

# Determination June 2021 storms cost pass through

**AusNet Services**

March 2022

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## Overview

During the regulatory control period, AusNet Services (electricity distribution) (AusNet Services) can apply to pass through to its customers, in the form of higher or lower network charges, costs it incurs as a result of pre-defined exogenous events. These events are called cost pass through events.

On 22 November 2021, AusNet Services submitted a cost pass through application (AusNet Services' application) seeking to recover actual costs it experienced as a result of the storms that occurred on 9 and 10 June 2021 (June 2021 storms) in Victoria. AusNet Services stated that the June 2021 storms caused extensive damage to AusNet Services' electricity distribution network and interrupted supply to over 230,000 customers.<sup>1</sup>

AusNet Services is seeking to recover \$39.1 million (\$nominal, smoothed) in incremental revenue over the 2021–26 regulatory control period, of which approximately 61 per cent is related to Guaranteed Service Level (GSL) payments.<sup>2</sup> AusNet Services made GSL payments to its customers who were impacted by the June 2021 storms, under a Victorian Government Ministerial Order.<sup>3</sup>

AusNet Services proposed that the June 2021 storms be deemed a catastrophic event and therefore excluded from the calculation of the Major Event Day (MED) threshold value because it was a clear outlier. We consider that the effect of the June 2021 storms event has met the MED threshold, thus it has been excluded from the STPIS.

On 7 December 2021, we published AusNet Services' application on our website and invited stakeholder submissions. We received eight stakeholder submissions; six from individuals, one from a community group (The Kingston & District Power Alliance) and a combined submission from two energy retailers (Red Energy and Lumo Energy).<sup>4</sup> These submissions raised concerns around the vulnerabilities of the network to natural disaster events, the recovery of GSL payments, as well as AusNet Services' practices relating to asset maintenance and vegetation management prior to the June 2021 storms. We have had regard to these submissions in making this determination and address the issues raised in section 4.4.4 below.

<sup>1</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. p 11.

<sup>2</sup> This is equivalent to \$36.5 million (\$2021, smoothed) as reflected in AusNet Services' cost pass through application.

<sup>3</sup> The relevant order (**Ministerial Order**) was made on 18 November 2021 by the Hon Lily D'Ambrosio, Victorian Minister for Energy, Environment and Climate Change (**Minister**). See: <http://www.gazette.vic.gov.au/gazette/Gazettes2021/GG2021S636.pdf> (accessed 11 February 2022).

<sup>4</sup> Submissions were published on the AER website. See: <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/cost-pass-throughs/ausnet-services-%E2%80%93-cost-pass-through-2020-21-storms-natural-disaster/initiation>. There was one submission which was not published due to privacy and confidentiality concerns.

Under the National Electricity Rules (NER), AusNet Services is able seek the approval of the AER to pass through to network users a positive pass through amount in respect of certain events (referred to in the NER as positive change events).<sup>5</sup> A cost pass through application must address specified matters.<sup>6</sup>

If the AER determines that a positive change event has occurred in respect of a cost pass through application, the AER is required to determine (within a specified timeframe):

- the approved pass through amount, and
- how much of that amount should be passed through to Distribution Network Users in the regulatory year, and each regulatory year after that, in which the positive change event occurred,

taking into account the matters referred to in clause 6.6.1(j) of the NER.<sup>7</sup>

This determination sets out our assessment of AusNet Services' application and addresses those requirements, as set out in clause 6.6.1 of the NER.

We are satisfied that the June 2021 storms meet the definition of a natural disaster pass through event. We do not consider that the Ministerial Order about GSL payments, in itself, is a 'natural disaster' event. However, based on our consideration of the factors set out in clause 6.6.1(j) of the NER, as well as other matters relevant under the National Electricity Law, we determine to include the GSL-related costs as costs incurred due to the June 2021 storms natural disaster pass through event.

In considering the issues raised by stakeholders, we reviewed AusNet Services' asset maintenance and vegetation management policies, procedures and actions, prior to and during the storms. We did not find evidence of poor asset maintenance and vegetation management practices that contributed to the costs incurred as a result of the storm event.

We are satisfied that the materiality threshold to constitute a positive change event has been met. Our decision is discussed in greater detail in sections 4 and 5 of this report.

Our determination is to approve a positive pass through amount of \$39.1 million (\$nominal, smoothed) for the 2021–26 regulatory control period, consisting of following.<sup>8</sup>

- \$9.7 million to be recovered in 2022–23
- \$9.8 million to be recovered in 2023–24
- \$9.8 million to be recovered in 2024–25
- \$9.8 million to be recovered in 2025–26

<sup>5</sup> NER, cl. 6.6.1(a). A positive change event is: (a) a pass through event, other than a retailer insolvency event, which entails the Distribution Network Service Provider incurring materially higher costs in providing direct control services than it would have incurred but for that event, but does not include a contingent project or an associated trigger event; or (b) a retailer insolvency event. A pass through event is those events specified in clause 6.6.1(a1).

<sup>6</sup> NER, cl. 6.6.1(c).

<sup>7</sup> NER, cl. 6.6.1(d).

<sup>8</sup> This is equivalent to \$36.5 million (\$2021, smoothed) as reflected in AusNet Services' application.

We estimate that the approved cost pass through amount will add approximately \$7 (\$nominal) per year to residential consumer bills, and \$29 (\$nominal) per year to small business consumer bills, over the remaining four years of AusNet Services' 2021–26 regulatory control period.

# 1 Introduction

We received a cost pass through application from AusNet Services for additional expenditure related to restoring electricity supply and repairing damage to its network caused by the June 2021 storms in Victoria.

AusNet Services' application proposed to recover \$39.1 million (\$nominal) from electricity users through an increase in distribution prices in each of the remaining four years of the current regulatory control period,<sup>9</sup> that is, from 1 July 2022 to 30 June 2026.<sup>10</sup>

This section sets out the AER's role in assessing cost pass through applications from electricity distribution network service providers (DNSP), as well as information on AusNet Services' application.

## 1.1 Who we are and our role in this process

We, the Australian Energy Regulator (AER), exist to ensure all Australian energy consumers are better off, now and in the future. Consumers are at the heart of our work, and we focus on ensuring a secure, reliable and affordable energy future for Australia. We are the economic regulator for electricity distribution and transmission services in the National Electricity Market (NEM). Our electricity-related powers and functions are set out in the National Electricity Law (NEL) and NER.<sup>11</sup>

The AER regulates AusNet Services' revenues through five-year distribution revenue determinations. AusNet Services' current revenue determination for the 2021–26 regulatory control period runs from 1 July 2021 to 30 June 2026. However, the pass through application relates to an event that took place in a six-month extension of AusNet Services' revenue determination for the 2016–20 regulatory control period.<sup>12</sup>

<sup>9</sup> This is equivalent to \$36.5 million (\$2021, smoothed) as reflected in AusNet Services' cost pass through application.

<sup>10</sup> AusNet Services' initial application sought to pass through \$36.2 million (\$2021, smoothed) but it subsequently revised the proposed pass through amount to \$36.5 million (\$2021) to reflect additional GSL payments. See: [AusNet Services, AST AER Letter GSL variation, 14 January 2022](#).

<sup>11</sup> In addition to regulating transmission and distribution in the NEM and the Northern Territory, we also monitor the wholesale electricity market to ensure suppliers comply with the legislation and rules, taking enforcement action where necessary, and regulate retail energy markets in Queensland, New South Wales, South Australia, Tasmania (electricity only) and the ACT.

<sup>12</sup> AusNet Services' 2016–20 regulatory control period was extended by six months to align with a financial year basis. This extension was reflected in an Order in Council published by the Victorian Government on 27 October 2020 under section 16VE of the amended NEVA. On 28 October 2020, we released our final decision on AusNet Services' electricity distribution determination for the six-month extension variation decision for the 2016–20 regulatory control period (see <https://www.aer.gov.au/node/72919>).

We are responsible for assessing cost pass through applications.<sup>13</sup> Under the NER, a distribution business may apply to us seeking the recovery of additional costs incurred during a regulatory control period, if predefined events occur as specified in either the NER or in its respective revenue determination.<sup>14</sup>

## 1.2 AusNet Services' application

On 22 November 2021, AusNet Services submitted a cost pass through application seeking to recover the costs it has incurred, and is forecast to incur, as a result of the June 2021 storms in Victoria.<sup>15</sup>

AusNet Services submitted that the June 2021 storms caused extensive damage to its network. The extreme weather, including gusts of wind exceeding 100km/h, resulted in flooding, fallen trees and poles, and significant damage to overhead power lines. In total, fourteen 66kV feeders (power lines) were taken out of service, fifty-eight 22kV feeders reported faults and ten zone substations went black. At its peak, this resulted in 230,000 customers (approximately 30 per cent of AusNet Services' customer base) without power.<sup>16</sup>

AusNet Services applied to the Essential Services Commission (ESC) to be excused from making GSL payments in relation to the June 2021 storms. It stated that the June 2021 storms caused the largest measured interruption to its distribution network since 1995.<sup>17</sup> The Electricity Distribution Code (EDC)<sup>18</sup> requires the ESC to excuse a DNSP from making a supply restoration payment or a low reliability payment (both types of GSL payments) under certain conditions.<sup>19</sup>

AusNet Services submitted that it withdrew its application to the ESC following the Ministerial Order about GSL payments. On 18 November 2021, the Victorian Government made a Ministerial Order to amend AusNet Services' electricity distribution licence with the effect of requiring AusNet Services to make GSL payments for outages resulting from the June 2021 storms.<sup>20</sup>

<sup>13</sup> NER, cl. 6.6.1.

<sup>14</sup> NER, cl. 6.6.1(a).

<sup>15</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021.

<sup>16</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. pp 10-11.

<sup>17</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. p 25.

<sup>18</sup> Version 12 of the EDC was the version that applied at the time of the June Storms. Version 13 commenced on 1 July 2021.

<sup>19</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. pp 25-26

<sup>20</sup> See: <http://www.gazette.vic.gov.au/gazette/Gazettes2021/GG2021S636.pdf> (accessed 11 February 2022).



AusNet Services stated that it has incurred \$51.6 million (\$2021) in costs as a result of the June 2021 storms, apportioned as follows: <sup>21</sup>

- \$21.8 million in capital expenditure (capex) covering emergency (replacement) capital works
- \$29.8 million in operating expenditure (opex), the bulk of which covers GSL payments made to customers for supply interruptions experienced by AusNet Services customers as a result of the June 2021 storms (\$22.5 million) and the remainder, emergency corrective works and vegetation management.

Table 1 shows the additional costs that AusNet Services has incurred as a result of the June 2021 storms.

**Table 1 AusNet Services – costs related to the June 2021 storms (\$million, \$2021)**

	Jan-Jun 2021	2021-22	2022-23	2023-24	2024-25	2025-26	Total
Capex	21.58	0.19	-	-	-	-	21.77
Opex (excluding GSL)	7.18	0.13	-	-	-	-	7.31
GSL payment (opex)	22.54	-	-	-	-	-	22.54
Total	51.30	0.32	-	-	-	-	51.62

Source: AusNet Services' June 2021 storms cost pass through application – build up of costs

Note: '0.0' and '-0.0' represent small nonzero number and '-' represents zero.

The revenue impact of the proposed pass through amount is \$39.1 million (\$nominal, smoothed),<sup>22</sup> over the four-year period from 1 July 2022 to 30 June 2026.<sup>23</sup>

### 1.3 Structure of determination

This document sets out our assessment and determination, amongst other things, on whether a cost pass through event has occurred, the pass through amount, the time period for the recovery of the pass through amount, and our reasons for the determination.

The decision is structured as follows.

- Section 2 sets out our determination on AusNet Services' cost pass through application.
- Section 3 outlines relevant regulatory requirements and our assessment approach.

<sup>21</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application - November 2021*, p 19. This amount includes the additional GSL payments of \$311,160 (\$2021) made by AusNet Services. See: [AusNet Services, AST AER Letter GSL variation](#), 14 January 2022.

<sup>22</sup> This is equivalent to \$36.5 million (\$2021, smoothed) as reflected in AusNet Services' cost pass through application.

<sup>23</sup> AusNet Services' initial application sought to pass through \$36.2 million (\$2021, smoothed) but it subsequently revised the proposed pass-through amount to \$36.5 million to reflect additional GSL payments. See: [AusNet Services, AST AER Letter GSL variation](#), 14 January 2022.

- Section 4 sets out our reasons for the determination, including our assessment of the proposed positive pass through amount.
- Section 5 sets out our assessment of AusNet Services' cost pass through application against the NER requirements, including whether the materiality threshold is met, and consideration of stakeholder submissions.

## 2 Determination

Based on our consideration of all the matters set out in this decision, we consider that AusNet Services' application, as submitted on 22 November 2021, establishes that a pass through event has occurred in respect of the June 2021 storms, being a natural disaster pass through event as specified in AusNet Services' 2016–20 revenue determination. Our assessment against the requirements of a positive change event is summarised in section 5 (Table 4).

We are satisfied that the June 2021 storms constitutes a positive change event as defined under the NER. In particular, we are satisfied that AusNet Services incurred a material increase in the costs of providing direct control services in the 2020–21 regulatory year as a result of this pass through event.<sup>24</sup>

Our determination is to approve a positive pass through amount of \$39,098,155 (\$nominal, smoothed), which is to be recovered as follows.

- \$9,739,601 to be recovered in 2022–23.
- \$9,762,856 to be recovered in 2023–24.
- \$9,786,166 to be recovered in 2024–25.
- \$9,809,532 to be recovered in 2025–26.

Sections 4 and 5 set out our assessment of AusNet Services' cost pass through application and the positive pass through amount.

<sup>24</sup> This relates to the six-month extension of the 2016–20 regulatory control period.

### 3 Relevant regulatory requirements and assessment approach

The pass through mechanism recognises that an efficient revenue allowance cannot account for certain types of matters that are uncertain and outside the control of the business and which cannot be prevented or mitigated by prudent operational risk management. A cost pass through enables a network service provider to recover (or pass through) the costs of defined unpredictable, high-cost events that are not factored into our five-year revenue determination for the business.

Clause 6.6.1(a1) of the NER defines a pass through event as one of the following prescribed pass through events for all Distribution Network Service Providers (DNSPs):

- 1) a regulatory change event
- 2) a service standard event
- 3) a tax change event
- 4) a retailer insolvency event, and
- 5) any other event specified in a distribution determination as a pass through event for the determination (nominated pass through event).

The first step in our assessment is to determine whether a pass through event has occurred and examine timing matters, e.g. whether an application is submitted within the timeframe set out in the NER. Once we have determined that a pass through event has occurred, we are to determine whether it is a positive (or negative) change event.

The NER defines a positive change event for a DNSP as:

“a pass through event...which entails the DNSP incurring materially higher costs in providing direct control services than it would have incurred but for that event...”<sup>25</sup>

We undertake this assessment with reference to the NER and the revenue determination applicable to AusNet Services during the time period in which the June 2021 storms occurred, which is the six-month extension we approved to AusNet Services’ distribution determination for the 2016–20 regulatory control period.<sup>26</sup>

As part of this process, we examine whether AusNet Services’ application has addressed matters specified in clause 6.6.1(c) of the NER (see section 5 below (Table 3 and Table 4)). We also determine the materiality of the proposed pass through amount.

Clause 6.6.1(d) of the NER provides that if the AER determines that a positive change event has occurred, the AER must determine:

- the approved pass through amount, and
- the amount that should be passed through to distribution network users in the regulatory year, and each regulatory year after that, in which the positive change event occurred,

<sup>25</sup> NER, chapter 10.

<sup>26</sup> See: <https://www.aer.gov.au/node/72919>

taking into account the factors referred to in clause 6.6.1(j) of the NER.

### **3.1 Timing matters**

To seek the approval of the AER to pass through a positive pass through amount, clause 6.6.1(c) of the NER requires a DNSP to submit to the AER a written statement specifying a range of details relating to the event within 90 business days of the relevant positive change event occurring.

The NER requires us to make a determination within the timeframe specified in clause 6.6.1(e). That is, within 40 business days from the later of the date the AER received AusNet Services' cost pass through application and the date it received any additional information required by it through a notice issued under clause 6.6.1(e1) of the NER.

## 4 Reasons for determination

The sections below set out the reasons for our determination.

### 4.1 Occurrence of a natural disaster

This determination relates to a nominated pass through event, being a natural disaster event as specified in AusNet Services' 2016–20 revenue determination (thus applying to the six-month extension of this determination).

A natural disaster event is defined in AusNet Services' 2016–20 revenue determination (which also applies to the six month extension).

*“Natural disaster event means any natural disaster including but not limited to fire, flood or earthquake that occurs during the 2016–20 regulatory control period that increases the costs to AusNet Services in providing direct control services, provided the fire, flood or other event was not a consequence of the acts or omissions of the service provider.*

*Note: In assessing a natural disaster event pass through application, the AER will have regard to, amongst other things:*

- *whether AusNet Services has insurance against the event,*
- *the level of insurance that an efficient and prudent NSP would obtain in respect of the event.”<sup>27</sup>*

#### 4.1.1 Natural disaster event

We consider the June 2021 storms satisfy the definition of a natural disaster pass through event as specified in AusNet Services' determination. In particular, the June 2021 storms were:

- responded to by State and Federal Governments as a natural disaster;
- unexpected; and
- caused severe damage to property.

For example, the Victorian Government made a state of emergency declaration with respect to the impacts of flooding in Gippsland on the Yallorn power station and that the flooding was caused by the storms on the 9 and 10 June (the subject of AusNet Services' application). The Victoria State Emergency Services (VICSES) confirmed the severity of the impact the severe weather had on the region containing AusNet Services' network.<sup>28</sup>

<sup>27</sup> AER, Final decision AusNet distribution determination - Attachment 15 - Pass through events - May 2016, p. 7

<sup>28</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021, p 9, 11. This was also reported on by Emergency Management Victoria, (see: <https://www.emv.vic.gov.au/news/assessing-the-damage-to-homes-in-victoria>)

Further, the Federal Government provided disaster assistance with respect to the storms that are the subject of AusNet Services' application.<sup>29</sup>

The June 2021 storms increased the costs to AusNet Services in providing direct control services and the event was not a consequence of an act or omission of AusNet Services – it was outside of AusNet Services' control, and it was unforeseeable.

#### **4.1.1.1 Treatment of the Ministerial Order about the GSL payments as a natural disaster event**

AusNet Services treated the Ministerial Order as part of the natural disaster event, stating that its impetus was the consequence of the application of the regulatory framework in direct response to the June 2021 storms.<sup>30</sup> AusNet Services considered that this approach better aligns with the purpose and requirements of the cost pass through framework.<sup>31</sup>

While we consider that the June 2021 storms satisfies the definition of a natural disaster pass through event, we do not consider the Ministerial Order about GSL payments, in itself, is a 'natural disaster'. However, we have considered the treatment of GSL associated costs incurred by AusNet Services (i.e. whether to include them or not) as a separate matter based on the factors we are required to take into account as set out in clause 6.6.1(j) of the NER. Our consideration is set out in section 5, Table 4.

#### **4.1.1.2 Effect of the event could not be prevented or mitigated**

We consider the decisions and actions of AusNet Services in response to the event were efficient and that the June 2021 storms event could not have been prevented or mitigated through prudent operational risk management.

AusNet Services submitted that it has governance procedures and practices to efficiently manage its exposure to risks it faces as an owner and operator of a distribution network, as well as its approach to storms. In particular, AusNet Services submitted its current emergency response protocol, Strategic Plan for Intergrated Response and Contingency System (SPIRACS). SPIRACS outlines criteria for assessing the severity of an event and offers advice on preventative and mitigation controls aimed at reducing the consequences of crisis events. This emergency response protocol formed the response framework by which

<sup>29</sup> Disaster Assist 2021, Australian Government: Department of Home Affairs, <https://www.disasterassist.gov.au/Pages/disasters/current-disasters/Victoria/vic-floods-storms-09-06-2021.aspx>, viewed 15 December 2021.

<sup>30</sup> AusNet Services, AusNet Services - 2020-21 Storms disaster event cost pass through - Application - November 2021, p 26.

<sup>31</sup> AusNet Services, AusNet Services - 2020-21 Storms disaster event cost pass through - Application - November 2021, p 26.

AusNet Services coordinated and prioritised activities across its network to restore customer supply in response to the June 2021 storms.<sup>32</sup>

In response to our request for additional information AusNet Services also submitted:<sup>33</sup>

- its asset management plan relating to poles, pole top structures and overhead lines that was effective at the time of the storms as well as any previous versions covering the five years prior to the storms;
- details of the most recent inspections prior to the storms of all poles and lines in the area affected by the storms;
- details of any defects that were known prior to the storms within the affected areas and the plan to address the defect;
- its Vegetation Management Plan that was effective at the time of the storms as well as any previous versions covering the five years prior to the storms;
- details of the most recent vegetation clearing carried out prior to the storms, including the cost, sections of the network cleared (e.g., name of region/suburb and postcode); and
- details of the vegetation management program as well as any bushfire management programs applicable to the area impacted by the storms.

Although AusNet Services has measures in place to deal with inclement weather more generally, severe storms can and do have impacts on the network that cannot readily be mitigated beforehand.

We have reviewed this material and we accept that AusNet Services' asset management and vegetation management plans were appropriate and that AusNet Services did not reasonably do anything or omit to do anything that had the potential to increase the pass through amount.

## 4.2 Positive change event

If we are satisfied that a pass through event has occurred, we must determine whether the pass through event qualifies as a “positive change event”. That is, whether AusNet Services incurred materially higher costs in providing direct control services than it would have incurred but for the pass through event.

The NER defines “materially” as:

“For the purposes of the application of clause 6.6.1, an event results in a DNSP incurring materially higher or materially lower costs if the change in costs (as opposed to the revenue impact) that the DNSP has incurred and is likely to incur in

<sup>32</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application - November 2021*, p 13.

<sup>33</sup> AusNet Services, *Response to AER Follow up Questions - assets maintenance and vegetation management - AER information request IR01 to AusNet Services - June 2021 storms cost pass through application*, 14 January 2022 (including 14 attachments).



any regulatory year of a regulatory control period, as a result of that event, exceeds 1% of the annual revenue requirement for the DNSP for that regulatory year.”

The treatment of the GSL costs needed to be considered prior to determining whether the June 2021 storms ‘natural disaster’ pass through event had met the definition of ‘materially’. For the reasons stated in section 5 (Table 4), we have determined to include GSL payments as part of the pass through amount to be recovered under the June 2021 storms natural disaster.

We have allowed the recovery of costs associated with GSL payments under the natural disaster event, based on our consideration of all relevant factors. The GSL-related costs represent a material regulatory cost incurred by AusNet Services, which is largely outside its control.<sup>34</sup> Under the revenue and pricing principles, AusNet Services is to be provided with a reasonable opportunity to recover efficient costs. Further, while we included forecast GSL expenditure in the total opex allowance as part of the revenue determination, GSL payments for events similar to the June 2021 storms were not included in AusNet Services’ opex allowance for the 2016–20 regulatory period (including the 6-month extension). This is because under the GSL scheme applicable at the time, AusNet Services could apply to the Essential Services Commission (ESC) for an exemption to make GSL payments for supply interruptions exceeding a mandated threshold; which the June 2021 storms did.

We consider the additional costs incurred by AusNet Services in providing direct control services as a result of the June 2021 storms meets the materiality threshold.

### **4.3 Timing of AusNet Services’ application**

Clause 6.6.1(c) of the NER requires a DNSP to submit a pass through application to us within 90 business days of the positive change event occurring.

On 10 September 2021, AusNet Services requested an extension to submit an application for the pass through to allow time for the Victorian Government to finalise a Ministerial Order which impacted the GSL payments AusNet Services was required to make in relation to the June 2021 storms.<sup>35</sup>

On 1 October 2021, under clause 6.6.1(k) of the NER, we extended the timeframe for AusNet Services to submit its cost pass through application to 15 December 2021. We were satisfied that the difficulty of assessing or quantifying the effect of the various components relevant to the pass through event (in this case, the GSL payments) justified the extension of the usual 90 business day period.

We received AusNet Services’ pass through application on 22 November 2021.

Following our initial assessment of AusNet Services’ application, we issued an information notice to AusNet Services (on 17 December 2021) under clause 6.6.1(e1) of the NER, requesting further information on the scope of works and associated costs.

<sup>34</sup> The GSL payments represent approximately 7.6% of AusNet Services’ allowed annual revenue (based on half-year 2021 revenue applying to the six-month extension of the 2016–20 regulatory control period).

<sup>35</sup> NER, cl. 6.6.1(k).

We received AusNet Services' response to our information notice on 24 January 2022. Accordingly, we are required to make this determination by 22 March 2022.

## 4.4 Assessment of the pass through amount

In assessing a pass through application, the NER requires us to take into account a range of relevant factors,<sup>36</sup> including the need to ensure that AusNet Services only recovers any actual or likely increment in costs, to the extent that such an increment is solely as a consequence of the pass through event,<sup>37</sup> and that AusNet Services does not recover costs that have or will be factored into AusNet Services' annual revenue requirement.<sup>38</sup>

We approach this assessment by ensuring, amongst other factors, that:

- the pass through amount reflects only those costs incurred as a result of the June 2021 storms natural disaster event,<sup>39</sup> and not business-as-usual costs, or costs of increasing the scope of network services provided by AusNet Services
- the costs incurred are prudent and efficient costs required to rectify the damage caused by the storms;
- the pass through amount reflects only the incremental cost of the June 2021 storms, taking into account deductions for actual and expected cost savings that will occur as a result of works undertaken to address the storms. For example, the replacement of older assets damaged by the storms with new assets may result in lower future inspection and maintenance costs, which should be deducted from the costs to be passed through; and
- the concerns raised by stakeholders in the submissions we received as part of our community consultation process are examined and addressed.

We are satisfied that AusNet Services' estimates of the increase in capex and opex costs due to the June 2021 storms, accounting for the identified avoided costs, including in both its initial proposal and those subsequently in our information notice, are prudent and efficient.

Our determination on the approved incremental capex and opex costs for the June 2021 storms is set out in Table 1 earlier in this Determination, as we have not applied any adjustment to the the numbers proposed by AusNet Services.

Table 2 details our determination on incremental revenue.

<sup>36</sup> NER, cl. 6.6.1(j).

<sup>37</sup> NER, cl. 6.6.1(j)(5).

<sup>38</sup> NER, cl. 6.6.1(j)(7).

<sup>39</sup> For the purpose of this determination, 'costs incurred as a result of the June 2021 storms natural disaster event' include costs related to the GSL payments that AusNet Services incurred following the Ministerial Order.

**Table 2 AER – approved incremental revenue for the June 2021 storms (\$million, nominal)**

	2021-22	2022-23	2023-24	2024-25	2025-26	Total
Return on capital	1.0	1.0	1.0	0.9	0.9	4.9
Return of capital (regulatory depreciation)	0.0	0.0	0.0	0.0	0.0	0.2
Operating expenditure	30.4	-	-	-	-	30.4
Net tax allowance	-	-	-	-	-	-
Incremental annual revenue requirement (unsmoothed)	31.5	1.0	1.0	1.0	1.0	35.5
Incremental annual expected revenue (smoothed)	-	9.7	9.8	9.8	9.8	39.1

Source: AER's analysis

Note: '0.0' and '-0.0' represent small nonzero number and '-' represents zero.

#### **4.4.1 Costs reflect only June 2021 storms-related costs and not business-as-usual costs**

We are satisfied that the costs AusNet Services has incurred are costs incurred as a consequence of the June 2021 storms and do not include business-as-usual costs. This takes into account all the expected savings, in the 2021–26 regulatory period, from works that would have been required in future years and is part of the on-going cost of maintaining the network, but that was brought forward and carried out as a necessary part of the storms restoration activities. These costs have been demonstrated to be incremental costs and separate to the business-as-usual costs of operating the distribution network.

AusNet Services described the process it used for isolating the June 2021 storms-related costs it incurred from its business-as-usual costs as follows:

In calculating the eligible pass through amount, we included only the incremental costs for those activities that were incurred solely as a result of the positive change event. To be clear, we excluded the following costs from our claim:

- Fixed fees paid to our contractors that we would have paid if the June 2021 storms did not occur.
- Office-based staff time, as these costs would have been incurred by the business in any event.

We captured expenditures that were in response to the June 2021 storms in a manner consistent with our accounting framework, creating a specific project code in SAP to clearly record and track the costs incurred due to the storms. To ensure confidence in the accuracy of the transactions recorded in our financial

system [...] KMPG has reviewed our financial records based on agreed upon procedures.<sup>40</sup>

We requested and obtained AusNet Services' detailed costs build up, including the underlying assumptions and associated supporting evidence (e.g., invoices and receipts). We reviewed this information, including the calculation of GSL payments. We are satisfied that the capex and opex costs AusNet Services included in its cost pass through application are incremental and efficient. We are also satisfied that AusNet Services calculated the GSL payments to reflect only outages caused by the June 2021 storms, and excluded the contribution of the Victorian Government.<sup>41</sup>

#### **4.4.2 The level of June 2021 storms-related costs is the prudent and efficient costs to maintain service levels**

We are satisfied that the level of costs AusNet Services has incurred as a result of the June 2021 storms reflect efficient costs. We have examined the scope of actions and works AusNet Services undertook in response to the June 2021 storms event.

As stated section 4.4.1, we reviewed AusNet Services' costs build up relating to its cost pass through application. We note that the unit costs relating to the capex component of the pass through are materially higher than AusNet Services' typical business-as-usual unit costs. However, AusNet Services has sufficiently justified the higher unit cost due to the necessity of the emergency response actions and works and their cost.

#### **4.4.3 Cost reflects adjustments for savings to business-as-usual costs resulting from the June 2021 storms expenditure**

We are satisfied that AusNet Services' pass through amount reflects deductions for savings to business-as-usual costs resulting from its storms expenditure. AusNet Services proposed an expenditure decrement of \$0.17 million (\$2021) in future years to account for future work that was brought forward to the storms recovery period, and which no longer requires the funding approved in our 2021–2026 distribution determination.<sup>42</sup>

#### **4.4.4 Submissions from stakeholders**

We received eight submissions from stakeholders; six were made by individuals; one from a community group (Kingston & District Power Alliance); and a combined submission was received from two energy retailers (Red Energy and Lumo Energy).<sup>43</sup> In general, the

<sup>40</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. p 22.

<sup>41</sup> The Victorian Government reimbursed \$3.1 million of the GSL payments made by AusNet.

<sup>42</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. p 5.

<sup>43</sup> Submissions were published on the AER website. See: <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/cost-pass-throughs/ausnet-services-%E2%80%93-cost-pass-through-2020-21-storms-natural-disaster/initiation>. There was one submission which was not published due to privacy and confidentiality concerns.

submissions from individual customers and the Kingston & District Power Alliance were opposed to AusNet Services' application.

The main reasons behind this view were:

- Poor asset maintenance and vegetation management – some submissions stated that AusNet Services had not maintained the land surrounding the power lines prior to the storms and trees have been allowed to grow substantially large. If such maintenance had been performed prior to the storms the damage would not have been so extensive.
- Charging customers for compensation – stakeholders were concerned that by seeking to recover GSL payments, AusNet Services would be allowed to charge consumers for compensation paid as a result of AusNet Services' lack of service.
- Disincentive to innovate – the submissions stated that if we approve the proposed amounts, we would be disincentivising AusNet Services to innovate or implement long term solutions (e.g., undergrounding) to overcome current vulnerabilities in its networks to these types of events.

As stated in section 4.1.1.2, we have reviewed the information AusNet Services provided about its governance procedures and practices to efficiently manage its exposure to risks it faces as an owner and operator of a distribution network, as well as its approach to storms. In particular, we reviewed its asset maintenance and vegetation management policies and procedure, prior to and during the storms. We did not find evidence of poor asset maintenance and vegetation management practices. As such, we are satisfied that AusNet Services' actions, decisions and measures were efficient to mitigate the cost impact from the June 2021 storms.

As stated in sections 4.1.1.1, 4.4.1 and Table 4 of section 5, we are satisfied that the GSL-related costs AusNet Services incurred as a result of the June 2021 storms and the Ministerial Order represent a significant regulatory cost. GSL schemes operate on the assumption that there will always be a small number of customers who will receive payments because they live in weak parts of the grid where outages are frequent despite the best efforts of the distributor to meet the relevant service standards threshold. We consider GSL payments to be an efficient cost for a prudent operator. For this reason, we provide an allowance in forecast opex for GSL payments during our revenue determinations.

We acknowledge stakeholder concerns around the current vulnerabilities of electricity networks to natural disaster events such as the June 2021 storms. We note that undergrounding elements of a network would require significant capital investment. We recognise that policy and rule makers, and other stakeholders, continue to discuss the resilience of electricity networks, including long term effects of changing weather patterns on the operation of (and investments in) electricity networks. These wider issues are beyond the scope of our consideration of the June 2021 storms cost pass through application.

## 4.5 Timing of cost pass through recovery

AusNet Services has proposed to recover the incremental revenue arising from its cost pass through application over the remaining four years of its 2021–26 regulatory control period.

We are satisfied that this approach will minimise volatility in AusNet Services' revenue requirements while still allowing it to recover its efficient costs in a timely manner.

## 5 NER requirements and stakeholder submissions

For a cost pass through to be determined, there must be a positive change event that results in an eligible pass through amount. AusNet Services can then submit a pass through application, that must address certain matters specified in the NER.<sup>44</sup> We make a determination on AusNet Services’ cost pass through application, and determine the approved pass through amount and the regulatory years in which that pass through amount is to be recovered.<sup>45</sup> For the reasons set out in Table 3 below, we are satisfied that a positive change event has occurred, and that AusNet Services’ application relating to the June 2021 storms specifies the necessary matters required by the NER.

In making our determination on AusNet Services’ proposed pass through amount, we must take into account certain matters specified in the NER (see Table 4). Additionally, we have taken into account the eight stakeholder submissions received on AusNet Services’ application. Our consideration of these matters is set out in Table 3 below. After having regard to all of the matters in Table 3 below and throughout this decision, we make the determination set out in section 2 above.

**Table 3: Requirements for determining a positive change event has occurred**

Requirement of the NER	Our consideration
Is the pass through event a regulatory change event, service standard event, tax change event, or retailer insolvency event? <sup>46</sup>	No.
Is the pass through event a contingent project or a trigger event associated with a contingent project? <sup>47</sup>	No.
Does the pass through relate to any other event specified in AusNet Services’ 2016–20 distribution determination as a pass through event for that determination? <sup>48</sup>	Yes. We consider that the June 2021 storms satisfy the natural disaster pass through event specified in AusNet Services’ determination, which is defined as including fire, flood, or other event, provided the event was not a consequence of the acts or omissions of the service provider. <sup>49</sup>

<sup>44</sup> NER, cl. 6.6.1(c).

<sup>45</sup> NER, cl. 6.6.1 (d).

<sup>46</sup> NER, cll. 6.6.1(a1)(1) through 6.6.1(a1)(4); and chapter 10.

<sup>47</sup> See the definition of “positive change event” in chapter 10 of the NER.

<sup>48</sup> NER,cl. 6.6.1(a1)(5)

<sup>49</sup> AER, *Final decision AusNet distribution determination - Attachment 15 - Pass through events - May 2016*, p. 7. This determination was in place in June 2021 as the AER determined to extend the 2016-2020 control period by six months to commence a new regulatory period on 1 July 2021: AER, *Final Decision: AusNet Services – Six-month extension – Variation decision*, October 2020.

Requirement of the NER	Our consideration
Was the pass through event a consequence of acts or omissions of AusNet Services? <sup>50</sup>	No, there is no evidence that AusNet Services' acts or omissions caused the June 2021 storms. <sup>51</sup>
Did the June 2021 storms pass through event entail AusNet Services incurring materially higher costs in providing direct control services than it would have incurred but for the event? <sup>52</sup>	Yes. As discussed in section 4.2, we consider the additional costs incurred by AusNet Services in providing prescribed distribution services as a result of the June 2021 storms meets the materiality threshold. AusNet Services' annual revenue requirement (unsmoothed) for the six-month extension of the 2016–20 regulatory period during which the storms occurred was \$296.1 million (\$nominal), 1% of which is \$2.96 million. We consider that an efficient amount of opex and capex incurred as a result of the June 2021 storms exceeds this amount, and therefore the increase in costs incurred in providing direct control services as a result of the event exceed the materiality threshold.
What is the date on which the positive change event occurred?	For the purpose of complying with 6.6.1(c), AusNet Services indicated that the storms occurred on 9 and 10 June 2021. We agree with AusNet Services as the Victorian and Federal Governments recognises these dates in providing assistance packages to affected individuals and communities. <sup>53</sup>
Did AusNet Services submit a written statement of its pass through application within 90 business days of the positive change event occurring? <sup>54</sup>	Yes. As discussed in section 4.3, AusNet Services submitted its written statement on 22 November 2021, following an extension of time by the AER under clause 6.6.1(k) of the NER. We consider that AusNet Services has submitted its written statement within the allowed timeframe.
Did AusNet Services specify details of the positive change event, including the date on which the event occurred, in its written statement? <sup>55</sup>	Yes. AusNet Services' written statement is available on our website. <sup>56</sup>
Did AusNet Services specify in its written statement the eligible pass through amount, the proposed positive pass through amount, and the amounts proposed to be recovered from customers in each regulatory year? <sup>57</sup>	Yes. AusNet Services proposed an eligible, positive pass through amount of \$36.5 million (\$2021) to be recovered from consumers in the last four years of the current regulatory control period: 2022–23 to 2025–26.
Did AusNet Services specify in its written statement evidence of the actual and likely	Yes. AusNet Services' pass through application (that is, its written statement) set out the costs it incurred as a result of

<sup>50</sup> AER, *Final decision AusNet distribution determination - Attachment 15 - Pass through events* - May 2016, p. 7.

<sup>51</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021. p 10-16.

<sup>52</sup> That is, does it meet the definition of a “positive change event” as defined in chapter 10 of the Rules.

<sup>53</sup> Disaster Assist 2021, Australian Government: Department of Home Affairs, <https://www.disasterassist.gov.au/Pages/disasters/current-disasters/Victoria/vic-floods-storms-09-06-2021.aspx>, viewed 16 January 2022.

<sup>54</sup> NER, cl. 6.6.1(c).

<sup>55</sup> NER, cll. 6.6.1(c)(1) and 6.6.1(c)(2).

<sup>56</sup> <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/cost-pass-throughs/ausnet-services-%E2%80%93-cost-pass-through-2020-21-storms-natural-disaster/initiation>

<sup>57</sup> NER, cll. 6.6.1(c)(3), 6.6.1(c)(4), and 6.6.1(c)(5).



Requirement of the NER	Our consideration
increase in costs that occurred solely as a consequence of the positive change event? <sup>58</sup>	the June 2021 storms, as well as how it calculated its proposed pass through amount. <sup>59</sup>
Was there a regulatory information instrument applicable to the pass through application? <sup>60</sup>	No.
Is the pass through amount, in whole or in part, in respect of expenditure for a restricted asset? <sup>61</sup>	No.

Source: AER's analysis

**Table 4 Factors that the AER is to consider under the NER when determining a positive pass through amount**

Relevant factors under cl. 6.6.1(j)	AER consideration
In making the pass through determination we must take into account the matters and proposals set out in AusNet Services' written statement. <sup>62</sup>	This decision sets out how we have taken into account the matters and proposals set out in AusNet Services' pass through application (written statement).
We must take into account the incremental increase in costs in providing direct control services resulting from the pass through event. <sup>63</sup>	In section 4.4 above we set out our assessment of the costs incurred by AusNet Services as a consequence of the June 2021 storms. We have considered the costs that AusNet Services has incurred and is likely to incur as a result of the June 2021 storms as well as the likely cost savings to AusNet Services' business-as-usual activities as a result of its expenditure related to the June 2021 storms.
We must take into account the efficiency of AusNet Services' decisions and actions in relation to the risk of the event. <sup>64</sup>	<p>In making this determination, we must take into account the efficiency of AusNet Services' decisions and actions in relation to the risk of the positive change event, including whether AusNet Services has failed to take any action that could reasonably be taken to reduce the magnitude of the eligible pass through amount, or omitted to take any action where such action has increased the magnitude of the amount.</p> <p>We do not have evidence to consider that AusNet Services' decisions and actions in relation to the risk of the positive change events were inefficient. We believe AusNet Services has taken positive actions during the positive change event, including working collaboratively and assisting with authorities where necessary.</p> <p>There does not appear to be any action that AusNet Services has failed to take, that it could reasonably have taken, to</p>

<sup>58</sup> NER, cl. 6.6.1(c)(6).

<sup>59</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application* - November 2021, section 6, pp. 20–25; ASD - Attachment 1 - Build up of costs - Public\_Amended (01.12.21).

<sup>60</sup> 6.6.1(c)(7).

<sup>61</sup> NER, cl. 6.6.1(c1) and (d2).

<sup>62</sup> NER, cl. 6.6.1(j)(1).

<sup>63</sup> NER, cl. 6.6.1(j)(2).

<sup>64</sup> NER, cl. 6.6.1(j)(3).

Relevant factors under cl. 6.6.1(j)	AER consideration
	<p>reduce the magnitude of the storm repair costs or GSL payments, or that it took or omitted to take which has increased the magnitude of these payments. Prior to the Ministerial Order being made, AusNet Services took steps to minimise the magnitude of any GSL payments arising from outages caused by the June 2021 storms. This is demonstrated by its application to the ESC to exclude outages caused by the June 2021 storms from GSL calculation.</p> <p>Therefore, we do not consider that AusNet Services' actions increased the magnitude of the pass through amount.</p>
<p>We must take into account the time cost of money.<sup>65</sup></p>	<p>To account for the recovery of the pass through amount over four years commencing from 2022–23, we have used the nominal rate of return, as determined in AusNet Services' 2021–26 distribution determination, as well as a forecast inflation of 2 per cent to calculate the approved pass through amount in nominal terms.</p>
<p>We must take into account the need to ensure that the pass through amount reflects only costs incurred solely as a consequence of the June 2021 storms.<sup>66</sup></p>	<p>We have examined two alternative views regarding GSL payments. The first view is that GSL payments can be considered to have occurred solely as a consequence of the June 2021 storms as the GSL payments would not have been payable but for the June 2021 storms. The other view is that GSL payments are not a direct consequence of the June 2021 storms because the Ministerial Order directed AusNet Services to make these payments. While we note that different interpretations are open, in the context of this determination we have allowed the recovery of costs associated with GSL payments under the natural disaster event, based on our consideration of all relevant factors, including this factor (6.6.1(j)(5)). The GSL-related costs represent a material regulatory cost incurred by AusNet Services, which is largely outside its control. Under the revenue and pricing principles, AusNet Services is to be provided with a reasonable opportunity to recover efficient costs.</p>
<p>The AER will have regard to whether AusNet Services has insurance against the event, and whether it is the level of insurance that an efficient and prudent network operator would obtain?<sup>67</sup></p>	<p>AusNet Services submitted that none of the costs in this application related to insured structures. AusNet Services also submitted that it did not have insurance covering poles and wires of its network, and the insurance was limited to structures such as substations and buildings. AusNet Services stated that not insuring poles and wires is consistent with other network businesses. It explained that obtaining this insurance product is difficult and expensive as few insurers are willing to provide this high risk product. The associated premiums would consequently result in consistently high network charges for customers.<sup>68</sup></p> <p>We note that this approach to managing this risk is generally consistent with comparable peer NEM networks including</p>

<sup>65</sup> NER, cl. 6.6.1(j)(4).

<sup>66</sup> NER, cl. 6.6.1 (j)(5).

<sup>67</sup> AER, *Final decision AusNet distribution determination - Attachment 15 - Pass through events - May 2016*, p. 7.

<sup>68</sup> AusNet Services, *AusNet Services - 2020-21 Storms disaster event cost pass through - Application - November 2021*. p 24.

Relevant factors under cl. 6.6.1(j)	AER consideration
	those also impacted by other natural disasters (e.g., bushfires). As such, we are satisfied that it was prudent and efficient for AusNet Services to not obtain storms insurance cover for its poles and wires assets.
We must take into account whether the costs of the pass through event have already been factored into the calculation of the Distribution Network Service Provider's annual revenue requirement for the regulatory control period in which the pass through event occurred or will be factored into the calculation of the Distribution Network Service Provider's annual revenue requirement for a subsequent regulatory control period <sup>69</sup>	We do not consider the GSL costs that AusNet Services is proposing to recover have been factored into AusNet Services' annual revenue requirement for the regulatory control period in which the pass through event occurred (e.g. 2016–20) or in the annual revenue requirement for the subsequent regulatory control period (e.g. 2021–26). We include forecast GSL payments in annual revenue allowances when determining total opex forecast as part our distribution revenue determinations but GSL payments for events similar to the June 2021 storms were not accounted for in our 2016–2020 determination (including the 6-month extension). This is because under the GSL scheme applicable at the time (version 12), AusNet Services could apply to the ESC for an exemption to make GSL payments for supply interruptions exceeding a mandated threshold; which the June 2021 storms did.
We must take into account the extent to which AusNet Services' costs have already been funded by previous pass through determinations. <sup>70</sup>	AusNet Services submitted that it undertook temporary solutions to re-establish supply to some customers. This included deploying mobile generators and working directly with local councils to set up community hubs in some areas. We scrutinised costs related to this activity in the light of an allowance we provided in the context of bushfire cost pass through for acquisition of generators. AusNet Services provided evidence that it disposed of these generators and made necessary adjustments to the regulatory asset base. There is no evidence to suggest that costs included in AusNet Services' application have already been funded by previous pass through determinations.
We must take into account any other factors that we consider relevant. <sup>71</sup>	The other factors we took into account in our assessment of AusNet Services' application are set out below. The AER must exercise its power in a manner that will or is likely to contribute to the achievement of the National Electricity Objective (NEO). The AER may take into account the revenue and pricing principles set out in section 7A of the NEL. <sup>72</sup> In this matter, the principle that a regulated network service provider should be provided with a reasonable opportunity to recover efficient costs is applicable. The GSL payments represent a significant cost that has been incurred by AusNet Services (approximately 7.6% of allowed annual revenue).

Source: AER's analysis

<sup>69</sup> NER, cl. 6.6.1(j)(7).

<sup>70</sup> NER, cl. 6.6.1(j)(7A).

<sup>71</sup> NER, cl. 6.6.1(j)(8).

<sup>72</sup> NEL, s. 16(2)(b).

## Glossary

Term	Definition
AER	Australian Energy Regulator
Capex	Capital Expenditure
Minister	the Hon Lily D'Ambrosio, Victorian Minister for Energy, Environment and Climate Change
Ministerial Order	The order made on 18 November 2021 by the Hon Lily D'Ambrosio, Victorian Minister for Energy, Environment and Climate Change
NEL	National Electricity Law
NEM	National Electricity Market
Opex	Operating Expenditure

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