evoenergy

Appendix 1.1: 2019–24 period capital expenditure

Regulatory proposal for the ACT electricity distribution network 2024–29

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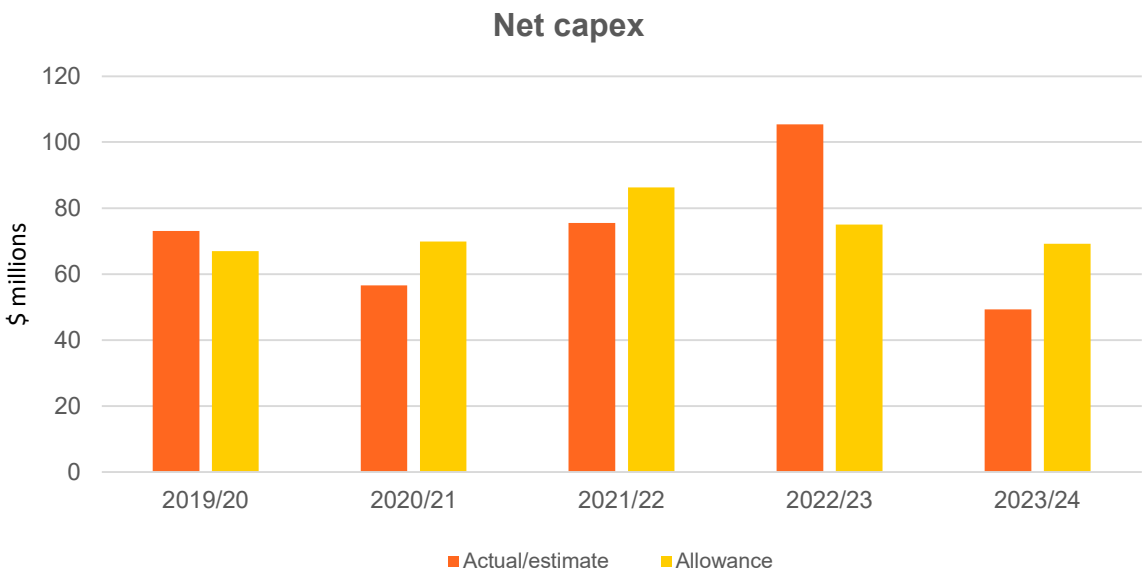
1. Overview

The purpose of this document is to demonstrate that Evoenergy's capital expenditure (capex) during the 2019–24 regulatory period has been prudent and efficient, with investments undertaken consistent with good industry practice and in the long-term interests of our customers.

This document presents comparisons between the capital expenditure forecast contained in the Australian Energy Regulator's (AER) distribution determination for Evoenergy's current 2019–24 regulatory period (regulatory allowance) against our actual and estimated capital expenditure (referred to as actual expenditure). It has been adjusted for the time value of money for ease of comparison. Consistent with our 2024–29 regulatory period proposal, all dollars are in $2023/24 unless otherwise stated.

We expect to underspend against our regulatory allowance by $7 million or two per cent for the current regulatory period (2019–24). Figure 1 shows our allowance and estimated net capex[1] for the period. Table 1 sets out our allowed and estimated expenditure by capex expenditure category. Variances contributing to this overall result are explained by capex category in each section below.

Figure 1 Current period capex against allowance ($ million, $2023/24)



[1] Net capital expenditure is gross capital expenditure less capital contributions and asset disposals.

Table 1 Summary of current period capex against allowance ($ million, $2023/24)

Expenditure category	Allowance	Actual/estimate	Variance (actual less allowance, $m)	Variance (%)
Repex	107.3	95.2	-12.1	-11.3
Augex*	64.2	58.0	-6.1	-9.6
Net connections	54.1	36.3	-17.8	-32.9
Non-network	65.4	90.1	24.7	37.7
Capitalised overheads	77.6	84.4	6.8	8.8
Disposals	1.4	4.0	2.7	197.5
Total	**367.3**	**360.0**	**-7.3**	**-2.0**

* Includes 'reliability and quality' capex.

Note: variance ($) may not sum from totals due to rounding.

Table 2 provides a year by year breakdown of Evoenergy's current regulatory period (2019–24) capex against the total regulatory allowance. Evoenergy is expected to underspend its allowance in three years and overspend in two years (2019/20 and 2022/23).

Table 2 Evoenergy current period capex program by category ($ million $ June 2024)

	2019/20	2020/21	2021/22	2022/23	2023/24	Total
Repex	15.2	15.4	17.1	25.3	22.1	**95.2**
Customer initiated	35.9	27.6	30.8	42.7	27.2	**164.2**
Augex	9.4	9.3	11.6	7.8	14.9	**53.0**
Reliability and Quality	0.6	0.6	1.0	1.0	1.8	**5.0**
Non-network	12.6	11.7	16.0	31.6	18.1	**90.1**
Capitalised overheads	19.6	14.1	14.4	19.4	16.8	**84.4**
Gross capex	93.4	78.8	91.0	127.9	100.9	**491.9**
Capital contributions	19.7	21.5	14.5	21.1	51.1	**127.9**
Disposals	0.6	0.7	0.9	0.9	0.9	**4.0**
Net capex	**73.1**	**56.6**	**75.5**	**106.0**	**48.9**	**360.0**
Allowance	**66.9**	**69.9**	**86.3**	**75.0**	**69.1**	**367.3**
Variation	**6.1**	**-13.3**	**-10.8**	**31.0**	**-20.3**	**-7.3**

Note: individual numbers may not sum to the total due to rounding.

Evoenergy must make efficient investment decisions, consistent with the long-term interests of our customers, based on the best information available at the time of that investment decision, even if this information is different from that which formed the basis of our capex allowance. Over a five year period, typically, variances will arise between our allowance and actual capex, particularly at a category level. Often unforeseen circumstances will drive these adjustments to our capital works program. This is particularly the case for categories such as connections expenditure, which are led by customer requests and developments, and therefore, difficult to precisely forecast over a five year period.

The regulatory framework provides incentives to Evoenergy as a distribution network service provider (DNSP) to continuously optimise the efficiency of its capex, that is, only undertake necessary investments. Unexpected changes affecting investment have occurred during the current regulatory period (2019–24). This is because Evoenergy continues to invest to meet regulatory obligations and customer service expectations that have driven investing in capital projects not foreseen at the time our regulatory allowance for 2019–24 was set. Investments include obligations to maintain safety and reliability and to connect and meet new customer demand. Conversely, prudent capital planning can also lead to deferring projects previously thought to have been required in the 2019–24 regulatory period.

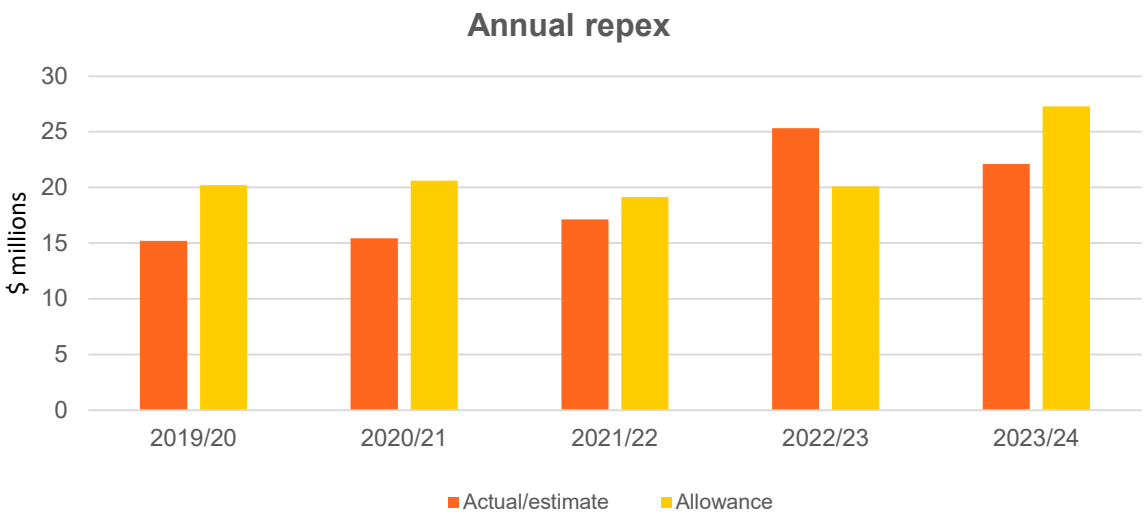
Additionally, the Capital Efficiency Sharing Scheme (CESS) provides further incentives to efficiently optimise capex, while ensuring that we still meet customer expectations. As set out in Attachment 4 to our regulatory proposal, we may receive a small CESS payment during the next regulatory period based on our capex spend against the allowance during the current regulatory period (2019–24). The benefits of capex efficiencies are ultimately shared with consumers through lower network prices. In approaching the CESS, Evoenergy has had regard to the AER's Capital Expenditure Incentive Guideline for Electricity Network Service Providers.

2. Replacement expenditure

Replacement expenditure (repex) occurs to replace or refurbish parts of the existing network which have reached the end of their economic lives with modern equivalents. Repex is required to continue to maintain our current levels of network service, consistent with our customer's expectations and our regulatory obligations.

Evoenergy estimates that its actual repex for the current regulatory period (2019–24) will be $95 million ($2023/24). This is 11 per cent lower than our regulatory allowance of $107 million. Figure 2 shows how repex has been tracked on a year-by-year basis. The expected underspend has been driven by lower repex in the first two years of the current regulatory period (2019–24). For the remainder of the 2019–24 regulatory period, Evoenergy expects repex will track relatively closely to the regulatory allowance.

Figure 2 Current period repex (actual vs. allowance, $ million, $2023/24)



During the current regulatory period, the distribution pole asset strategy was reviewed to improve Reliability Centered Maintenance (RCM) to better understand the asset's condition and associated risk. The criteria for condemning poles were subsequently adjusted, and the number of poles requiring replacement was reduced in the current regulatory period.

Partly offsetting this reduction in repex (due to lower numbers of poles being replaced), there was an increase in low voltage (LV) pillar, high and low voltage cable and distribution substation replacements as a result of asset failures (historically replaced reactively). Zone substation repex increased in the 2019–24 regulatory period due to an unplanned power transformer replacement due to poor conditions (Telopea Park). Additional repex uplift in the 2023 financial year has come from targeted repex post-storm event damage repair and will continue depending on storm events into the 2024 financial year.

3. Augmentation expenditure

Augmentation expenditure (augex) enlarges our network and its capacity to distribute electricity or improves the quality or capability of the distribution network. For analytical and reporting purposes in this Appendix, augex reflects two different categories:

- **Augex** — which is primarily demand driven. Expenditure is required due to forecast growth in the maximum demand of our customers. It also includes some non-demand driven capex, such as on secondary systems.
- **Reliability and quality capex** — expenditure that reflects other factors than demand growth, including power quality issues and regulatory compliance obligations.

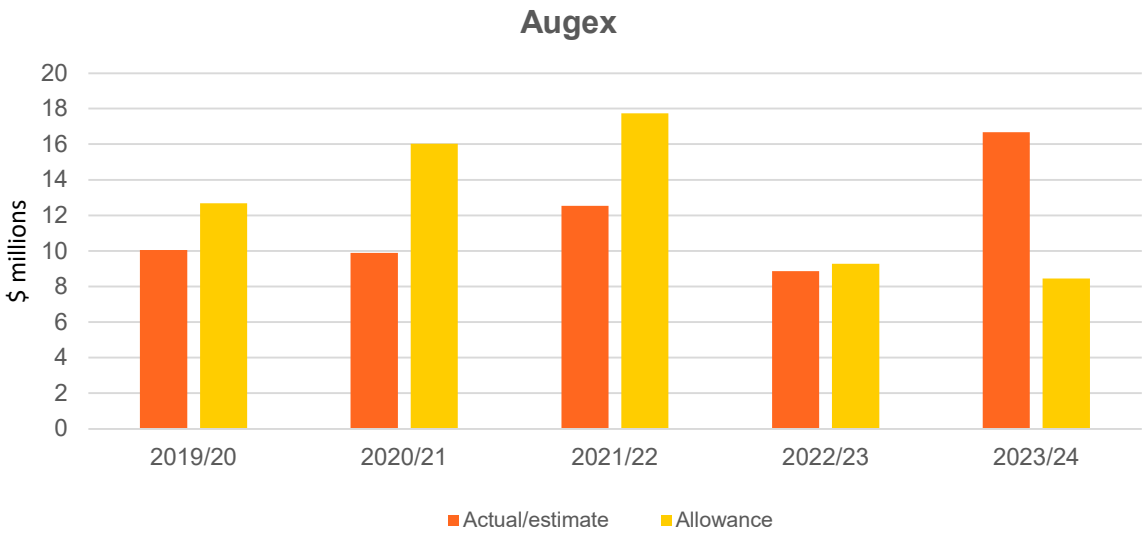
Evoenergy estimates that its total augex for the current regulatory period (2019–24) will be $58 million ($2023/24), $53 million of demand driven augex, and $5 million of reliability and quality capex. This is six million, or 10 per cent lower than our combined regulatory allowance for these two categories ($64 million).

During the 2019–24 regulatory period, Evoenergy identified that development and subsequent load growth in some areas were slower than forecast, resulting in the deferral of several planned augmentation projects. While the delays were partially driven by slower growth due to shutdowns and supply chain difficulties from the pandemic, Evoenergy has also improved the probabilistic planning methodology to better account for common third-party project delays. Appendix 1.15 (Demand Driven Augmentation Capital Expenditure Business Case) contains more information on the probabilistic planning methodology. It is also worth noting that conversely, some augmentation projects were required but not part of our allowance, as also discussed in Appendix 1.15.

Overall, Evoenergy has invested in new capacity quite conservatively in the current 2019–24 regulatory period. Given that the national 2021 census revised an increase in the ACT's population growth between 2016 and 2021,[2] this has affected our forward program for augex (i.e., in the 2024–29 regulatory proposal, as we have identified growing constraints on our network). This is also discussed in Attachment 1.

[2] After rebasing for the 2021 census, the ACT's estimated population in June 2021 increased from 432,000 to 454,000, over 20,000 residents.

Figure 3 Current period augex (actual vs. allowance, $ million, $2023/24)



4. Connections expenditure

Connections expenditure is required for connecting new customers to our network and augmenting or altering existing network connections. Evoenergy's gross capex on connections is offset by customer contributions to the works to yield net connections capex.

Evoenergy forecasts that gross connections capex ($164 million) will be higher than the regulatory allowance ($124 million), as shown in Figure 4. This is driven by a significant forecast increase in connections works in 2022/23 and 2023/24. Evoenergy's Customer Initiated Works Report, in Appendix 1.21 contains further information on the connections program, including a disaggregation by the category of connections work.

Evoenergy estimates its net connections capex for the current regulatory period (2019–24) will be $36 million ($2023/24). This is $18 million or 33 per cent lower than our regulatory allowance ($54 million). Although gross connections capex ($164 million) is higher than the regulatory allowance ($124 million), this is more than offset by higher than forecast capital contributions ($119 million compared to $70 million), giving rise to lower net connections capex than the regulatory allowance.

Figure 4 Current period gross connections capex (actual vs. allowance, $ million $2023/24)

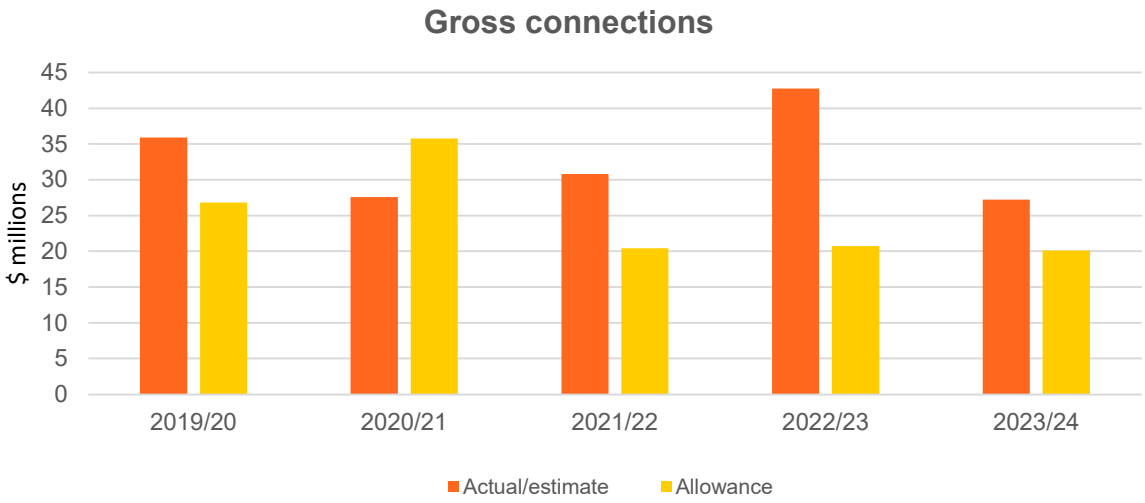


Table 3 Current period connections capex and variance to allowance ($ million, $2023/24)

	Allowance	Actual/estimate	Variance ($m)	Variance (%)
Gross connections	124	164	40	33
Capital contributions	70	128	58	84
Net connections	**54**	**36**	**-18**	**-33**

As seen in Figure 5, Evoenergy's (net) connection expenditure generally exceeded the allowance throughout the 2019–24 period, except for a negative net capex amount in 2023/24. This relatively unusual occurrence is due to a timing issue, with Evoenergy forecast to receive a large capital contribution from a single (high voltage) customer in 2023/24 after the work done in 2022/23 (Harman Zone Substation). Due to this timing issue, the forecast capital contributions in 2023/24 exceed Evoenergy's forecast gross connections capex, giving rise to a counter intuitive negative number in this financial year.

Figure 5 Current period net connections capex (actual vs. allowance, $ million, $2023/24)

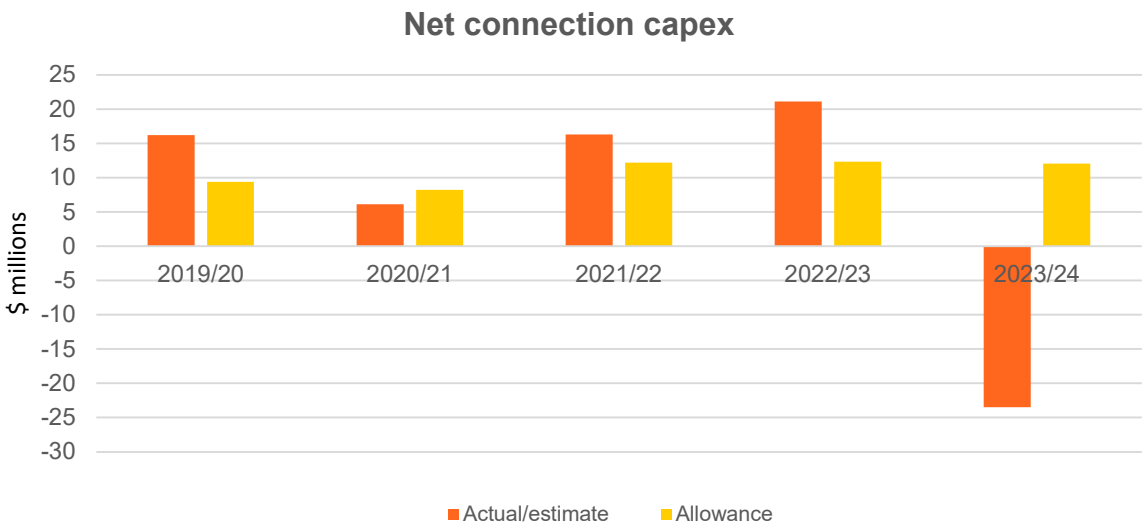
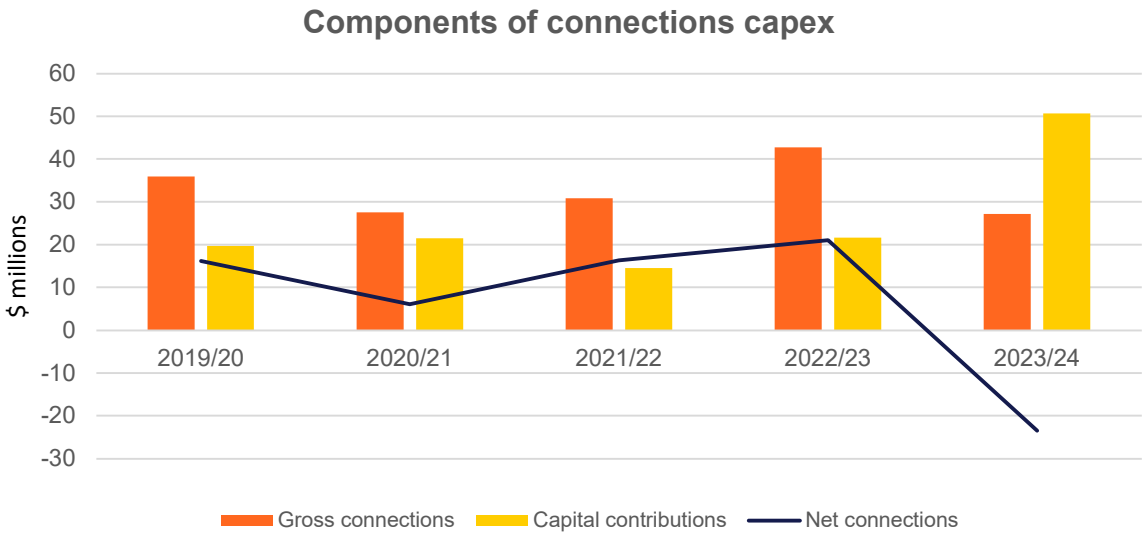


Figure 6 shows Evoenergy's gross connections capex, and capital contributions by year to further illuminate the trends shown in Figure 5. The temporal division between work done on the HMAS Harman Zone Substation (2022/23) and the estimated receipt of capital contribution (2023/24) can be observed by the increase in gross connections capex in 2022/23 and then the increase in capital contributions in 2023/24. This explains the atypical difference between gross capex and capital contributions in these two years.

Figure 6 Current period actual/estimated connections capex ($ million, $2023/24)



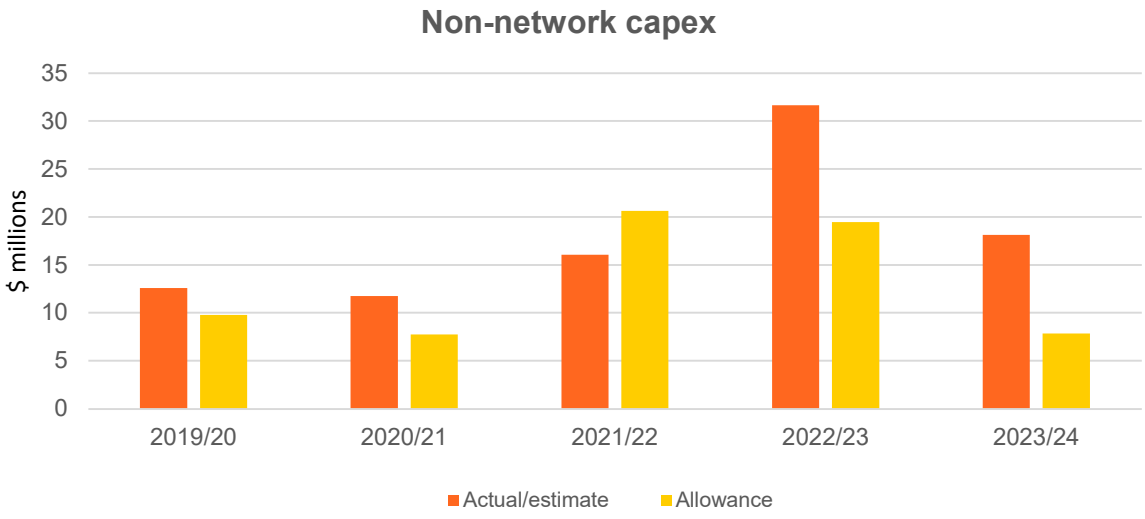
5. Non-network expenditure

Non-network capex is expenditure on assets that are used to support the operation of our network and delivery of standard control services to customers. Non-network expenditure is grouped into four separate categories in the AER's Regulatory Information Notice (RIN):

- Information and communications technology (ICT) and equipment;
- Motor vehicles;
- Property; and
- Other non-network.

Evoenergy estimates that its total non-network capex for the current regulatory period (2019–24) will be $90 million ($2023/24). This is $25 million or 38 per cent higher than our regulatory allowance of $65 million. As shown in Figure 7, Evoenergy anticipates a significant overspend in the final two years of the current regulatory period (2019–24).

Figure 7 Current period non-network capex (actual vs. allowance, $ million, $2023/24)



Given the diverse categories comprising non-network capex, Evoenergy discusses key reasons for variance from the allowance in the below subsections by a component of non-network capex.

ICT capex

Evoenergy estimates that its ICT capex for the current period will be $37 million ($2023/24). This is two million or five per cent higher than our regulatory allowance.

Evoenergy has progressed effectively in delivering the IT programs described in the 2019–24 regulatory proposal. Significant progress has been made on Advanced Distribution Management System (ADMS) upgrades. The project recently completed Phase 3, involving software installation, training and testing. More information on this project is in the box on the following page.

The Gentrack Velocity billing solution has been extended to meet compliance with five minute global settlement rules. These two projects account for almost half of the investment across the current capital expenditure.

ADMS upgrade

On 19 November 2022, SCADA, Inter Control Centre Communication Protocol (ICCP) and Reports were successfully transitioned from an end of life version to a version with vendor support for an additional five years. Core system changes include:

- Introduction of the Energy Management System (EMS), providing an integrated transmission network view and expanding all functionality available through the existing Distribution Management System (DMS) to the transmission level.
- Addition of Arch Flash module to facilitate the calculation of incident energy values associated with planned switching.
- Implementation of the supported ADMS Supervisory Control and Data Acquisition (SCADA) management system replacing the existing system
- Addition of more integrations including weather data and ability to share information with other systems such as Beakon and the Integrated Vehicle Management System (IVMS).
- Updated user interface with more intuitive operation and enhanced usability.

A brief overview of key programs outcomes and achievements delivered to date has been provided in section 2 of the Technology Plan, contained in Appendix 1.22.

Motor vehicles

Evoenergy estimates its motor vehicles capex for the current regulatory period (2019–24) will be $13 million ($2023/24). This is one million or one per cent lower than our regulatory allowance ($14 million). As a result, Evoenergy's actual capex on motor vehicles in the current period is expected to be closely aligned with the regulatory allowance.

Evoenergy's capex on motor vehicles occurs in the context of our fleet strategy.

The Evoenergy Fleet Strategy governs fleet asset selection, management, operational targets, safety and environmental strategies to achieve an efficient fleet. The strategy includes:

- Standards in safety, ergonomics, systems and environment sustainability.
- Controls in fleet asset selection and options, cost reduction, maximising the fleet by managing vehicle to staff ratio, and key performance indicators (KPIs) to set expectations for drivers and managers.
- Process fleet asset replacement and assessment to reduce whole of life costs.
- Maximising lease arrangements for all asset classes (i.e., passenger, light commercial, trailers, plant and heavy vehicles).
- Transition to electric and hydrogen vehicles where they meet operational needs and the whole of life costs are comparable to that of conventional vehicles. However, current costs are likely to be somewhat higher, reflecting the relative infancy of zero emission vehicles (ZEVs).
- Continue to leverage expertise and efficiencies from our fleet management organisation in managing the fleet.

The benefits of the strategy are to build a fleet that is efficient, cost effective and can adapt swiftly to changes in the energy sector, enabling Evoenergy to meet its strategic objectives and operational business requirements.

Property

Evoenergy estimates that its property capex for the current period will be $22 million ($2023/24). This is $15 million or 199 per cent higher than our regulatory allowance ($7 million).

The uplift in spend on property (buildings) in the current regulatory period (2019–24) primarily relates to the following upgrades to Evoenergy's Greenway office and depot:

- Greenway Depot Properties Program;
- Greenway South Refurbishment; and
- Greenway Property Works.

The costs of the works have been adversely affected by the increase in construction costs during the current 2019–24 regulatory period (refer to the BIS Oxford Cost Escalation Report in Appendix 1.7). These works at Greenway are slated primarily for the final two years of the current regulatory period, 2022/23 and 2023/24.

The key driver of the project is to consolidate Evoenergy's existing leased site at Fyshwick which expires on 30 June 2023 into the existing footprint at the Greenway office and depot. The project will also allow all Evoenergy staff to be centrally located to improve collaboration and improve our physical security, parking and traffic flow.

Other non-network

Evoenergy estimates its other non-network capex for the current regulatory period (2019–24) will be $18 million ($2023/24). This is $9 million or 104 per cent higher than our regulatory allowance.

Other non-network capex includes corporate services and business support. In simple terms, this is capex that occurs on tools, equipment and devices across divisions such as the finance division, people and legal, technology (operation/security and engineering) and the CEO.

In the current regulatory period (2019–24), expenditure of more than $7 million on the replacement of the aged Financial Information Management System (FIMS)[3] has contributed to Evoenergy spending higher than its allowance in this category. There was also further spending on property and facilities for Bunda Street and the Facilities Asset Management Plan Replacement program.

[3] And a regulatory dispensation allowing Evoenergy to categorise this spend as capex rather than opex.

6. Capitalised overheads

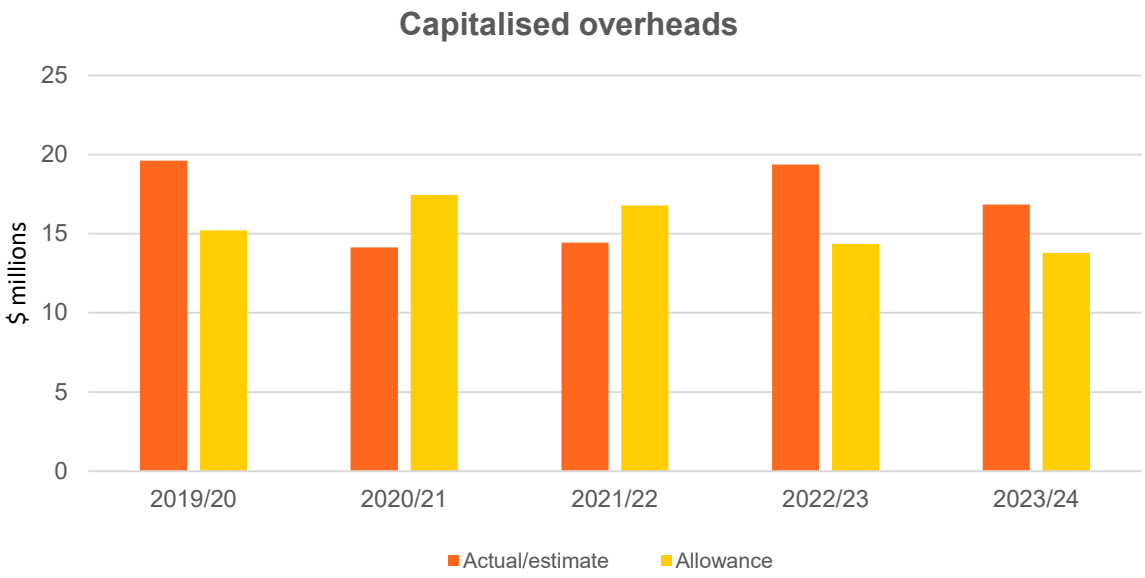
Our total capital expenditure for the current regulatory period includes an amount reflecting the capitalised portion of our overhead expenditure. This approach reflects that some of the activities we carry out as a business which are classified as overhead in nature, are necessary to support the delivery of our capital works program.

Our capitalised overheads are primarily driven by Evoenergy's share of the fixed price servicing charge (FPSC). The FPSC covers corporate overhead costs such as legal, human resources, executive, economic regulation and others. The FPSC is allocated evenly across Evoenergy's program of works from year to year.

Consider a hypothetical example where Evoenergy spent $50 million on capex, $30 million on opex and $20 million on maintenance in a given year and had a $20 million charge under the FPSC. Its share of corporate overheads that would be capitalised would be 0.5 (*$50 million ÷ $100 million*), and thus capitalised corporate overheads would be $10 million (*0.5 × $20 million*).

We estimate that our total capitalised overheads for the current regulatory period (2019–24) will be $84 million. Our estimated capitalised overheads expenditure for this period is 9 per cent higher than our allowance for this category. This reflects slightly higher than anticipated charges under the FPSC over the 2019–24 regulatory period.

Figure 8 Current period capitalised overheads (actual vs. allowance, $ million, $2023/24)



Abbreviations

Abbreviation	Meaning
ADMS	Advanced Distribution Management System
AER	Australian Energy Regulator
CESS	Capital Efficiency Sharing Scheme
DNSP	Distribution Network Service Provider
FIMS	Financial Information Management System
FPSC	Fixed Price Servicing Charge
ICT	Information and Communications Technology
MPFP	Multilateral Partial Factor Productivity Index
MTFP	Multifactor Total Factor Productivity
RAB	Regulatory Asset Base
RCM	Reliability Centered Maintenance
RIN	Regulatory Information Notice
ZEV	Zero Emission Vehicles