to release V2 of AESCSF with implications for Security Profile 3 – raises the bar appreciably • ElectraNet is revisiting cost analysis • Thorough understanding of cost may not be ready in time for submission of Revised Revenue Proposal	• Insurance and cyber security were subject to consumer scrutiny by the previous CAP. • Check that the forecasts on cyber security are commensurate with other networks. • Is ElectraNet taking adequate action or only the bare minimum? Ascertain that SP3 is the target and how does that sit with broader risks? • For consideration: Is the AER looking at cybersecurity from a 'whole of economy' perspective, given the impact of loss of supply to businesses, particularly the mining industry? • ElectraNet to update the CAP regularly in managing cyber security given the dynamic environment. • The key issue is what is prudent? • Important to have updated information in advance of the Revised Revenue Proposal to allow the opportunity for the CAP to engage and consider this issue in its submission.	• ElectraNet has learned that AEMO shortly plans to increase the compliance level for industry target Security Profile 3 (SP3) in the release of version 2 of the AESCSF. • ElectraNet is revisiting its cost analysis to reflect the cost implications of the higher SP3 requirements. • ElectraNet will provide further cost information to the CAP as it becomes available, which may not be fully settled by the time the Revised Revenue Proposal is submitted. This may require a best estimate to be submitted at the time and updated subsequently. • Separately, the AER did not accept pass through for cyber related costs if insurance becomes unavailable or is exhausted. ElectraNet will also be responding to this.

	Issue	CAP input	ElectraNet input
5	**Renewable Energy Zones** • The CAP has expressed an interest in learning about the future planning of the network, particularly Renewable Energy Zones (REZs) • ElectraNet proposed a pass through for the costs of preparing REZ Design Reports • AER did not accept pass through event, which was not subject to a 1% materiality threshold	• CAP needs to understand the network's capacity to accommodate Renewable Energy Zones. This includes the pace of change, and emissions reporting by businesses. • Where is SA is sitting from a national perspective? • ElectraNet agreed to provide its 2022 Transmission Annual Planning Report (due 31 October 2022) and to engage with the CAP on the development of REZs during its ongoing planning cycle. • Important that REZ development is on the agenda for CAP in the next phase. Also note interrelationship with land compensation issues. • Whether the existence of REZ means that TNSPs will focus less on other places, thus limiting access to network in other areas? How do REZs interact with other works, infrastructure and planning programs? Issue for ongoing CAP engagement.	• There are two issues: o The development of Renewable Energy Zones will occur as required by AEMO's Integrated System Plan. These projects automatically become contingent projects if required and do not need to be addressed in the Revised Revenue Proposal. ElectraNet plans to engage with the CAP on these developments during its annual planning cycle. It is also undertaking a REZ development study for the SA Government, outcomes of which will inform this engagement in 2023. o ElectraNet plans to include the expected cost of preparing REZ Design Reports (which are intended to address questions such as those above) in the revised opex forecast.
6	**Inertia Services** • ElectraNet is tendering for inertia services required by AEMO in FY24 and FY25 • Under network support pass through arrangements, costs will either be recovered at the time with a small true-up in arrears, or fully recovered in arrears • Placeholder cost estimate is $6.7m pa based on historical outcomes	• The CAP recommended that ElectraNet submit an estimate of expected cost upfront and have smaller variations later. • Price certainty and stability are important to customers and it's better to create budget/ cost clarity for customers than not to. • The impact of synchronous condensers and their impact on inertia was discussed given that they are recent, noting they have reduced the requirement for inertia and associated costs to customers. • Difficult for CAP to know whether the cost is the right number. Role is limited to ensuring process/ governance is reasonable. Would see it as AER role to review numbers in more detail e.g. by reference to experience elsewhere.	• [redacted] • However, negotiations may not be finalised in time for the Revised Revenue Proposal. • This may require a best estimate to be submitted at the time and updated subsequently. • ElectraNet will provide full information on the tender process in Revised Revenue Proposal to allow assessment of the prudency of the process undertaken, even if costs are not final at that time. • Critical to have firm estimates by the end of 2022 to enable meaningful consultation.

Additional matters being addressed in the Revised Revenue Proposal

Issue	Proposed Approach
Cloud Migration step change	• The AER rejected ElectraNet's proposed 'cloud migration' step change ($9.0m) as it expects the benefits of migrating to outweigh the relevant costs. • While ElectraNet does not agree with this in principle, we propose to accept the AER's Draft Decision.
Escalation	• Inflation to be applied consistently throughout the revised forecasts based on updated inflation outlook to be issued by the RBA in its Statement on Monetary Policy on 4 November 2022. • The AER will update escalation again in Final Decision based on Feb 2023 RBA Statement on Monetary Policy.

Incentive schemes	• Efficiency Benefit Sharing Scheme (EBSS)
	  o designed to reward opex efficiency and penalise inefficiency
	  o updated opex forecast leads to larger penalty ($14m) - i.e. $3m larger revenue reduction compared to Draft Decision ($11m penalty)

Demand Management Innovation Allowance Mechanism (DMIAM)	• DMIAM is intended to fund R&D by TNSPs to reduce long term network costs through improved demand management
	• Key features:
	  o Funding of 0.1% of annual revenue (~$2.1m max)
	  o Endorsement of projects by independent panel or CAP with engineering expertise (supported by additional funding up to $200,000)
	  o Allowances can be combined with other TNSPs or across periods to fund larger projects
	• ElectraNet proposes a role for the CAP to review projects (independent endorsement)

Rule change step change (system complexity, REZ Design Reports, Rule changes)	• Taking action to manage an increasingly complex power system with 100% renewable energy and mitigating growing system security risks
	• Capability uplift required across system planning and operations (e.g.)
	  o Near real time modelling
	  o Control room monitoring / alarms
	  o Network outage management
	• Indicative need for 10-20 FTEs for various functions
	• Includes new Rule change obligations previously identified and REZ Design Reports (as above)
	• Also includes the impact of a recently advised increase in SA Government licence fees of approximately $2.3m.