DRAFT DECISION
Evoenergy
Distribution Determination

2019 to 2024

Attachment 10

Service target performance incentive scheme

September 2018

AUSTRALIAN ENERGY REGULATOR

Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Tel: 1300 585 165
Email: AERInquiry@aer.gov.au

Note

This attachment forms part of the AER's draft decision on the distribution determination that will apply to Evoenergy for the 2019–2024 regulatory control period. It should be read with all other parts of the draft decision.

The draft decision includes the following documents:

Overview

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency benefit sharing scheme

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Attachment 10 – Service target performance incentive scheme

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Contents

Shortened forms

Shortened form	Extended form
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
capex	capital expenditure
CCP10	Consumer Challenge Panel (subpanel 10)
CESS	capital expenditure sharing scheme
EBSS	efficiency benefit sharing scheme
F&A	framework and approach
GSL	guaranteed service level
NER	national electricity rules
opex	operating expenditure
SAIDI	system average interruption duration index
SAIFI	system average interruption frequency index
STPIS	service target performance incentive scheme
VCR	value of customer reliability

10 Service target performance incentive scheme

Under clauses 6.3.2 and 6.12.1(9) of the National Electricity Rules (NER) our regulatory determination must specify how any applicable service target performance incentive scheme (STPIS) is to apply in the next regulatory control period.

This attachment sets out our draft decision on how we will apply the STPIS to Evoenergy for the 2019–24 regulatory control period.

AER's service target performance incentive scheme

We published the current version of our national STPIS in November 2009.[1] The STPIS is intended to balance incentives to reduce expenditure with the need to maintain or improve service quality. It achieves this by providing financial incentives to distributors to maintain and improve service performance where customers are willing to pay for these improvements.

AER framework and approach (F&A) to the application of STPIS

In the final F&A, we stated that we will continue to apply the distribution STPIS to Evoenergy in the next regulatory control period. We proposed to:

- set revenue at risk at ± 5 per cent
- segment the network according to the urban and short rural feeder categories
- apply the system average interruption duration index or SAIDI, system average interruption frequency index or SAIFI and customer service (telephone answering) parameters
- set performance targets based on Evoenergy's average performance over the past five regulatory years
- apply the method in the STPIS for excluding specific events from the calculation of annual performance and performance targets
- apply the method and value of customer reliability (VCR) values as indicated in AEMO's 2014 Value of Customer Reliability Review final report.[2]

Our F&A also stated that the:

- Guaranteed service level (GSL) component will not apply to Evoenergy if it remains subject to a jurisdictional GSL scheme.[3]

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1 AER, *Electricity distribution network service providers—service target performance incentive scheme*, November 2009. (AER, *STPIS*, November 2009).

2 AER, Framework and approach ActewAGL Regulatory control period commencing, 1 July 2019 to 30 June 2024, July 2017, pp. 51–52.

3 AER, Framework and approach ActewAGL Regulatory control period commencing, 1 July 2019 to 30 June 2024, July 2017, p. 52.

- revised STPIS may apply Evoenergy in the next regulatory period if the review of the STPIS is completed on time.[4]

10.1 Draft decision

Our draft decision is to apply the STPIS as is to Evoenergy for the 2019–14 regulatory control period. This is consistent with our F&A position on the application of the STPIS in our 2019-24 determinations for NSW and ACT distributors.

We have taken into account Evoenergy's revenue proposal, submissions raised by stakeholders and the F&A in reaching our draft decision.[5] Our responses to the matters raised by Evoenergy and stakeholders about the application of the STPIS are discussed below.

Table 10-1 and Table 10-2 present our draft decision on the applicable incentive rates and targets that will apply to Evoenergy for the 2019–24 regulatory period. The incentive rate for the customer service component will be –0.040 per cent per unit of the telephone answering parameter.[6]

Table 10-1 Draft decision—STPIS incentive rates for Evoenergy for the 2019–24 regulatory period

	Urban	Short rural
SAIDI	0.07243	0.00918
SAIFI	4.00511	0.52635

Source: AER analysis.

4 AER, Framework and approach ActewAGL Regulatory control period commencing, 1 July 2019 to 30 June 2024, July 2017, p. 52.

5 Evoenergy, Revenue Proposal Attachment 10: Incentive schemes Regulatory proposal for the ACT electricity distribution network 2019–24, January 2018, pp. 7–16; Consumer Challenge Panel, CCP10 Response to Evoenergy regulatory Proposal 2019-24 and AER Issues Paper: May 2018, p. 17; AER, Framework and approach ActewAGL Regulatory control period commencing, 1 July 2019 to 30 June 2024, July 2017, p. 52;

6 AER, *STPIS*, November 2009, cl. 5.3.2(a).

Table 10-2 Draft decision—STPIS reliability targets for Evoenergy for the 2019–24 regulatory period

	value
Urban	
SAIDI	33.140
SAIFI	0.618
Short rural	
SAIDI	31.811
SAIFI	0.603
Telephone answering	
Percentage of calls will be answered within 30 seconds	77.67%

Source: AER analysis.

10.2 Evoenergy proposal

Evoenergy's revenue proposal accepted our F&A position on how the STPIS will apply with the exception of the application of the revenue at risk. Evoenergy proposed to apply a revenue at risk within the range of ± 2.5 per cent instead of ± 5 per cent for the reasons outlined at section 10.3.

Evoenergy also applied to reclassify 44 urban feeders into short rural feeders because the maximum load of these urban feeders have changed. As such, these feeders no longer met the definition of "urban" feeders under the STPIS.[7]

We are required to make a decision on how the STPIS is to apply to Evoenergy.[8] When making a distribution determination, the STPIS requires us to determine all performance targets, incentive rates, revenue at risk and other parameters under the scheme.[9]

10.2.1 Interrelationships

In implementing the STPIS we must take into account any other incentives available to the distributor under the NER or relevant distribution determination.[10] One of the

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7 Evoenergy, Revenue Proposal Appendix 10.3: Explanatory note on feeder reclassification Regulatory proposal for the ACT electricity distribution network 2019-24, January 2018, p. 4.

8 NER, cl. 6.12.1(a).

9 AER, *STPIS*, November 2009, cl. 2.1(d).

10 NER, cl. 6.6.2(b)(3)(iv).

objectives of the STPIS is to ensure that the incentives are sufficient to offset any financial incentives the distributor may have to reduce costs at the expense of service levels. For the 2019–24 regulatory control period, the STPIS will interact with the Capital Expenditure Sharing Scheme (CESS) and the operating expenditure (opex) Efficiency Benefit Sharing Scheme (EBSS).

The reward and penalty mechanism, under the STPIS (the incentive rates) are determined based on the average customer value for the improvement, or otherwise, to supply reliability (the VCR). This is aimed at ensuring that the distributor's operational and investment strategies are consistent with customers' value for the services that are offered to them.

Our capital expenditure (capex) and opex allowances are set to reasonably reflect the expenditures required by a prudent and efficient business to achieve the capex and opex objectives. These include complying with all applicable regulatory obligations and requirements and, in the absence of such obligations, maintaining quality, reliability, and security outcomes.

The STPIS provides an incentive for distributors to invest in further reliability improvements (via additional STPIS rewards) where customers are willing to pay for it. Conversely, the STPIS penalises distributors where they let reliability deteriorate. Importantly, the distributor will only receive a financial reward after actual improvements are delivered to the customers.

In conjunction with CESS and EBSS, the STPIS will ensure that:

- any additional investments to improve reliability are based on prudent economic decisions
- reductions in capex and opex are achieved efficiently, rather than at the expense of service levels to customers.

10.3 Reasons for draft decision

We will apply the STPIS in accordance with our F&A paper to Evoenergy.[11] The following section sets out our detailed consideration on applying the STPIS to Evoenergy for the 2019–24 regulatory control period.

10.3.1 Revenue at risk

Evoenergy's revenue at risk for each regulatory year of the 2019–24 regulatory control period will be capped at ± 5.0 per cent as per the scheme standard.

Revenue at risk, caps the potential reward and penalty for Evoenergy under the STPIS. We consider an incentive of ± 5.0 per cent of the annual allowable revenue

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[11] AER, Framework and approach ActewAGL Regulatory control period commencing, 1 July 2019 to 30 June 2024, July 2017, pp. 51–52.

would result in the right balance with the operation of the EBSS and CESS to ensure that the incentives to reduce costs will not be delivered at the expense of service levels to customers—hence meeting the long term interest of consumers.

Evoenergy's revenue proposal submitted that its network is the second most reliable in the national electricity market. As such, it would be difficult to economically justify projects aimed at further improving underlying reliability performance.[12] It also stated that the revenue at risk is unlikely to constrain any rewards or penalties if it is set at 2.5 per cent or more.

The AER Consumer Challenge Panel (CCP10) submitted that it was leaning towards supporting a maintenance of the current revenue at risk at ± 2.5 per cent because it considered Evoenergy already has a strong focus on reliability, which could be over-emphasised with a ± 5 per cent approach.[13]

We consider that the revenue at risk be set at ± 5.0 per cent of annual allowable revenue to better meet the objectives of the STPIS because:

- The ± 2.5 per cent revenue at risk under our 2014-19 was a transitional arrangement for the first application of the national STPIS to Evoenergy. Our expenditure incentive schemes encourage a business to pursue efficiency improvements in opex and capex.[14] The STPIS incentivises a business to maintain or improve the quality of its services. These incentives are balanced so a business is not incentivised to make expenditure savings at the expense of service quality. A reduction on the revenue at risk will change the balance of the suite of incentive schemes.
- We recognise that Evoenergy's customers may not want to pay for improvements in reliability. However, this should not be interpreted as customers' willingness to receive a lower level of supply reliability. The ± 5.0 per cent revenue at risk level together with the EBSS and CESS should provide a good balance to ensure that supply reliability does not deteriorate when attempting to reduce costs.
- The risk of Evoenergy achieving a reward (or penalty) higher than 2.5 per cent is fully in Evoenergy’s own control. However, if Evoenergy’s actual performance during the 2019–24 regulatory period is much worse than the performance targets leading to the financial penalty under the STPIS exceeding 2.5 per cent, its customers will not receive the entire compensation for the decline in service level within this period. This means it will take another five years after 2024 before the customers will receive the compensation for a decline in service and this risk of mismanagement will be passed onto the customers.

[12] Evoenergy, Revenue Proposal Attachment 10: Incentive schemes Regulatory proposal for the ACT electricity distribution network 2019–24, January 2018, pp. 7–16.

[13] Consumer Challenge Panel, CCP10, Response to Evoenergy regulatory Proposal 2019-24 and AER Issues Paper, May 2017, p. 17.

[14] These are the capital expenditure sharing scheme (CESS) for capex, and the efficiency benefit sharing scheme (EBSS) for opex.

10.3.2 Reliability of supply component

Applicable components and parameters

We will apply unplanned SAIDI and unplanned SAIFI parameters under the reliability of supply component to Evoenergy's feeders for the 2019–24. Unplanned SAIDI measures the sum of the duration of each unplanned sustained customer interruption (in minutes) divided by the total number of distribution customers. Unplanned SAIFI measures the total number of unplanned sustained customer interruptions divided by the total number of distribution customers.

Exclusions

The STPIS allows certain events to be excluded from the calculation of the S-factor revenue adjustment. These exclusions include the events specified in the STPIS, such as the effects of transmission network outages and other upstream events. They also exclude the effects of extreme weather events that have the potential to significantly affect Evoenergy's underlying STPIS performance.

Evoenergy proposed to calculate the major event day (MED) threshold using the 2.5 beta method in accordance our F&A. Since we have not received any submissions that we should depart from our F&A, we accept Evoenergy's proposal.

Feeder reclassification

We accept Evoenergy's proposal to increase the number of short rural feeders from 19 to 63 based on the 0.3 MVA/km threshold level as defined in the STPIS.[15]

Performance targets

The STPIS specifies that the performance targets should be based on the average performance over the past five regulatory years. It also states that the performance targets must be modified for any reliability improvements completed or planned where the planned reliability improvements are included in the expenditure program proposed by the network service provider and expected to result in a material improvement in supply reliability.[16]

As our draft decision has not included capex for improving reliability, we made no adjustments to Evoenergy's reliability targets. Please refer to the capex attachment for further details.

We received no submissions from stakeholders regarding the application of Evoenergy's performance targets.

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15 AER, *STPIS*, November 2009, Appendix A.

16 AER, *STPIS*, November 2009, cl. 3.2.1.

Our calculated performance targets for Evoenergy for the 2019–24 regulatory control period are presented in the Table 10-2.

10.3.3 Customer service component

The STPIS customer service target applicable to Evoenergy is telephone response measured as the number of telephone calls answered within 30 seconds. This measure is referred to as the telephone Grade of Service (GOS).

We received no submissions from stakeholders regarding the application of Evoenergy's customer service performance target.

Our calculated performance targets for Evoenergy for the 2019–24 regulatory control period are presented in the Table 10-2.

10.3.4 Incentive rates

The incentive rates applicable to Evoenergy for the reliability of supply performance parameters of the STPIS have been calculated in accordance with clause 3.2.2 and using the formulae provided as appendix B of the National STPIS. Our draft decisions on Evoenergy's incentive rates are at Table 10-1. The incentive rate for the customer service component will be –0.040 per cent per unit of the telephone answering parameter.[17]

10.3.5 Value of customer reliability to calculate the incentive rates

Our F&A paper stated that we will apply a latest value for VCR through the distribution determination in calculating Evoenergy's incentive rates.[18] Evoenergy provided energy usage information based on AEMO's load classification of residential, commercial, industry and agriculture. Hence, for this draft decision, we have calculated Evoenergy's VCR for the incentive rates by deriving it from its consumption data and AEMO's published segment VCR.

The VCR for network segments is outlined in Table 10-3. We have applied this VCR to calculate Evoenergy's incentives rates for 2019–24.

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[17] AER, *STPIS*, November 2009, cl. 5.3.2(a).

[18] AER, *STPIS*, November 2009.

Table 10-3 Value of customer reliability ($/MWh)

	Urban	Short rural
VCR	38,350.00	38,350.00

Source: AER analysis, and AEMO, *Value of customer reliability review, final report*, September 2014, p. 30. VCR values have been escalated to the June 2018 quarter and will be updated for the final decision.