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John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Via website: www.aemc.gov.au

Project Number: EPR0031

Dear Mr Pierce,

Review of Distribution Reliability Outcomes and Standards: Draft Report

We welcome the opportunity to respond to the AEMC's Draft Report on the National Workstream 'Review of distribution reliability outcomes and standards'. SP AusNet supports a level of consistency in the national framework for reliability to the extent that this is beneficial to the National Electricity Objective. Our detailed response is attached.

There are many aspects of the Draft framework that SP AusNet supports, including: the establishment of transparent guidelines; a focus on capturing better information on customer preferences and the value of customer reliability; the acceptance of an 'output based' reliability framework; and, the adoption of consistent reliability measures to allow benchmarking.

However, SP AusNet does not support the Draft Framework in its current form. While the AEMC's intent has been to provide flexibility to allow differences in the application of the reliability framework across jurisdictions, the Draft framework imposes an approach that is inconsistent with the use of incentives to drive reliability outcomes. By imposing a target setting process, and one which is prescriptive and resource intensive, administrative burden is increased while the incentive driver for 'least cost' reliability improvement is lost. As such the approach is likely to raise the cost to Victorian customers, without compensating benefits.

We look forward to continued participation in the development of a national reliability framework. Please contact Katie Yates, Principal Economist, ph. 03 9695 6622 for any inquiries regarding this submission.

Yours sincerely,

Alistair Parker
Director Regulation and Network Strategy

Attachment

SP AusNet Submission on Draft Report – Review of Distribution Reliability Outcomes and Standards (project no. ERP0031)

Introduction

SP AusNet welcomes this opportunity to respond to the AEMC's Draft Report for the review of distribution reliability outcomes and standards.

The Draft Report sets out the AEMC's proposal for achieving a nationally consistent framework. There are many aspects of the framework that SP AusNet supports. These include: the adoption of an outputs-based approach; the use of a consistent framework for measuring the value of customer reliability (VCR) including through a transparent process of customer consultation; the inclusion of an incentive system with material financial rewards and penalties; and, a move to greater consistency in the measures and reporting of reliability performance.

However, in considering the framework's implications, it is apparent that the proposed process for establishing reliability targets is inconsistent with the existing Victorian arrangements. In particular, the framework will have the following effects:

- Reliability investment will be determined predominantly through price control decisions, rather than be driven by incentives, due to the need to prepare reliability options and conduct an economic assessment; and
- It will effectively impose a minimum standard.

These elements of the proposed framework are likely to reduce the efficiency with which reliability levels are delivered and paid for in Victoria. We therefore consider that the approach outlined, if adopted, would be a backward step for Victorian consumers.

This section of the submission sets out SP AusNet's concerns with the proposed framework in detail, as well as some general observations. Responses to some of the AEMC's specific questions are set out in the next section.

Value of Customer Reliability

SP AusNet supports the proposal for further work to be completed to broaden the understanding of the value customers place on reliability, including the establishment of a transparent and nationally consistent methodology and an increased role for customer consultation in the process.

Indeed, as SP AusNet argued in its submission to the Issues Paper, this work should be conducted by one independent expert body for all jurisdictions. Establishing a single responsible institution would aid the transparency, consistency and accountability of the process. It would also be more efficient to have a single centre of expertise that can

develop and evolve its knowledge of measurement of the customer value of reliability; a task the AEMC has acknowledged to be complex.

Chapter four of the Draft Report sets out a process of customer consultation on reliability outcomes. It is not clear whether this is intended to be different to the consultation involved in measuring the value of customer reliability, and if not, what the relationship between the two consultation processes would be. Preferably, this process would input to the measurement of the value of customer reliability. To the extent that the consultation reveals a more complex picture than is appropriate to include in VCR-type measures, the increased focus on DNSP-customer consultation and communication should aid the delivery of the types of reliability valued by customers.

Incentives should be preferred

SP AusNet has long been an advocate of well-designed, financially material performance incentive schemes as an efficient means of driving service reliability improvement.

In Victoria, distribution network reliability is governed by an economic benefits based probabilistic planning approach, coordinated with the AER Service Target Performance Incentive Scheme (STPIS). Both elements are based on an assessment of the value of customer reliability (VCR). The approach represents best practice for electricity distribution network services, particularly having regard to the high needle peak in demand on extreme temperature summer days compared to average demand. The approach also satisfies the best practice criteria identified by the Brattle Group[1].

The AEMCs framework approach to setting reliability targets is not an incentive based regime (i.e. one that uses incentives and the value of customer reliability (VCR) to reveal the economically efficient level of reliability), but rather seeks to choose the best reliability outcome from a set of investment options (this relies on DNSPs to propose a series of investment options with various reliability outcomes).

An incentive based regime, such as is operating in Victoria, will be more effective as it drives innovation and least-cost solutions which contribute to better consumer outcomes, i.e. an increase in the economic level of reliability at the margin. This approach ensures that reliability investment decisions are made with the benefit of the best available and most timely information. Plus, customers only pay for reliability improvements once they are achieved.

A significant example of innovative reliability improvement in SP AusNet's experience is the development and implementation of Distribution Feeder Automation on our network. Under the current arrangements, the risks and costs in the development stage were carried by SP AusNet. The prospect of financial reward from the performance improvements that were eventually delivered, have delivered real and cost effective reliability improvements for customers.

[1] The Brattle Group, *Approaches to setting electric distribution reliability standards and outcomes,* Jan 2012

Evidence from Victoria shows that reliability has increased under the incentive based regime, without the need for expensive capital programs, and in the absence of minimum standards. The proposed framework will be less effective at driving efficient reliability investment.

Victorians will pay more for reliability performance, without commensurate benefits

The proposed framework will weaken Victorian reliability arrangements as there will be a greatly increased resource burden, a diminished role for incentives to drive efficient investment, and there is little evidence that customers would receive a substantially preferable outcome in terms of reliability performance.

The process of proposing 'reliability options' and conducting economic assessments, including for options that are not chosen, would be resource intensive and costly. There would need to be transitional arrangements if targets are to be set above current levels, as it is not clear how networks are expected to meet new targets, over what time frame, and how the costs of achieving targets would be paid for.

AEMC Draft Report Questions

The following discussion addresses some of the questions posed by the Draft Report.

Q1. Customer consultation and development of guidelines

What should be included in nationally consistent guidelines and which body should be responsible for their development?

SP AusNet supports the focus on customers and customer preferences as a central driver of the reliability framework. Customer consultation on the relevant types of reliability measures (e.g. SAIDI, SAIFI), the level of disaggregation of results, and whether unplanned and/or planned outages are important, can and should help establish what level of expenditure is appropriate to achieve different forms of reliability outcomes.

The availability of nationally consistent reliability information should also improve transparency and assist in the achievement of efficient delivery of reliable electricity services in the NEM. This notwithstanding, it is expected that jurisdictional and network differences in costs and consumer preferences will remain.

Q2. Customer Consultation

What are the important elements of customer consultation and what types of issues should customers be consulted on as part of the process of setting output reliability targets? Should customer consultation consider whether additional measures are warranted to inform customers of planned and unplanned interruptions?

SP AusNet is supportive of the national framework including a role for the DNSP-customer relationship.

As stated above, customer consultation should form a useful component of the framework. SP AusNet views this as working best as part of the value of customer reliability survey work. This is because it is necessary at some stage to make judgments as to the relative importance of different types of reliability and how much to pay for these types of reliability improvements.

It is noted that there is potential that broad customer consultation will add complexity and the findings may be difficult to implement within an incentive scheme (e.g. incentives around very short and frequent interruptions). The guidelines should address how such complexities may be addressed, with an eye to maintaining a relatively simple and transparent scheme (as the Brattle Group suggested is best practice).

Q3. Economic assessment process

What are the relevant considerations for the development of a nationally consistent economic assessment process?

The Victorian model, where reliability targets are set to historical average levels and reliability improvement is funded through the STPIS,

delivers economically efficient levels of reliability without the need for complex multi-party economic assessments. This is because DNSPs are incentivised to invest in reliability improvements up to the point where it is efficient (because DNSPs are rewarded at the level of VCR).

Q4. Worst served customers

Should the jurisdictional target setter have flexibility in setting additional obligations for worst served customers? Are there any other considerations that should be taken into account in addressing worst served customers? What are the costs and benefits of imposing a nationally consistent GSL scheme?

This is rightly a jurisdictional issue.

It is possible to address preferences (such as for protecting worst performed customers) through weightings within the incentive scheme and Guaranteed Service Level (GSL) schemes. There is also the opportunity for DNSPs to work with local communities to identify the most cost effective reliability solutions in their circumstances.

Whatever approach is adopted, it is important that it is transparent about the economic trade-off that is being made, regarding the costs of service improvements to these smaller customer groups and who pays these costs.

Q5. Consistent definitions and exclusions

What issues would arise from adopting a consistent set of definitions and exclusions for the development of output reliability targets across NEM jurisdictions?

Does the publication of unplanned SAIDI and SAIFI as a minimum provide a sufficient level of consistency for the purposes of benchmarking?

When it comes to the treatment of excluded events (such as the classification of a major event day), there may be valid reasons and jurisdictional differences for adopting different exclusion definitions. For example, SP AusNet under the current STPIS has a higher threshold for defining 'major event day' exclusions than other Victorian DNSPs. This results in fewer exclusions and a stronger incentive for reliability improvement, and was considered appropriate due to statistical analysis that revealed the standard definition was excluding days that were not considered extreme in practice. By including a greater number of these days, there is a stronger incentive on SP AusNet to improve its reliability performance.

Consideration could be given to whether, rather than imposing consistent exclusion definitions, a consistent *reporting* framework would allow the benefits of benchmarking, without limiting jurisdictional variability that reflects consumer preferences. (i.e. networks could report against a consistent set of exclusions, as well as the exclusions that apply to them for their STPIS).

Q6. Applying consistency across jurisdictions

Does the proposed framework provide sufficient flexibility to meet the specific locational characteristics of individual jurisdictions while achieving the benefits of national consistency?

No – Relative to the existing arrangements in Victoria, the proposed framework adds additional costs and is likely to decrease the efficiency with which service reliability is delivered.

Q7. Process controls and performance safeguards

To what extent should there be an obligation on DNSPs to meet their reliability targets in any given year?

What options are available to provide confidence that DNSPs are seeking to meet the output reliability targets on average?

Evidence from Victoria has shown that an incentive based scheme (STPIS) provides a high degree of assurance that DNSPs are seeking to meet their reliability targets, and to improve their reliability where it is economic to do so.

The incentive based approach is transparent, where performance is reported on annually and given further prominence in the price review process. For profit motivated businesses, further process controls and performance safeguards are unnecessary.