Ref: C2133207

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Mr Chris Pattas
General Manager
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Email: AERInquiry@aer.gov.au

Dear Chris

Proposed amendment to the Service Target Performance Incentive Scheme

Essential Energy welcomes the opportunity to provide feedback on the proposed amendment to the Service Target Performance Incentive Scheme (STPIS).

We believe that many of the proposed amendments will enhance the operation of the STPIS. Specifically, the following outcomes are welcomed:

- Exclusions for load interruptions caused by obligations under jurisdictional legislation or National Electricity Law, a direction from emergency services or a failure of transmission connection assets that were not the fault of the distributor;
- Adjusting the targets where the rewards or penalty exceed the revenue cap under the STPIS;
- The alignment with other changes proposed for the distribution reliability measures guideline;
- The continued symmetrical operation of the financial incentive scheme;
- The continuation of the current level of flexibility in linking distributor's customer engagement findings to the setting of reliability levels; and
- The inclusion of supply interruptions associated with unexpected performance of demand management projects in the STPIS.

However, we do have continued concerns in two areas. These are discussed below.

The proposed change in the ratio of SAIDI/SAIFI incentives from 50/50 to 60/40

One-off amounts of capital expenditure can generally improve SAIFI, whereas ongoing operating expenditure (generally labour costs) is required to make and maintain SAIDI improvements. Although the STPIS provides a short-term incentive for distributors to invest in ongoing operating expenditure for reliability improvements, there is uncertainty as to how the AER will deem the efficiency of this operating expenditure in future regulatory determinations. This is particularly the case under the current deterministic approach to setting operating expenditure levels. As a result, the current scheme does, unintentionally, favour one-off investments over on-going operating expenditure investment.

To improve investment certainty and rebalance distributor investment between SAIFI and SAIDI, we would suggest that the AER need only clarify how it will translate SAIDI related on-going operating expenditure investments under the scheme into its operating expenditure benchmarking. Removing this uncertainty would alleviate the concerns of distributors and correct the balance of the incentive scheme.

In addition, the proposed change in the ratio may create new distortions:

- It favours higher density, predominately underground networks over dispersed, overhead networks as the increased SAIDI weighting is greatly impacted by weather;

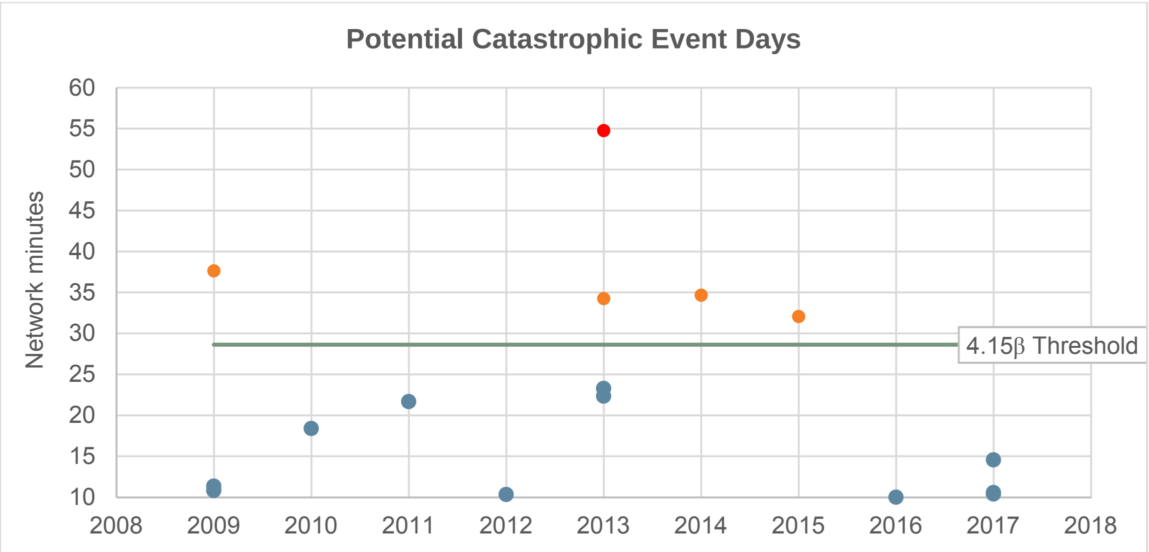
> It assumes that customers value SAIDI more than SAIFI. Our recent customer engagement undertaken as part of our upcoming determination has found that the majority of our customers are happy with reliability levels and are not willing to pay more to reduce the duration (SAIDI) of unplanned outages. The current approach of using CAIDI to apportion the incentive, along with equal allocation of unserved energy between SAIDI and SAIFI acts to best reflect the average restoration time experienced by customers and ensure that distributors are not penalised for responding to their customer's preferences.

Exclusions and treatment of major event days

Essential Energy welcomes the AER working to develop a clear method for the identification of catastrophic event days. However, in the absence of such a method, Essential Energy does not believe it is appropriate for the AEMC's recommendation of the adoption of a catastrophic event day to go unimplemented.

In the interim the AER should adopt either the IEEE 4.15 beta method, another heuristic method or simply a subjective graphical assessment of past daily network SAIDI values, to determine a register of past catastrophic event days for each specific network - recognising that these events, by definition, should be rare.

To assist, the figure below shows the last nine years of potential catastrophic event days for Essential Energy. Depending on the approach taken either five days in nine years would be classified under 4.15β threshold (all orange and red points) or a subjective assessment may consider only one catastrophic event day occurred. Whatever the approach, these five days do impact the daily SAIDI distribution, as they range from 6.5 times to 11 times the threshold for a major event day.



Should you have any questions regarding our submission, please don't hesitate to contact Natalie Lindsay, Manager Network Regulation, on (02) 6589 8419.

Yours sincerely

Chantelle Bramley

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