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# Attachment 7.2: Nominated pass throughs events

Ausgrid's 2024-29 Regulatory Proposal

Empowering communities for a resilient, affordable and net-zero future.



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# Contents



- 1. Introduction ..... 3
- 2. Our proposed pass through events ..... 4
- 3. Natural disaster event ..... 9

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# 1. Introduction

## 1.1 This document's purpose

The National Electricity Rules (**NER**) lists four defined pass through events in section 6.6.1(a1) and provides scope under section 6.5.10 for Ausgrid to propose additional 'nominated' pass through events in a Regulatory Proposal.

The purpose of this document is to put forward the nominated pass through events that Ausgrid considers should apply during our 2024-29 Regulatory Period.

## 1.2 This document in context

The NER requirements for pass through events (see section 1.4) establish the context for this document.

## 1.3 Document overview

We are proposing four nominated pass through events for our 2024-29 Regulatory Period, being:

- Natural disaster;
- Insurance coverage;
- Insurer's credit risk; and
- Terrorism.

The AER has previously approved these four events. Our proposal for the 2024-29 Regulatory Period includes substantive changes to the definition of 'natural disaster' event and minor adjustments to the other definitions.

## 1.4 Regulatory context

The following pass through events apply under clause 6.6.1(a) of the NER:

- (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.*

The scope to nominate additional pass through events as part of our 2024-29 Regulatory Proposal is set out in clause 6.5.10 of the NER, which states:

- a building block proposal may include a proposal as to the events that should be defined as pass through events under clause 6.6.1(a1)(5) having regard to the nominated pass through event considerations.*
- In determining whether to accept the pass through events nominated by a Distribution Network Service Provider in its building block proposal under paragraph (a), the AER must take into account the nominated pass through event considerations.*

## 2. Our proposed pass through events

Our proposed nominated pass through events are outlined in Table 2.1 to Table 2.4 below. For ease of reference, each table includes our proposed 2024-29 definition compared to the current version that applies to us. The explanation for our proposed changes is noted and, in the case of the natural disaster event, elaborated on in more detail in section 3 of this document.

Table 2.1 Natural disaster event

Our proposed 2024-29 definition	Our current 2019-24 definition	Explanation for changes
<p>Natural disaster events will include, but may not be limited to, natural disasters declared by a relevant government authority. Where a government authority has made a declaration that a natural disaster has occurred, the temporal and geographic scope of the natural disaster event will be defined by reference to the terms of that declaration.</p>	<p>A natural disaster event occurs if:</p> <ul style="list-style-type: none"> <li>Any major fire, flood, earthquake or other natural disaster occurs during the 2019-24 regulatory control period and materially increases the costs to Ausgrid 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.</li> <li>The term 'major' in the above paragraph means an event that is serious and significant. It does not mean material as that term is defined in the Rules (that is 1 per cent of the DNSP's annual revenue requirement for that regulatory year).</li> </ul> <p>Note: in assessing a natural disaster event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>Whether Ausgrid has insurance against the event,</li> <li>The level of insurance that an efficient and prudent NSP would obtain in respect of the event,</li> <li>Whether a relevant government authority has made a declaration that a natural disaster has occurred.</li> </ul>	<p>See section 3 for detailed reasons supporting our proposed 2024-29 definition.</p>

Table 2.2 Insurance coverage event (formerly 'insurance cap' event)

Our proposed 2024-29 definition	Our current 2019-24 definition	Explanation for changes
<p>An insurance coverage event occurs if:</p> <ol style="list-style-type: none"> <li>1. Ausgrid:               <ol style="list-style-type: none"> <li>a) makes a claim or claims and receives the benefit of a payment or payments under a relevant insurance policy or set of insurance policies; or</li> <li>b) would have been able to make a claim or claims under a relevant insurance policy or set of insurance policies but for changed circumstances; and</li> </ol> </li> <li>2. Ausgrid incurs costs:               <ol style="list-style-type: none"> <li>a) beyond a relevant policy limit for that policy or set of insurance policies; or</li> <li>b) that are unrecoverable under that policy or set of insurance policies due to changed circumstances; and</li> </ol> </li> <li>3. The costs referred to in paragraph 2 above materially increase the costs to Ausgrid in providing direct control services.</li> </ol> <p>For the purposes of this insurance coverage event:</p> <p>'changed circumstances' means movements in the relevant insurance liability market that are beyond the control of Ausgrid, where those movements mean that it is no longer possible for Ausgrid to take out an insurance policy or set of insurance policies at all or on reasonable commercial terms that include some or all of the costs referred to in</p>	<p>An insurance cap event occurs if:</p> <ul style="list-style-type: none"> <li>• Ausgrid makes a claim or claims and receives the benefit of a payment or payments under a relevant insurance policy,</li> <li>• Ausgrid incurs costs beyond the relevant policy limit, and</li> <li>• The costs beyond the relevant policy limit materially increase the costs to Ausgrid in providing direct control services.</li> </ul> <p>For this insurance cap event:</p> <ul style="list-style-type: none"> <li>• The relevant policy limit is the greater of:               <ul style="list-style-type: none"> <li>○ Ausgrid's actual policy limit at the time for the event that gives, or would have given rise to a claim, and</li> <li>○ The policy limit that is explicitly or implicitly commensurate with the allowance for insurance premiums that is included in the forecast operating expenditure allowance approved in the AER's final decision for the regulatory control period in which the insurance policy is issued.</li> <li>○ A relevant insurance policy is an insurance policy held during the 2019-24 regulatory control period or a previous regulatory control period in which Ausgrid was regulated.</li> </ul> </li> </ul>	<p>Our proposed 2024-29 definition of an 'insurance coverage' event reflects the AER's latest regulatory determinations for the Victorian electricity distributors<sup>1</sup> and the AER's Guidance Note on the Insurance Coverage Pass through Event.<sup>2</sup></p>

<sup>1</sup> AER (2021), [Final Decision - Ausgrid distribution determination 2021-26 - Pass through events](#), pp. 15-13 to 15-15.

<sup>2</sup> AER (2021), [Final guidance note - Insurance coverage pass through event](#)

Our proposed 2024-29 definition	Our current 2019-24 definition	Explanation for changes
<p>paragraph 2 above within the scope of that insurance policy or set of insurance policies.</p> <p>'costs' means the costs that would have been recovered under the insurance policy or set of insurance policies had:</p> <ul style="list-style-type: none"> <li>i. the limit not been exhausted; or</li> <li>ii. those costs not been unrecoverable due to changed circumstances.</li> </ul> <p>A relevant insurance policy or set of insurance policies is an insurance policy or set of insurance policies held during the regulatory control period or a previous regulatory control period in which Ausgrid was regulated; and</p> <p>Ausgrid will be deemed to have made a claim on a relevant insurance policy or set of insurance policies if the claim is made by a related party of Ausgrid in relation to any aspect of Ausgrid's network or business; and</p> <p>Ausgrid will be deemed to have been able to make a claim on a relevant insurance policy or set of insurance policies if, but for changed circumstances, the claim could have been made by a related party of Ausgrid in relation to any aspect of Ausgrid's network or business.</p> <p>Note for the avoidance of doubt, in assessing an insurance coverage event through application under rule 6.6.1(j), the AER will have regard to:</p> <ul style="list-style-type: none"> <li>i. the relevant insurance policy or set of insurance policies for the event</li> <li>ii. the level of insurance that an efficient and prudent DNSP would obtain, or would have sought to obtain, in respect of the event;</li> <li>iii. any information provided by Ausgrid to the AER about Ausgrid's actions and processes; and</li> </ul>	<p>Note for the avoidance of doubt, in assessing an insurance cap event cost pass through application under rule 6.6.1(i), the AER will have regard to:</p> <ul style="list-style-type: none"> <li>• The relevant insurance policy for the event, and</li> <li>• The level of insurance that an efficient and prudent NSP would obtain in respect of the event.</li> </ul>	



Our proposed 2024-29 definition	Our current 2019-24 definition	Explanation for changes
iv. any guidance published by the AER on matters the AER will likely have regard to in assessing any insurance coverage event that occurs.		

Table 2.3 Insurance credit risk event

Our proposed 2024-29 definition	Our current 2019-24 definition	Explanation for changes
<p>An insurer's credit risk event occurs if an insurer of Ausgrid becomes insolvent, and as a result, in respect of an existing or potential claim for a risk that was insured by the insolvent insurer, Ausgrid:</p> <ul style="list-style-type: none"> <li>a) Is subject to a higher or lower claim limit or a higher or lower deductible than would have otherwise applied under the insolvent insurer's policy; or</li> <li>b) Incurs additional costs associated with funding an insurance claim, which otherwise have been covered by the insolvent insurer.</li> </ul> <p>Note: In assessing an insurer's credit risk event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>i. Ausgrid's attempts to mitigate and prevent the event from occurring by reviewing and considering the insurers track record, size, credit rating and reputation.</li> <li>ii. In the event that a claim would have been made after the insurance provider became insolvent, whether Ausgrid had reasonable opportunity to insure the risk with a different provider.</li> </ul>	<p>An insurer's credit risk event occurs if:</p> <ul style="list-style-type: none"> <li>• A <b><u>nominated</u></b> insurer of Ausgrid becomes insolvent, and as a result, in respect of an existing or potential claim for a risk that was insured by the insolvent insurer, Ausgrid: <ul style="list-style-type: none"> <li>○ Is subject to a higher or lower claim limit or a higher or lower deductible than would have otherwise applied under the insolvent insurer's policy; or</li> <li>○ Incurs additional costs associated with funding an insurance claim, which otherwise have been covered by the insolvent insurer.</li> </ul> </li> </ul> <p>Note: In assessing an insurer's credit risk event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>• Ausgrid's attempts to mitigate and prevent the event from occurring by reviewing and considering the insurers track record, size, credit rating and reputation.</li> <li>• In the event that a claim would have been made after the insurance provider became insolvent, whether Ausgrid had reasonable opportunity to insure the risk with a different provider.</li> </ul>	<p>Minor editorials to reflect the AER's latest round of determinations.</p> <p>These editorials are:</p> <ul style="list-style-type: none"> <li>• Combining the first dot-point in the current 2019-24 definition with the opening paragraph;</li> <li>• Removing the word 'nominated' (see <b><u>nominated</u></b>) given this word does not add to or modify the meaning of the text; and</li> <li>• Converting the dot-points to (A) and (B) and (i) and (ii)</li> </ul>

Table 2.4 Terrorism event

Our proposed 2024-29 definition	Our current 2019-24 definition	Explanation for changes
<p>Terrorism event means an act (including, but not limited to, the use of force or violence or the threat of force or violence) of any person or group of persons (whether acting alone or on behalf of or in connection with any organisation or government), which:</p> <ul style="list-style-type: none"> <li>a) from its nature or context is done for, or in connection with, political, religious, ideological, ethnic or similar purposes or reasons (including the intention to influence or intimidate any government and/or put the public, or any section of the public, in fear); and</li> <li>b) changes the costs to Ausgrid in providing direct control services.</li> </ul> <p>Note: In assessing a terrorism event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>i. whether Ausgrid has insurance against the event;</li> <li>ii. the level of insurance that an efficient and prudent NSP would obtain in respect of the event; and</li> <li>iii. whether a declaration has been made by a relevant government authority that a terrorism event has occurred.</li> </ul>	<p>A terrorism event occurs if:</p> <ul style="list-style-type: none"> <li>• An act (including, but not limited to, the use of force or violence or the threat of force or violence), attacks or other disruptive activities against the critical infrastructure or underlying technology, or the threat of such attacks or disruptive activities, or the deliberate introduction of malware) of any person or group of persons (whether acting alone or on behalf of or in connection with any organisation or government), which from its nature or context is done for, or in connection with, political, religious, ideological, ethnic or similar purposes or reasons (including the intention to influence or intimidate any government and/or put the public, or any section of the public, in fear) and which materially increases the costs to Ausgrid in providing direct control services.</li> </ul> <p>Note: In assessing a terrorism event pass through application, the AER will have regard to, amongst other things:</p> <ul style="list-style-type: none"> <li>• Whether Ausgrid has insurance against the event,</li> <li>• The level of insurance that an efficient and prudent NSP would obtain in respect of the event, and</li> <li>• Whether a declaration has been made by a relevant government authority that a terrorism event has occurred.</li> </ul>	<p>Minor editorials to reflect the AER's latest round of determinations.</p> <p>These editorials are:</p> <ul style="list-style-type: none"> <li>• Combining the first dot-point in the current 2019-24 definition with parts of the opening paragraph; and</li> <li>• Splitting the key requirements in the first dot-point of the current 2019-24 definition into two limbs (A) and (B).</li> </ul>



# 3. Natural disaster event

The AER approved a ‘natural disaster’ pass through event for our 2019-24 period. We assess the current definition (**section 3.1** below) and then propose an alternative set of words for the 2024-29 period (**section 3.2** below).

## 3.1 Our assessment of the current definition

The current definition of a ‘natural disaster’ event is set out in **Table 3.1** below. Each element is marked ‘A’ to ‘G’ for ease of reference when outlining our views (see **sections 3.1.1** to **3.1.3**).

Table 3.1 The current definition broken down into its key elements

Reference	Definitional element (emphasis added)
A	A natural disaster event occurs if:
B	<ul style="list-style-type: none"><li>Any <b>major</b> fire, flood, earthquake or other natural disaster occurs during the 2019-24 regulatory control period and materially increases the costs to Ausgrid 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.</li></ul>
C	<ul style="list-style-type: none"><li>The term '<b>major</b>' in the above paragraph means an event that is <b>serious and significant</b>. It does not mean material as that term is defined in the Rules (that is 1 per cent of the DNSP's annual revenue requirement for that regulatory year).</li></ul>
D	Note: in assessing a natural disaster event pass through application, the AER will have regard to, amongst other things:
E	Whether Ausgrid has <b>insurance</b> against the event,
F	The <b>level of insurance that an efficient and prudent</b> NSP would obtain in respect of the event,
G	Whether a relevant <b>government authority has made a declaration</b> that a natural disaster has occurred.

### 3.1.1 Centrality of the term ‘major’ in the current definition

In the first part of the current ‘natural disaster’ definition (see ‘A’ to ‘C’ in Table 3.1 above), the term ‘major’ takes a central position. This includes expressly defining the term as ‘serious or significant’ (see ‘C’ in Table 3.1 above) which in our view does not provide additional guidance about how the AER will recognise the coverage and scope of a natural disaster event. All fire, floods and earthquakes that pass the NER pass through materiality threshold (1% of Ausgrid’s annual revenue) will be ‘serious or significant’.

Our proposed alternative set of words is set out in **section 3.2** below. It shifts the focus away from defining broad terms such as ‘major’, in favour of establishing a clear mechanism to determine the temporal and geographic limits of a natural disaster.

### 3.1.2 Overlapping considerations in the NER

The second part of the current definition (see sections ‘D’ to ‘F’ in Table 2.1 above) focuses on insurance. We agree that this is an important consideration, yet it is one the AER is already required to consider in the NER.

In assessing a pass through application, clause 6.6.1(j) of the NER requires the AER to assess (emphasis added):

*... the efficiency of the Distribution Network Service Provider's **decisions and actions in relation to the risk of the positive change event**, including whether the Distribution Network Service Provider has failed to take **any action that could reasonably be taken to reduce the magnitude of the eligible pass through amount in respect of that positive change event** and whether the Distribution Network Service Provider has taken or omitted to take any action where such action or omission has increased the magnitude of the amount in respect of that positive change event..*

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Whether insurance has been obtained in relation to a natural disaster event (see 'E' in Table 3.1 above) would be directly relevant to the 'decisions and actions in relation to the risk of the positive change event' which the AER must consider in clause 6.6.1(j)(3). The level of insurance (see 'F' in Table 3.1 above) obtained would also fall under the AER's required assessment of whether 'any action that could reasonably be taken to reduce the magnitude of the eligible pass through amount [has been obtained]' (see clause 6.6.1(j)(3)). This prompts us to find that insurance, while an important consideration, is already dealt with in the NER and does not necessarily have to be included in the 'natural disaster' event definition.

### 3.1.3 The relevance of a government authority declaration

The final part of the current definition (see section 'G' in **Table 2.1** above) relates to 'whether a relevant government authority has made a declaration that a natural disaster has occurred'.

We consider the reference to a declaration from a government authority to be pertinent. It is also a factor that is not considered in the NER, reinforcing the need for its inclusion in the 'natural disaster' definition. The way we consider this should happen is outlined in **section 3.2** below.

## 3.2 Our proposed 'natural disaster' event definition

We propose the following definition for a natural disaster event in our 2024-29 Regulatory Period:

***Natural disaster events will include, but may not be limited to, natural disasters declared by a relevant government authority. Where a government authority has made a declaration that a natural disaster has occurred, the temporal and geographic scope of the natural disaster event will be defined by reference to the terms of that declaration*** (emphasis added).

Our proposal builds on the reference in the current definition to a declaration by a government authority (see section 3.1.3 above). However, we consider these declarations can take on a more central position given that they:

- confirm whether a natural disaster event has occurred; and
- are accompanied by information regarding the time of the event and the impacted locations.

We outline our reasoning in greater detail in **sections 3.2.1** and **3.2.2** below. The NSW Government website which sets out disaster declarations can be accessed here: <https://www.nsw.gov.au/disaster-recovery/natural-disaster-declarations#toc-financial-year-2022-23>.

### 3.2.1 Clear mechanism to define the scope and boundaries of natural disasters

Natural disaster declarations from a government authority provide a clear mechanism for identifying the temporal and geographic scope of the event in question.

The clarity of the mechanism stems from its specificity. NSW government declarations state the timing of the event and the impacted Local Government Areas.<sup>3</sup> Using this information, the AER can clearly define the temporal and geographic boundaries of a natural disaster event, without having to investigate meteorological data or other scientific information.

### 3.2.2 Use of objective expertise to define the scope and boundaries of natural disaster

Government authorities tasked with making natural disaster declarations are an objective source of the expertise needed to identify the scope and boundaries of these events. This expertise is likely to become increasingly important as climate change leads to compounding storm and other natural disaster activity occurring over large geographical areas and potentially longer timespans.

Our proposed definition of a natural disaster event provides a mechanism for the AER to leverage this expertise to define the scope and boundaries of a natural disaster. It also avoids relying on hard to define words such as 'major' (see **section 3.1.1** above) and allows the AER to focus on its core economic analysis relating to a pass through application, rather than interpreting meteorological and other data to inform its determination.

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<sup>3</sup> <https://www.nsw.gov.au/disaster-recovery/natural-disaster-declarations#toc-financial-year-2022-23>.