



Decision

Cost pass through

Endeavour Energy's 2019-20 bushfire natural disaster event

February 2021

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1. Summary of our assessment

During the regulatory control period Endeavour Energy can apply to pass through to its customers, in the form of higher or lower network charges, certain material changes in its costs caused by pre-defined exogenous events. These events are called cost pass through events. Such events are limited to circumstances where the business can recover potential costs of defined yet unpredictable, high cost events that are outside the control of the business.

On 31 August 2020 Endeavour Energy submitted a cost pass through application seeking recovery of actual and expected costs as a result of bushfires that occurred between November 2019 and February 2020.

Endeavour Energy submitted that the bushfires caused significant damage to parts of its network, affecting approximately 11,000 km² or 44 per cent of its network area. The fires either damaged or destroyed 840 homes and businesses connected to the network and interrupted supply to over 55,000 customers.¹

For a positive pass through to be determined there must be a positive change event. That is:

- A pass through event specified in either the National Electricity Rules (NER) or in our current revenue determination for Endeavour Energy² (in this case, a natural disaster event) – typically an event that is largely unavoidable and with unforeseeable timing, and
- That event must entail Endeavour Energy incurring materially higher costs in providing direct control services than it would have incurred but for the event.

Endeavour Energy may then submit a pass through application.³ Its application must address certain matters specified in the NER.⁴

We must then make a determination on Endeavour Energy's pass through application and, if a positive change event occurred, determine the approved pass through amount and the regulatory years in which the pass through amount is to be recovered from electricity consumers. In making our determination on Endeavour Energy's pass through application, we must have regard to certain matters, which are specified in the NER.⁵

Our consideration of these requirements is set out in section 6 below.

In summary, we are satisfied that the 2019–20 bushfires that are the subject of Endeavour Energy's application constitute a single positive change event⁶ and that Endeavour Energy's pass through application addresses the matters required by the NER. Most notably that the

¹ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 11.

² AER, Final Decision: Endeavour Energy 2015-16 to 2018-19 Distribution Determination – Attachment 15 – Pass Through Events, April 2015.

³ Cl. 6.6.1(a) of the Rules.

⁴ Cl.6.6.1(c) of the Rules.

⁵ Cl. 6.6.1(j) of the Rules.

⁶ See Table 1 of section 6 for our assessment of this.

bushfire event was not caused by Endeavour Energy; the costs incurred in providing direct control services as a result of the event meet the materiality threshold; and the costs due to the bushfires were not already funded through insurance, self-insurance, or other regulatory allowances.

However, we are not satisfied that Endeavour Energy's proposed positive pass through amount of \$31.3 million (\$2019–20)⁷ in increased costs due to the bushfires meets the requirements of the NER. Specifically, we do not consider that the proposed \$7.8 million (\$2019–20) in herbicide spraying costs reflects costs that are required to restore network services to pre-event levels. We are satisfied that the remainder of Endeavour Energy's proposed positive pass through amount reflects a necessary and efficient response to the bushfires.

We accept Endeavour Energy's proposal to recover the pass through amount over the final three years of the current regulatory control period commencing in financial year 2021–22 (FYs 2021–22, 2022–23 and 2023–24). The smoothing of the recovery of the pass through amount will reduce bill volatility and maintain the downward trend in network prices.

Our determination is to approve a positive pass through amount of \$26.7 million (\$2019–20).⁸ The resulting revenue impact totals \$25.8 million (\$ nominal, smoothed) for the 2019–24 regulatory control period, consisting of:

- \$8.4 million to be recovered in 2021–22
- \$8.6 million to be recovered in 2022–23, and
- \$8.8 million to be recovered in 2023–24.

The proposed cost pass through is estimated to incrementally increase the average annual bill of residential customers by approximately \$5 (\$ nominal) and by \$19 (\$ nominal) for small businesses over 1 July 2021 to 30 June 2024.

⁷ This is \$31.2 million in 2018–19 dollar terms as per the proposed pass through PTRM. The resulting revenue impact totals \$31.1 million for the 2019–24 period in nominal terms.

⁸ This is \$26.6 million in 2018-19 dollar terms as per the AER pass through final decision PTRM.

2. Introduction

We received a cost pass through application from Endeavour Energy for additional expenditure associated with restoring supply and repairing damage to its network caused by the 2019–20 summer bushfires.

Endeavour Energy proposed to recover additional revenue of \$31.1 million (\$ nominal, smoothed)⁹ over the final three years of the 2019–24 regulatory control period from consumers as a result of an increase in costs incurred to restore supply and replace damaged parts of their network.

2.1. Who we are and our role in this process

We, the AER, work to make all Australian energy consumers better off, now and in the future. We are the economic regulator for electricity distribution and transmission services in the NEM. Our electricity-related powers and functions are set out in the National Electricity Law and NER.¹⁰

Endeavour Energy's revenues are regulated by the AER through five year distribution revenue determinations. The current revenue determination commenced on 1 July 2019 and will finish on 30 June 2024.

We are responsible for assessing pass through applications. Under the pass through provisions in 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 their revenue determination.¹¹

2.2. Endeavour Energy's application

On 31 August 2020 Endeavour Energy submitted a cost pass through application seeking recovery of actual and expected costs as a result of the 2019–20 bushfires.

Endeavour Energy stated that bushfires caused significant damage, affecting approximately 11,000 km² or 44 per cent of its network area. The fires either damaged or destroyed 840 homes and businesses connected to the network and interrupted supply to over 55,000 customers. Endeavour Energy established a Customer Management Working Group and Bushfire Customer Liaison Roles to keep customers safe and informed and to assist in coordinating internal and external customer response activities. The emergency restoration and subsequent response included, inspecting bushfire-affected spans of conductor to identify damage, deploying 95 portable diesel generators to provide temporary supply, replacing 999 poles and the clearing of damaged and dangerous vegetation in and around

⁹ This is a result of the proposed pass through amount of \$31.3 million (\$2019–20).

¹⁰ 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.

¹¹ Cl.6.6.1 of the Rules.

easements.¹² The three major bushfires that are the subject of Endeavour Energy's application are:

- The Gospers Mountain bushfire (Blue Mountains/Hawkesbury): The fire started on 26 October 2019 and joined with other fires over November and December 2019 burning 512,000 hectares across the Lithgow, Hawkesbury, Hunter Valley, Cudgegong, Blue Mountains and Central Coast local government areas and. The fire was contained on 12 January 2020 and extinguished on 7 February 2020.
- The Green Wattle Creek bushfire (NSW Southern Highlands): The fire started on 27 November 2019 and burned through 279,000 hectares across the Blue Mountains, Wingecarribee, Wollondilly and Upper Lachlan local government areas, as well as areas around the Sydney water catchment including Oakdale, Orangeville and Werombi adjacent to Lake Burragorang. The fire was contained on 30 January 2020 and extinguished on 7 February 2020.
- The Currowan bushfire (Shoalhaven/South Coast): The fire started on 26 November 2019 and burned through 499,000 hectares including around Shoalhaven and the NSW South Coast. These areas were among the most severely impacted in the network. The fire was contained on 9 February 2020.

Endeavour Energy submitted it expects to incur \$31.3 million (\$2019–20) in additional costs as a result of the bushfires (\$25.2 million (\$2019–20) of operating expenditure and \$6.1 million (\$2019–20) of capital expenditure). Endeavour Energy states this amount consists of \$15.1 million (\$2019–20) of additional costs incurred in 2019–20, the year of the bushfires, and \$16.1 million (\$2019–20) in forecast additional costs it expects to incur over the final four years of the current regulatory control period (FY 2020–21, 2021–22, 2022–23 and 2023–24).¹³

The revenue impact of the proposed pass through amount is \$31.1 million (\$nominal, smoothed) over the final three years of the current regulatory control period (that is, in FYs 2021–22, 2022–23 and 2023–24).¹⁴

¹² Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, pp. 11, 29, 35.

¹³ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 29. Numbers may not add up to totals due to rounding.

¹⁴ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 47.

2.3. Structure of this document

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

The decision is structured as follows:

- Section 3 sets out our determination on Endeavour Energy's cost pass through application
- Section 4 sets out our assessment of the proposed positive pass through amount
- Section 5 sets out our assessment of the proposed recovery period of the positive pass through amount
- Section 6 sets out our assessment of Endeavour Energy's cost pass through application against the NER requirements, including whether the materiality threshold is met, and consideration of stakeholder submissions.

3. Our determination

Having taken into account all the matters set out in this decision, we determine that 2019–20 bushfires which caused damage to Endeavour Energy’s distribution network constitute a positive change event. Our assessment against the requirements of a positive change event is summarised in Table 1 (contained below in section 6).

Our determination is to approve a total positive pass through amount of \$26.7 million (\$2019–20).¹⁵ In making our determination, we have taken into account the time cost of money based on the allowed rate of return for Endeavour Energy for the regulatory control period in which the pass through event occurred.¹⁶ The resulting revenue impact totals \$25.8 million (\$ nominal, smoothed) for the 2019–24 regulatory control period to be recovered over the following three regulatory years accordingly:

- \$8.4 million (\$nominal) to be recovered in 2021–22
- \$8.6 million (\$nominal) to be recovered in 2022–23, and
- \$8.8 million (\$nominal) to be recovered in 2023–24.

Our assessment of the positive pass through amount is set out in sections 4 and 5, and Table 2 (contained below in section 6).

¹⁵ This is \$26.6 million in 2018-19 dollar terms as per the AER pass through final decision PTRM.

¹⁶ This is discussed further in table 2.

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,¹⁷ including the need to ensure that Endeavour Energy 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,¹⁸ and that Endeavour Energy does not recover costs that have or will be factored into Endeavour Energy's annual revenue requirement.¹⁹

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

- the pass through amount reflects only those costs incurred as a result of the bushfire event and not business-as-usual costs or costs of increasing the scope of network services provided by Endeavour Energy;
- the costs incurred are the lowest possible to rectify the damage caused by the bushfires (that is, to restore network service to the pre-bushfire levels); and
- the pass through amount reflects only the incremental cost of the bushfires, taking into account deductions for actual and expected cost savings that will occur as a result of works undertaken to address the bushfires. For example, the replacement of older assets damaged by the bushfires with new assets may result in lower future inspection and maintenance costs, which should be deducted from the costs to be passed through.

We are satisfied that Endeavour Energy's estimates of the increase in opex and capex costs due to the bushfires, less the proposed herbicide spraying costs, are efficient. The subsections below set out our assessment of the efficiency of the pass through amount.

Herbicide spraying program

Endeavour Energy proposed \$7.8 million (\$2019–20)²⁰ for a herbicide spraying program to address vegetation growth within network clearances in bushfire impacted work spans. We have not accepted this cost for the reasons provided below.

Endeavour Energy states that the herbicide spraying is to be undertaken on land within its network easements after the areas have been cleared of post-fire remnant vegetation. The herbicide spraying is planned to occur in FY 2020–21 and in each of the following three financial years 2021–22, 2022–23 and 2023–24. The aim of the spraying is to prevent new tree growth within the freshly cleared easements to limit future vegetation management work and the costs that would typically be incurred in future regulatory periods as seeds germinate and new trees grow after the bushfires.

Endeavour Energy states that the proposed herbicide spraying is a new, lower cost approach to meeting its future vegetation management requirements, compared to its business as usual approach of mechanical slashing and tree trimming, as it allows the

¹⁷ Clause 6.6.1(j) of the Rules.

¹⁸ Clause 6.6.1(j)(5) of the Rules.

¹⁹ Clause 6.6.1(j)(7) of the Rules.

²⁰ Endeavour Energy, Endeavour Energy - Bushfire cost pass through - cost detail – Public, November 2020.

business to use the opportunity presented by the bushfire to spray the freshly cleared easements, prevent new tree growth, and avoid these future business as usual costs.²¹

A decision by Endeavour Energy to change its approach to vegetation management by implementing the proposed herbicide spraying program is a matter that is within Endeavour Energy's control. We do not consider that this change is necessary to rectify the damage caused by the bushfires and restore network services to pre-bushfire levels.

As such, we do not consider that the costs of the proposed herbicide spraying program can be recovered as part of this pass through application.

We consider the costs recoverable through a pass through are limited to those that are entailed by the event – that is, the costs that are necessary to put the business in a like position to what it was in prior to the event,²² and do not include costs associated with adopting a new or changed approach after the event. This reflects the objective of the pass through rules, which is to “provide a degree of protection for [a network service provider] from the impact of unexpected changes in costs outside of its control”.²³ As the change in approach to vegetation management is not necessary to rectify the damage caused by the bushfires or to restore network services to pre-bushfire levels of service, we do not consider it an efficient response to the bushfires.

We note that if Endeavour Energy wishes to continue to carry out the herbicide spraying program in the current regulatory control period, it can choose to fund the activity itself or through its current revenue allowance. If the program proves effective, it may result in cost reductions for vegetation management in future regulatory periods.

In response to AER information requests, Endeavour Energy provided additional information on its cost pass through application stating that the planned herbicide spraying work was estimated to achieve \$2.5 million (\$2019-20) in savings to business-as-usual vegetation management costs in the current regulatory control period. This is based on the assumption that in the absence of herbicide spraying, by FY24 70% of the impacted spans will return to BAU cutting and slashing costs.²⁴ In addition, Endeavour Energy stated that it would not be able to achieve a \$0.62m (\$2019-20) ‘unscoped efficiency adjustment’ saving included in its original cost pass through application if the herbicide spraying program was not undertaken. Endeavour Energy also included a minor adjustment to its estimate of BAU vegetation management costs to reflect that it has been undertaking some limited herbicide spraying as part of its BAU vegetation management practises.

We consider that the lower updated estimate of savings to business-as-usual costs and the removal of the efficiency adjustment saving is reasonable in the absence of the herbicide spraying program. As we are not allowing the costs of the proposed herbicide spraying

²¹ Endeavour Energy, Endeavour Energy - Bushfire CPT Information Request Response - October 2020 – Public, October 2020, pp. 21-22.

²² See for example, the definition of “positive change event”. We also note sub-clause 6.6.1(j)(8) requires the AER, in making a pass through determination, to take into account any factors it considers relevant.

²³ See AEMC, Rule Determination – National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 No.18, 16 November 2006, p. 104, <https://www.aemc.gov.au/sites/default/files/content/14c81a96-dd77-4530-9d6b-2c55ebe889c3/Rule-Determination.pdf>.

²⁴ Endeavour Energy, Endeavour Energy – Response 161220, December 2020, pp. 3-4; Endeavour Energy, Endeavour Energy - Bushfire cost pass through - cost detail - 161220 Update - Public, December 2020.

program to be recovered in this decision, we have used the updated, lower estimate of savings to business-as-usual vegetation management costs and not included the efficiency adjustment in calculating the pass through amount. The net reduction in the pass through amount from rejecting the herbicide spraying program and accounting for the above items is \$4.6m (\$2019-20).

Emergency response costs

Endeavour Energy's pass through application includes \$3.3 million (\$2019–20) in incremental bushfire-related emergency response costs. Endeavour Energy stated in its proposal that these costs were incremental emergency response costs and not BAU costs already factored into Endeavour Energy's annual revenue requirement because the 2017–18 base year used to set its current maximum revenue allowance did not include emergency response costs related to bushfires.²⁵

We do not consider it reasonable to disaggregate emergency response costs or allowances by the type of emergency. Under the NER, the distributor is required (and funded) to provide standard control services, which includes responding to interruptions to supply, irrespective of the cause of the interruptions.²⁶

We sought clarification from Endeavour Energy on the incremental nature of the emergency response costs. Endeavour Energy explained that these costs were in addition to business as usual emergency response activities and were incurred in response to the bushfire event. In support, Endeavour Energy provided transactional level data to demonstrate the build-up of these costs and the processes and controls in place to ensure that only incremental costs were captured. Based on the supplied information, we are satisfied that no BAU emergency response costs were captured.

Costs reflect only bushfire-related costs and not business-as-usual costs

We are satisfied that the costs Endeavour Energy has incurred and is likely to incur, less herbicide costs, are costs it has incurred or is likely to incur as a result of the bushfires, and that these costs have been demonstrated to be incremental costs separate to the business as usual costs of operating the distribution network.

Endeavour Energy described the process it used for isolating the bushfire-related costs it incurred from its business as usual costs:²⁷

Bushfire event costs were recorded using our accounting system (Ellipse) consistent with our BAU processes. These processes allow costs (recorded from timesheet entries, Endeavour Energy stores requisitions, supplier invoices and corporate cards) to be booked to either a work order or account code.

Endeavour Energy raised four parent work orders to link any work orders raised so we could capture bushfire related costs.

²⁵ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 37.

²⁶ Clause 5.2.3(e1)(4) of the Rules.

²⁷ Endeavour Energy, Endeavour Energy - Bushfire CPT Information Request Response - October 2020 – Public, October 2020, pp. 3-4

During the bushfire response Endeavour Energy staff booked labour, vehicle costings and expenses such as contractors, materials, fuel, plant & equipment hire across a total of 271 work orders over 42 organisation units. The 271 work orders were raised specifically to capture bushfire recovery costs and help distinguish these costs from business as usual costs.

Supplier invoices for bushfire related services were loaded into Ellipse as “Unapproved” and directed to the relevant Manager. Managers were required to: review the invoice; check the amounts; and ensure that they cost the invoice to the correct bushfire recovery work order(s) prior to approving the invoice payment.

We are satisfied that the processes, controls and documentation Endeavour Energy used to identify bushfire-related costs show that only incremental costs were captured and these costs relate only to activities that would be expected to occur following a bushfire event. That is, the costs relate to restoring supply and returning to pre-existing levels of reliability, and not to:

- the ordinary provision of network services in non-bushfire-affected areas, or
- the ordinary provision of network services in bushfire affected areas after rectification of the bushfire damage, or
- expanding the scope of the network or network services.

The level of bushfire-related costs is lowest possible to maintain service levels

We have examined the scope of actions and works Endeavour Energy has undertaken and planned in response to the bushfire event. We considered the necessity of the actions and works and their cost, and compared this to industry standards and costs. We are satisfied that the level of costs Endeavour Energy has incurred and the estimates of costs it expects to incur as a result of the bushfires (other than in respect of the herbicide spraying program) reflect efficient costs.

Adjustments for savings to business-as-usual costs resulting from the bushfire expenditure

We are satisfied that Endeavour Energy’s pass through amount reflects deductions for an efficient level of partially-offsetting savings that are expected to occur as a result of works undertaken by Endeavour Energy to repair its network.

In estimating its proposed pass through amount, Endeavour Energy estimated the amount of business-as-usual costs that would be avoided over the current regulatory control period as a result of its works to rectify bushfire damage. These included some future vegetation management, asset inspection, pole replacement works and ordinary time labour costs that can be avoided or deferred.

Endeavour Energy’s estimate was based on condition based indicators, extent of works avoided as a result of the bushfire tree rectification programs, and forecasts of activity rates

(such as vegetation management cycles, inspection cycles, and replacement rates of inspected assets), and unit costs following the bushfires.²⁸

We are satisfied that Endeavour Energy's forecasts of activity rates and unit costs used in estimating its proposed pass through amount are efficient and align with industry standards. As a result, we are satisfied that Endeavour Energy's method for estimating expected cost savings results in appropriate estimates of savings for asset inspections, asset replacements and vegetation management.

²⁸ Endeavour Energy, Endeavour Energy - Bushfire CPT Information Request Response - October 2020 – Public, October 2020, p. 17; Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, pp. 38-41.

5. Timing for recovery of the cost pass through from end users

Endeavour Energy proposed the pass through amount be recovered from end users over the final three years of the current regulatory control period commencing from 2021–22 (FYs 2021–22, 2022–23 and 2023–24).

Endeavour Energy noted the preference of their customers for low and stable electricity prices. Accordingly, it has sought to smooth the revenue impact of the eligible pass through amount in a manner that will allow it to continue delivering real price reductions for customers.²⁹

We approve Endeavour Energy's proposal to recover the pass through amount in the remaining three years of the current regulatory control period commencing from 2021–22. We consider that smoothing the recovery of the pass through amount over a three year period will limit the impact on prices paid by end users.

²⁹ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 14.

6. 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. Endeavour Energy can then submit a pass through application, which must address certain matters specified in the NER (see Table 1 and Table 2). We make a determination on Endeavour Energy's pass through application and determine the approved pass through amount and the regulatory years in which that pass through amount is to be recovered. For the reasons set out in Table 1 below, we are satisfied that a positive change event has occurred, and that Endeavour Energy's pass through application specifies all the matters required by the NER.

In making our determination on Endeavour Energy's approved pass through amount, we must take into account certain matters specified in the NER (see Table 2). In assessing a natural disaster pass through application, we will also have regard to certain matters set out in Endeavour Energy's distribution determination. Additionally, we have also taken into account the two stakeholder submissions received on Endeavour Energy's cost pass through application. Our consideration of these matters are set out in Table 2 below. After having regard to all of the matters in Table 2 below and throughout this decision, we make the determination set out in section 3 above.

Table 1 Requirements for determining a positive change event has occurred

#	Requirement of the NER	Our consideration
1.	Is the pass through event a regulatory change event, service standard event, tax change event, or retailer insolvency event? ³⁰	No
2.	Is the pass through event a contingent project or a trigger event associated with a contingent project? ³¹	No
3.	Does the pass through relate to any other event specified in Endeavour Energy's 2019-24 distribution determination as a pass through event for that determination? ³²	Yes. We consider that the bushfires satisfy the natural disaster pass through event specified in Endeavour Energy's determination, which is defined as including fire, flood, or earthquake, provided the event was not a consequence of the acts or omissions of Endeavour Energy. ³³
4.	Was the pass through event a consequence of acts or omissions of Endeavour Energy? ³⁴	No, there is no evidence that Endeavour Energy's acts or omissions caused the bushfires. ³⁵

³⁰ Cl. 6.6.1(a1)(1) through 6.6.1(a1)(4) of the Rules; and chapter 10 of the Rules.

³¹ See the definition of "positive change event" in chapter 10 of the Rules.

³² Cl. 6.6.1(a1)(5) of the Rules.

³³ AER, Final Decision: Endeavour Energy 2015-16 to 2018-19 Distribution Determination – Attachment 15 – Pass Through Events, April 2015, pp. 7-8.

³⁴ AER, Final Decision: Endeavour Energy 2015-16 to 2018-19 Distribution Determination – Attachment 15 – Pass Through Events, April 2015, pp. 7-8.

³⁵ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 47.

5. **Did the bushfire pass through event entail Endeavour Energy incurring materially higher costs in providing direct control services than it would have incurred but for the event?**³⁶

Yes. Endeavour Energy provided us with Ellipse extracts detailing the actual incurred increase in costs, and forecast increases in costs based on these actual costs and a forecasting methodology.

The NER defines a material change in costs³⁷ as a change in costs (as opposed to the revenue impact) that a DNSP has incurred and is likely to incur in any regulatory year of a regulatory control period, as a result of that event, that exceeds 1% of the annual revenue requirement for that regulatory year. Endeavour Energy's annual revenue requirement was \$555.9 million (\$2018-19) for 2019-20 and \$846.3 million (\$2018-19) for 2020-21,³⁸ with 1% of these revenue requirements being \$5.6 million (\$2018-19) and \$8.5 (\$2018-19), respectively. We consider that the efficient amount of opex and capex incurred as a result of the bushfires in 2019-20 is \$15.1 million (\$2018-19) and in 2020-21 is \$15.3 million (\$2018-19). Therefore, the costs incurred in providing direct control services as a result of the event exceed the materiality threshold in both years.

6. **Does the pass through application relate to one event or multiple events?**

Endeavour Energy submitted that the 2019-20 bushfires constituted a single natural disaster event that impacted its network in three operational areas. We agree.

We consider that multiple bushfires are capable of being considered a single natural disaster if they are sufficiently related and have the same underlying causes. If they occurred relatively closely in both time and/or geographic proximity, we consider this may also support treating them together.

We are satisfied that the bushfires that caused damage to Endeavour Energy's network all had the same underlying cause. Namely, ignition by dry lightning fuelled by high temperatures and strong winds that led to their rapid expansion. In addition, the bushfires occurred over the same period of time and were burning at the same time. Figure 1 and table 1 in Endeavour Energy's pass through application show the geographic proximity of the bushfires.³⁹ We note that the bushfires impacted communities to such an extent that they are recognised collectively as the NSW bushfires with the NSW Government declaring a State of Emergency across the entire state and the event obtaining formal natural disaster status in NSW.⁴⁰

Endeavour Energy stated in its pass through application that two storm events in February 2020 caused \$2.1 million (\$2019-20) in damage to the electricity network. Endeavour Energy states that while it has funded these costs from its current revenue allowance rather than included them in the pass through, the same conditions and trends that were responsible for the 2019-20 bushfire event also contributed to the February storms.

While not necessary for the purposes of this determination, we note that the relevant storms and bushfires are unlikely to constitute the same natural disaster.

7. **What is the date on which the positive change event occurred?**

The bushfire event is associated with bushfires that first started on 26 October 2019 and that were progressively brought under control and extinguished in February 2020. For the purposes of complying with 6.6.1(c)(2) of the NER, Endeavour Energy nominated the final day of the statutory bushfire season in NSW - 31 March 2020 - as the effective date.

However, we consider 9 February 2020 to be the date on which the positive change event occurred. This is the date the final bushfire that

³⁶ That is, does it meet the definition of a "positive change event" as defined in chapter 10 of the Rules.

³⁷ For the purposes of a cost pass through.

³⁸ AER, Post-tax revenue model – 2020-21 return on debt update, March 2020.

³⁹ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, pp. 12-13.

⁴⁰ Endeavour Energy, Cost pass through application – 2019-20 Bushfire disaster event, August 2020, p. 8.

caused damage to Endeavour Energy's network was brought under control.⁴¹

<p>8. Did Endeavour Energy submit a written statement of its pass through application within 90 business days of the positive change event occurring?⁴²</p>	<p>Endeavour Energy submitted its application within the relevant timeframe.</p> <p>We note that on 9 April 2020, Endeavour Energy submitted a request to the AER under clause 6.6.1(k) of the NER for an extension to submit its cost pass through application. It claimed that due to the scale and impact of the damage to its network it was not possible to submit an application with the degree of certainty of the cost associated with the event to enable a proper consideration of a pass-through application by the AER, within the 90-business day timeframe.</p> <p>The AER extended the timeframe in which Endeavour Energy had to submit the cost pass through application until 31 August 2020 on the basis that it was satisfied the difficulty of assessing or quantifying the effect of the relevant pass through event justified the extension.</p> <p>Endeavour Energy subsequently submitted its written statement on 31 August 2020.</p>
<p>9. Did Endeavour Energy specify details of the positive change event, including the date on which the event occurred, in its written statement?⁴³</p>	<p>Yes. Endeavour Energy's written statement is available on our website.⁴⁴</p>
<p>10. Did Endeavour Energy 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?⁴⁵</p>	<p>Yes. Endeavour Energy proposed an eligible, positive pass through amount of \$31.3 million (\$2019–20). It proposed a total of \$31.1 million (\$ nominal) to be recovered from customers in the final three years of the current regulatory control period (2021-22, 2022-23 and 2023-24).</p>
<p>11. Did Endeavour Energy specify in its written statement evidence of the actual and likely increase in costs that occurred solely as a consequence of the positive change event?⁴⁶</p>	<p>Yes. Endeavour Energy's pass through application (that is, its written statement) set out the costs it incurred and forecast to incur as a result of the bushfires, as well as how it calculated its proposed pass through amount.⁴⁷ However, we considered that a more detailed breakdown was required. In response to our information requests Endeavour Energy provided further information detailing all costs, adjustments, working and assumptions used to derive the incremental cost increase.⁴⁸</p>
<p>12. Was there a regulatory information instrument applicable to the pass through application?⁴⁹</p>	<p>No.</p>

⁴¹ NSW Rural Fire Service, Media Release - Fire season comes to a close in NSW, 31 March 2020, https://www.rfs.nsw.gov.au/__data/assets/pdf_file/0003/171921/200331-End-of-season-20.pdf

⁴² Cl. 6.6.1(c) of the Rules.

⁴³ Cl. 6.6.1(c)(1) and 6.6.1(c)(2) of the Rules.

⁴⁴ <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/cost-pass-throughs/endeavour-energy-cost-pass-through-2019-20-bushfire-natural-disaster/initiation>

⁴⁵ Cl. 6.6.1(c)(3), 6.6.1(c)(4), and 6.6.1(c)(5) of the Rules.

⁴⁶ Cl. 6.6.1(c)(6) of the Rules.

⁴⁷ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, pp. 29-30.

⁴⁸ Endeavour Energy, build up of costs spreadsheet, Endeavour Energy - IR01 Consolidated PTE costs - October 2020 – Public, October 2020.

⁴⁹ Cl. 6.6.1(c)(7) of the Rules.

13. Is the pass through amount, in whole or in part, in respect of expenditure for a restricted asset?⁵⁰ No.⁵¹

Table 2 Relevant matters the AER must take into account to determine the pass through amount

#	Requirement of the NER	Our consideration
15.	In making the pass through determination we must take into account the matters and proposals set out in Endeavour Energy's written statement. ⁵²	This decision sets out how we have taken into account the matters and proposals set out in Endeavour Energy's pass through application (written statement).
16.	We must take into account the increase in costs in providing direct control services resulting from the pass through event ⁵³	<p>In making the pass through determination we must take into account the increase in costs in the provision of direct control services that, as a result of the positive change event, Endeavour Energy incurred and is likely to incur until the end of the regulatory control period in which the positive change event occurred.</p> <p>In section 4 above we set out our assessment of the costs incurred by Endeavour Energy as a consequence of the bushfires. We consider the costs incurred as well as partially-offsetting savings to future costs that we expect to occur as a result of works undertaken by Endeavour Energy to repair its network.</p> <p>Endeavour Energy deducted cost savings that it forecast to achieve up to the end of its 2019–24 regulatory period.</p>
17.	We must take into account the efficiency of Endeavour Energy's decisions and actions in relation to the risk of the event ⁵⁴	<p>In making the pass through determination we must take into account the efficiency of Endeavour Energy's decisions and actions in relation to the risk of the positive change event, including whether Endeavour Energy 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 consider that Endeavour Energy's decisions and actions in relation to the risk of the positive change event were inefficient. We do not consider that Endeavour Energy's actions increased the magnitude of the amount.</p>
18.	We must take into account the time cost of money	<p>In making the pass through determination we must take into account the time cost of money based on the allowed rate of return for Endeavour Energy for the regulatory control period in which the pass through event occurred.⁵⁵</p> <p>The AER uses the forecast inflation rate as determined at the April 2019 final decision for Endeavour to calculate the figures in nominal terms for each year of the 2019–24 regulatory period.</p> <p>While we have not accepted Endeavour Energy's entire pass through amount, we do accept recovering the revised pass through amount of \$26.7 million (\$2019-20). The resulting revenue impact totals \$25.8</p>

⁵⁰ Cl. 6.6.1(c1) and (d2) of the Rules.

⁵¹ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 42.

⁵² Cl. 6.6.1(j)(1) of the Rules.

⁵³ Cl. 6.6.1(j)(2) of the Rules.

⁵⁴ Cl. 6.6.1(j)(3) of the Rules.

⁵⁵ Cl. 6.6.1(j)(4) of the Rules.

		million (\$ nominal, smoothed) which will be recovered in the remaining three years of the current regulatory period.
19.	We must take into account the need to ensure that the pass through amount reflects only costs incurred solely as a consequence of the bushfires	<p>In making the pass through determination we ensure that Endeavour Energy only recovers any actual or likely increment in costs to the extent that such increment is solely as a consequence of the pass through event.⁵⁶</p> <p>In section 4 above we set out our assessment of the costs incurred by Endeavour Energy as a consequence of the bushfires. We are satisfied that Endeavour Energy's proposed pass through amount, less herbicide spraying costs, reflects only those costs incurred solely as a consequence of the bushfires.</p>
20.	The AER will have regard to whether Endeavour Energy has insurance against the event, and whether it is the level of insurance that an efficient and prudent network operator would obtain?⁵⁷	<p>Endeavour Energy did not have insurance covering the bushfires. Endeavour Energy submitted that its decision not to insure its 'poles and wires' reflects the unavailability of such coverage in the insurance market and other complexities around attempting to insure the risk.⁵⁸ We note that this approach to managing this risk is generally consistent with comparable peer NEM networks including those also impacted by the 2019–20 bushfires. As such, we are satisfied that it was prudent and efficient for Endeavour Energy to not obtain bushfire insurance cover for its 'poles and wires' assets.</p>
21.	We must take into account costs already funded by customers through our five-yearly regulatory determinations	<p>The National Electricity Rules provide that we must take into account whether the costs of the bushfires have already been factored into the calculation of the Endeavour Energy's annual revenue requirement for its 2019–24 regulatory control period.⁵⁹</p> <p>We provided revenue allowances in Endeavour Energy's 2019–24 distribution determination to fund Endeavour Energy to inspect, maintain, and replace some of its assets. However, the bushfires resulted in the need for an additional, increased level of inspections, maintenance, and replacement above the levels forecast in our determination.</p> <p>Costs incurred as a result of bushfires or other natural disasters can be funded through our regulatory determinations by providing allowances for self-insurance provisions. However, we did not provide allowance for self-insurance provisions in Endeavour Energy's 2019-24 distribution determination.</p> <p>After excluding the proposed herbicide spraying costs, we are satisfied that Endeavour Energy has accurately recorded the additional costs incurred as a result of the bushfires (see section 4).</p> <p>As well as causing additional costs, there may be partially-offsetting savings that are expected to occur as a result of works undertaken by Endeavour Energy to repair its network. Therefore, some portion of the additional costs incurred as a result of the bushfires can be considered to have already been funded through cost savings in other areas, for which revenue allowances were provided in our 2019–24 determination.</p> <p>Endeavour Energy did deduct a number of cost savings that it forecast to achieve following works undertaken to repair its network. We are satisfied that Endeavour Energy appropriately forecast these cost savings.</p>
22.	We must take into account the extent to which Endeavour Energy's costs have already been	There are no relevant previous pass through determinations.

⁵⁶ Cl. 6.6.1(j)(5) of the Rules.

⁵⁷ AER, Final Decision: Endeavour Energy 2019-24 Distribution Determination – Overview, April 2019, p. 44.

⁵⁸ Endeavour Energy, Cost pass through application – 2019-20 bushfire disaster event, August 2020, p. 20.

⁵⁹ Cl. 6.6.1(j)(7) of the Rules.

23.

We must take into account any other factors that we consider relevant

Stakeholder submissions

We published Endeavour Energy's pass through application on our website and sought submissions from interested stakeholders. We received submissions from the Public Interest Advocacy Centre (PIAC) and Red Energy. We have considered the issues raised in submissions in making this decision.

PIAC raised concerns with the rationale used to explain the incremental basis of emergency response costs, and called for a review to consider how to better incorporate extreme weather events costs into the risk allocation and cost recovery frameworks of the NEM.

We sought clarification from Endeavour Energy on the basis of the incremental nature of the emergency response costs. Endeavour Energy provided additional information demonstrating that these costs were not BAU emergency response costs (see section 4). We note that, whilst the proposed review is outside the scope of this specific pass through decision, such matters are the subject of further and ongoing consideration by policy and rule makers.

Red Energy encouraged the AER to protect consumers from paying for insurance losses that an efficient and prudent network should have obtained in advance. It also considered that the pass through should not be recovered in the current regulatory period to ensure it will be included in next Default Market Offer (DMO).

We note that the DMO offer for the first full regulatory year following this determination (i.e. FY 2021-22) will take the change in network revenues due to this decision into account.

Additional information

We issued an information notice to Endeavour Energy under clause 6.6.1(e1) of the National Electricity Rules seeking further information on how Endeavour Energy estimated its proposed pass through amount. We received information in response to this notice on 22 October 2020. Endeavour Energy also provided some additional information on how they estimated their proposed pass through amount on 11 November 2020. We have taken this information into account in our assessment of the efficiency of the positive pass through amount (see section 3 above).

Decision-making timeframe

On the basis that this decision involved issues of such complexity or difficulty that the timeframe in which the AER has to make its decision should be extended, the AER extended the due date for its decision by 60 business days under sub-clause 6.6.1(k1) to 16 March 2021.

⁶⁰ Cl. 6.6.1(j)(7A) of the Rules.