

16 August 2013

Mr Chris Pattas

General Manager
Network Operations and Development
Australian Energy Regulator
Level 35, The Tower
360 Elizabeth St
Melbourne Victoria 3000

email: expenditure@aer.gov.au

Dear Mr Pattas

Revised draft economic benchmarking templates for comment

The Energy Networks Association (ENA) is pleased to have this opportunity to respond to the Australian Energy Regulator's emails dated 22 July, 31 July and 5 August on the revised draft economic benchmarking templates.

We note also that the AER has recently published its draft forecast assessment guidelines and associated explanatory statement which deals extensively with matters to do with data availability, quality and collection. The ENA will be responding to those matters by the stated deadline of 20 September.

This response addresses three issues where further discussion and guidance is needed to achieve the objectives proposed by the AER.

1. Clarity of definitions

The ENA considers that it is very important that the AER ensure that the definitions in the benchmarking RIN are clear and precise in order to ensure that data collected is consistent across NSPs and through time. Inconsistent interpretations of the data requirements across business would distort the results of any benchmarking models. At present it is the ENA's view that many of the definitions set out in the draft RIN do not provide sufficient clarity regarding the exact information that is to be provided.

This section sets out some specific areas where the data definitions are particularly unclear.

It not completely clear whether each NSP is to report the data based on the regulatory year applicable to them. It is unlikely that a NSP could provide the data for a different year.

DOPEX 01 to 08 - Opex categories

The draft RIN requests that NSPs should populate the opex categories on the basis of their annual RIN categories. This information will be inconsistent across DNSPs in different jurisdictions and

therefore will be of limited value for economic benchmarking. The AER should specify which opex categories it requires for the economic benchmarking purposes. For example in Victoria, vegetation management is not reported separately from other routine maintenance expenditure in the annual RIN which is inconsistent with practises in some other jurisdictions. However the AER would require this information to understand the drivers of increased opex in recent years for some networks.

DRAB0101 to DRAB0110

It is not currently possible to directly allocate RAB Asset values to these proposed categories. Some form of allocation process would be required. For example current Distribution RAB templates do not distinguish between overhead and underground lines.

OPSD 01 to 08 & DEF01 03 – Peak demand

Peak demand measures are requested at zone substation level however this will fail to take account of demand from customers directly connected at sub-transmission voltages. Peak demand should therefore be measured at the terminal station level.

DOPSD 02, 04, 06, 08 – Weather adjusted peak demand

The definition does not specify on what basis (i.e. the Probability of Exceedance level) the weather adjustment should be reported.

DOPSD 09 - Power factor conversion between MVA and MW

Real power (MW) rather than apparent power (MVA) is the output valued by customers. An efficient network investment in capacitor banks is likely to reduce the power factor and apparent power at peak demand, however it would also increase cost inputs in the AER's economic modelling and would therefore be regarded as a sign of increased network inefficiency. The power factor level varies by zone substation depending on the day of maximum demand and load characteristics. Therefore the power factor and apparent power data requirements should be removed from the AER templates.

DSQ 01 – SAIDI

The unit of measurement is minutes however the description is minutes/customers. It is therefore not clear if the index is required or total customer minutes off supply.

DSQ 02 – Distribution –related unplanned SAIDI

The unit of measurement is minutes however the description relates to customer numbers. It is therefore not clear what is required.

DQS 05 - Network utilisation

The proposed definition should not include network length in system capacity as it would mean that network utilisation would be more a function of line length of the network than the use of the network. A ratio of non-coincident peak demand compared to the sum of transformer capacity at the last distribution transformer level would be independent of line length.

If however the AER retains the current definition then it would be necessary to clarify if 'total network length' is based on route or circuit kilometres.

DEF02 02 - Vegetation encroachment

This item is not clearly defined. The definition needs to specify what 'requiring vegetation management' means. For example - does it mean spans are inspected or cut or both? Based on the current definition most DNSPs could reasonably assign a 100% value in all years on the basis that the entire network requires vegetation management at all times.

The definition needs to clarify that the DNSP is responsible for undertaking any cutting that is required and would not include any spans that would be responsibility of third parties such as Councils.

A percentage of spans 'managed' are not likely to give the AER information about vegetation effort. This is because a DNSP with a small number of spans could have the same % of spans managed as a DNSP with a large number of spans.

DEF02 03 – Standard vehicle access

More clarity is required on how to calculate the percentage. For example - is it measured in kilometres of line? Are 'open paddocks' included where they are not easily accessible due to fencing and locked gates?

2. RIN audit requirements

The ENA considers that high quality data is essential to the credibility of the AER's benchmarking. The AER has indicated that it will be relying on its benchmarking analysis to:

- Publish the annual benchmarking reports which will attract significant media and investor attention and have real business impacts;
- Make an assessment of whether DNSPs are responding to the Efficiency Benefit Sharing Scheme; and
- Determine whether or not revealed costs should be applied as the basis for expenditure forecasts.

These are not trivial decisions and it is therefore essential that the AER seek to use high quality data as the basis for its benchmarking analysis. The ENA therefore consider that it is essential that all data, financial and non-financial, provided by DNSPs for the purposes of benchmarking are audited against a clearly defined standard.

The AER has proposed that financial data that reconciles with data previously provided to the AER would not require audit. The ENA considers, however, that where the disaggregation of data will impact on the benchmarking results then the disaggregation of this data should be audited against the defined standard. If this were not the case the benchmarking results are likely to be distorted by measurement errors. The AER has proposed that, in lieu of audit, Director Certification that the data meets the requirements is appropriate. The ENA are concerned that this proposal risks placing Directors in an impossible position. Section 28N of the National Electricity Law which requires NSPs to comply with a RIN is a civil penalty provision. Therefore, in order for Directors to confidently certify that the data complies with the RIN they will require audit assurance. If audit assurance is not provided then Director's would face a significant risk of the AER taking enforcement action. This is an unreasonable position that would be unacceptable to any Director.

In addition, Directors are likely to be extremely anxious about providing assurance about historical data that was collected for a different purpose, with different reporting requirements and potentially under different management or ownership arrangements.

The AER has also proposed 'a special purpose financial report providing reasonable assurance that the data provided has been prepared with the RIN requirements would be appropriate for non-financial data'. Notwithstanding the ENA's view that audit of all data, including non-financial data is essential for accurate benchmarking, the ENA is interested in understand further details of what such as special purpose report could involve. ENA is open to further exploring pragmatic, practical mechanisms to ensure that data quality issues and legal enforcement risks are adequately resolved, whether through the proposed 'special purpose' report or any other mechanism.

3. Provision of historical data

The templates that the AER has provided for comment would require businesses to provide data for the 10 year period 2003 to 2012 inclusive. It is reasonable to assume that no business will be in a position to populate the templates directly from information that it has on record given that:

- Data may never have been collected in the form or on the basis requested;
- Data may have been collected but the records are no longer accessible;
- Data may be available but in a form such that there can be no assurance of its quality or basis; and
- Data may only be available at an aggregated level such that it has to be allocated or otherwise adjusted to produce information in the form and at the level of detail specified.

If data quality and consistency cannot be assured, then any conclusions drawn from that data will be compromised.

The AER has indicated that "where actual data isn't available then [it] will request that NSPs provide their best estimate of the data. To provide transparency, templates request that NSPs outline where they have extracted data from and any assumptions or allocations made".

If businesses are to be required to populate every data item in the templates with information taken directly from their records or, where that information is not available, by adjusting information that is available (e.g. by allocating an aggregate value to its components), or simply by providing an estimate, then there can be no assurance as to overall data quality and consistency. That is especially so if each business is free to adopt its own assumptions and methods to produce the data.

The ENA and members have, on numerous occasions in the course of the current consultation including in workshops and submissions expressed their concerns about the use of historical data for benchmarking, especially if the results of the analysis are to be used to inform regulatory processes. Those concerns are supported by the conclusions that the AEMC reached in 2011 following its detailed review into the use of Total Factor Productivity (TFP) for the determination of prices and revenues.

The AEMC conducted its review in the context of a rule change proposal that, if adopted, would have seen the rate of change—and only the rate of change—of prices set by reference to industry TFP. Importantly, the level of prices would have been re-set to costs at each price review. The AEMC concluded that the quality and reliability of available historical data was such that TFP could

not be measured with sufficient certainty to support that limited application. The AEMC recommended a forward-looking process to establish a reliable and consistent data set to support the measurement of TFP.

The ENA accepts that the AER does not intend to use benchmarking methods deterministically to set the level of allowances. However, the AER has indicated it may use benchmarking results to inform a view that a business's base year costs are not efficient, thus opening the way for the AER to substitute a value. Even though benchmarking may not be used directly to set the substitute value, the exposure for the business in that case is potentially significant. In order to populate every data item in the templates each business should be allowed to develop its own assumptions and methods for producing the data. However, a consequence of this practical approach is that if each business documents its data sources, assumptions and methods as proposed by the AER, the data will still require adjustment and rebasing prior to its use in any measurements across different businesses.

The ENA appreciates the work put into the revised draft economic benchmarking templates by the AER and appreciates the opportunity to continue to contribute to its development. If you have any questions please contact Jim Bain on 02 6272 1516.

Yours sincerely



John Bradley
Chief Executive Officer