SP AusNet™
A member of Singapore Power Group

14 May 2008

Mr Chris Pattas,
General Manager,
Network Regulation South Branch,
Australian Energy Regulator
Melbourne Vic 3001.

Dear Chris,

Electricity Distribution Guidelines, Models and Schemes

SP AusNet welcomes the opportunity to comment on the guidelines, models and schemes for electricity distribution network service providers released for comment in April 2008 by the Australian Energy Regulator (AER).

SP AusNet recognises that there are many challenges facing the AER arising from assuming economic regulatory functions for electricity distribution networks. Based on past jurisdictional regulatory practices the networks bring with them a range of different quality and regulatory arrangements.

Planned interruptions

SP AusNet considers that it is important that the AER strives to maintain and improve on the current best regulatory practice in distribution regulation. SP AusNet considers that the Essential Services Commission, Victoria (ESC) determination for the Electricity Distribution Review 2006 -2010 set a high standard in many respects. The S-factor scheme and the improvements made to the scheme documented in the Final Decision should be maintained until further improvements are identified. In that decision the ESC stated that: [1]

> *"Given the concerns raised that an incentive on planned SAIDA may create a tension with safe work practices and evidence that customers value a reduction in unplanned interruptions rather than planned interruptions (KPMG 2003), the Commission's decision is that planned SAIDI should not be included in the S-factor scheme but that unplanned SAIDI should be included as a separate measure."*

[1] EDPR Final Decision Page 81

SP AusNet considers the ESC was correct in it decision on the treatment of planned outages with regard to the S-factor scheme. SP AusNet considers the AER's proposal to revert to the original ESC arrangement, for the S-factor scheme with regard to planned outages, to be a retrograde step, and therefore disagrees with the proposed approach of treating planned interruptions in the same way as unplanned interruptions for the purpose of the incentive scheme.

Including planned interruptions within the service target performance incentive scheme is inconsistent with maximising incentives to maintain the network and there are potential negative incentives concerning the safety of operators working on the network that are unnecessarily encouraged if the AER's proposal is implemented. As noted above, these considerations recently led to the approach currently proposed by the AER, that was in force during the EDPR 2001 – 2005 in Victoria, being reversed as these issues were recognised by both distributors and the ESC.

The approach is also economically unsound as it presumes that customers are indifferent between planned outages (fixed time interruptions occurring with notice) and unplanned outages, which are by their nature episodic and of varying durations. SP AusNet considers this presumption is incorrect, as it is inconsistent with customers' capacity to avoid or shift at least elements of their electricity usage in response to advice of planned outages.

In addition, the type of behaviour a service standard scheme would want to incentivise would be different for planned and unplanned outages with implications for the magnitude of the appropriate incentive.

For planned outages, it is generally operational behaviour that is the target of the incentive, that is, planning, scheduling, work practices etc. The planned outage (availability) incentives in place for transmission businesses are of this nature and are not intended to incentivise investment in the transmission system. Therefore, the appropriate incentive is low powered and small in magnitude (as a share in revenue).

However, for unplanned outages, it is substantial operating and capital expenditure behaviour that is being incentivised. That is, informed by a willingness to pay assessment, the incentive is large enough to fully fund large expenditure programs. As such, the incentive is uncapped and, therefore, has the capacity to be very large relative to the appropriate incentives for planned outages.

Proposed cap on revenue at risk

The AER proposes a cap of three per cent of revenue at risk under the S-factor scheme, but will provide distributors with the opportunity to differentiate arrangements applying to their networks. SP AusNet has a number of queries on the proposed operation of the cap on the scheme, including:

- the empirical rationale for a discretionary decision to impose a 3 per cent cap;
- the definition of revenue to be used in the 3 per cent cap at risk;

- whether underperformance or over performance outside of the cap are subject to being carrying forward; and
- how any perverse incentives introduced by a cap will be mitigated?

SP AusNet does not understand how a cap can be introduced onto the S-factor scheme without degrading the incentive properties of the scheme, a scheme that is intended to hold electricity DBs accountable for meeting reliability obligations and reward improved reliability performance.

SP AusNet considers that the introduction of a cap will unnecessarily conflict with the working of the S-factor scheme.

Scope of exclusions

SP AusNet considers the available exclusions to be insufficient, exclusions should be expanded to include at least: directions from emergency service personnel, NEMMCO and automatic under-frequency load shedding.

An additional issue which the rules on exclusions should accommodate is that eligibility of events should be assessed on a rolling 24-hour period, from the commencement of the event, rather than a midnight to midnight assessment. This avoids the impact timing has, during the midnight to midnight period, of extreme weather events, for example, arbitrarily affecting eligibility for exclusion, and consequently the overall risk profile of revenues.

If you have any queries about our response, please contact me on 9695 6623.

Yours sincerely

Patrick Murphy
MANAGER, ECONOMIC REGULATION