



30 October 2020

Sebastian Roberts  
General Manager Transmission and Gas  
Australian Energy Regulator

By email: [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au)

Dear Sebastian

**Re: Consultation on the guidance note on key matters the AER is likely to have regard to when assessing an insurance coverage event application**

CitiPower, Powercor and United Energy welcome the opportunity to respond to the Australian Energy Regulator's (AER) consultation paper on the guidance note on key matters the AER is likely to have regard to when assessing an insurance coverage event application.

We support the AER providing further guidance on the matters it is likely to have regard to when assessing the insurance coverage event application. However, general liability insurance for electricity distribution is an extremely complex matter. As such, we caution against expectations of uniformity in insurance policies, documentation and risk appetites, given the vast differences in risk profiles of each distributor from its asset profile, environment, weather exposure, policy sharing and similar.

While the guidance note is useful in ensuring distributors can demonstrate the efficiency of their insurance policies, it should not be used as a tool for comparison of policies across distributors and it should be flexible enough to allow for assessment of the individual circumstances of each distributor at the time the policy, or set of policies, was obtained.

Our responses to the AER's questions and issues raised in the consultation paper are provided below.

**Independent reviews of distributors' insurance policies are not in the long-term interests of consumers**

In its consultation paper the AER suggests that distributors should obtain an independent report or certification from an insurance expert to validate its insurance coverage or policy. We do not consider this to be practical or in the long-term interest of consumers.

The specialist insurance market in which distributors obtain general liability insurance is extremely tight with only a few insurance brokers or insurance experts. These experts or brokers compete in the tight insurance market to obtain coverage for their clients, the distributors. Allowing a competitor insurance expert or broker to review policies and processes available to and considered by other insurance brokers would compromise competitive market processes, including any distributors' competitive position in the future and is likely to result in convergence of prices that is not in the long-term interest of consumers.

The AER should accept as evidence of the appropriateness of a distributor's coverage a report or certification from that distributor's broker.

**We support consumers' input into the insurance discussion however engagement will be challenging**

The global insurance market is in disruption which is resulting in higher prices for lower coverage, and the future of the market is uncertain. Consumers should be aware of the risks that result from the tightening market as well the impact this will have on their electricity prices.

As such, we plan to engage with our newly established Customer Advisory Panel on our general liability insurance on an annual basis, demonstrating the changing risk profiles as well as the options that are available for insurance at the time. However, we are cognisant of the high complexity of the topic, the speed at which

market offerings need to be settled across the stack of insurance cover, and the highly commercially sensitive nature of the insurance offering, all of which might limit meaningful customer input into the decision-making process.

Over time we expect the level of understanding and knowledge of the customer groups will improve, however, it will always remain important that any final decisions on our insurance policy are based on current evidence, prevailing market offerings and industry expertise.

As such, we agree that consumers should have a say regarding relative cost-risk trade-offs relating to insurance coverage and the cost of insurance. However, we caution against putting significant weight on this input for insurance coverage decisions in a given policy year, given the high complexity of the matter and speed at which insurance offers are undertaken.

### **Benchmarking of general liability insurance will not result in reliable outcomes**

In its consultation paper the AER questioned whether there is benefit in establishing an annual information process that provides networks the opportunity to inform and update the AER of material changes or to enable benchmarking across networks.

We believe there are merits in having an on-going conversation about the global insurance market between the industry and the AER. However, we do not support benchmarking of insurance policies between the networks and comparisons of policies are unlikely to result in reliable outcomes for the following reasons:

- there can be vast differences between networks' risk profiles (including, for example, from different operating environments, network characteristics, risk mitigation activities and past claims), which would make benchmarking irrelevant
- different ownership structures can lead to shared policies, such as with SA Power Networks, CitiPower, Powercor and United Energy. The shared policies are inherently more complex to untangle and cannot be compared to individual network policies
- there are many insurance product options in the specialist insurance market, some of which can be custom developed and therefore not available to all networks
- because of the highly competitive nature of the tight specialist insurance market, any benchmarking exercise would be based on highly confidential information. Therefore, the veracity of the benchmarking could not be tested by the AER with distributors or stakeholders and the benchmarking could not be relied upon as a publicly available benchmarking tool.

### **Existence of the pass-through event does not diminish incentive schemes**

We do not consider that the pass-through event will diminish the effectiveness of the existing incentives schemes under which we operate. This is because:

- we have continuous incentives to ensure we employ cost effective risk mitigation measures irrespective of the pass-through provisions because:
  - any risk mitigation activities act to minimise the costs of our insurance premiums in a highly competitive market, and claims on our insurance would lead to higher premiums in subsequent years
  - ex ante we do not know the scale or scope of the third party liability we may be exposed to in an event
  - the AER's decision to accept a pass-through application is ex post and not guaranteed, and we would expect the AER's assessment of our pass-through application to take account of the efficiency of risk mitigation measures. Additionally, there are costs associated with the application for the pass-through event

- a significant portion of our safety program is due to safety obligations, rather than driven by incentives, which ensures safety measures are in place to reduce bushfire risk as far as practicable. Additional to the obligations, we have the f-factor incentive scheme to reduce bushfire risk even further
- we are responsible for costs up to the value of the deductible (normally in millions) under any claim within the general liability insurance.

As such, we believe the current incentive-based framework combined with our safety obligations ensures distributors do not inefficiently under invest in risk mitigation measures due to the existence of the pass-through event.

**The AER should ensure the guidance note is in line with the most recent insurance coverage pass-through event definition and the event definition should require the AER to have regard to the guidance note**

The AER has recently updated the 'insurance cap event' to the 'insurance coverage event' in its South Australia and Queensland 2020-2025 final determinations, to account for the potential gaps in insurance coverage resulting from the current global market disruption. The wording of the event includes some matters to which the AER will have regard in the case of an event being triggered.

The Victorian distributors are yet to have their determinations finalised in April 2021, which may include further changes to the wording of the insurance coverage event. The AER should ensure that the final guidance note aligns with the final definition of the insurance coverage event for Victorian distributors.

We also note that the insurance coverage pass through event definition should require the AER to have regard to any guidance published by the AER on the matters it will likely have regard to in assessing any insurance coverage event that occurs.

Should you have any queries about this submission please do not hesitate to contact [REDACTED]

Yours sincerely,



Renate Vogt  
**General Manager Regulation**  
**CitiPower, Powercor and United Energy**