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Stephanie Jolly
Executive General Manager, Consumers, Policy and Markets
Australian Energy Regulator
By email: VCR2024@aer.gov.au

Dear Stephanie,

Ausgrid welcomes the opportunity to provide this submission to the Australian Energy Regulator (**AER**) in response to its Values of Customer Reliability (**VCR**) Revised Draft Determination (**Revised Draft Determination**).

Ausgrid operates a shared electricity network that powers the homes and businesses of more than 4 million Australians living and working in an area that covers over 22,000 square kilometers from the Sydney CBD to the Upper Hunter.

VCR is among the most important inputs into our investment decision making. From pole replacement to our cyber security program, we use VCR to align our investments with how much our customers are willing to pay for a reliable level of service. At a time of rapid technological change and evolving aspirations from customers in how they use, store and export energy back to the grid, it is critical that the AER undertakes a robust review of its VCR method in collaboration with stakeholders.

Our submission makes the following key points:

- The compressed timetable for finalising the VCR method should be revisited;
- The potential impact of transient macroeconomic factors should be considered when setting a VCR that informs investments that have a 40-year time horizon;
- The wording of the baseline outage scenario may anchor survey responses towards an artificially low willingness to pay for reliability;
- Quantifying the impact of safety from a loss of supply should form part of the AER's considerations;
- An annual adjustment for electrification should be developed following further consultation with a wide range of stakeholders; and
- The AER should prescribe a separate VCR for central business districts (**CBD**).

Highly compressed timetable should be revisited

We welcome the AER's switch to the standard consultation procedure for making its VCR determination but remain concerned about the updated decision-making timeframe.

Our concern is that the AER's current review timetable is to finalise the VCR methodology in August. This timeframe only provides sufficient time for relatively minor amendments to be made but provides very limited scope to consider the more complex issues raised in the AER's

Draft Determination. Some of these issues, such as an annual adjustment for growth in electrification, were raised in 2019 as matters the AER would address at a later VCR review. At this stage, however, these issues remain unresolved, and more time is needed to work collaboratively with network businesses and customers to progress these issues.

Our preference is for the AER to provide additional time in its timetable for matters that do not affect the customer surveys so that some progress can be made on these complex issues. By taking this approach, future VCR reviews will be able to build on the initial steps taken in this review.

Alternatively, if the AER is unable to make additional time available in this review, we recommend bringing forward the next review and allowing time for a collaborative effort with the industry and customers so that meaningful progress can be made. In making this recommendation, we are mindful of the significant benefit to consumers in developing a better understanding of the value they place on reliability in a rapidly changing environment.

Recommendation 1

Ideally, the AER should extend the decision-making timetable to provide more time to work with network businesses and customers on those matters in its Revised Draft Determination that are more complex than minor amendments to the current VCR method. This would lead to delaying the scheduled August 2024 surveys.

Recommendation 2

If the AER maintains its current timetable, then it should either:

1) Proceed with the surveys in August 2024 as planned but continue to engage with stakeholders on more complex amendments (e.g. annual adjustment mechanism) up until December 2024 when the AER finalises its new VCR; or

2) Consider revisiting its VCR method earlier than the usual 5-year period.

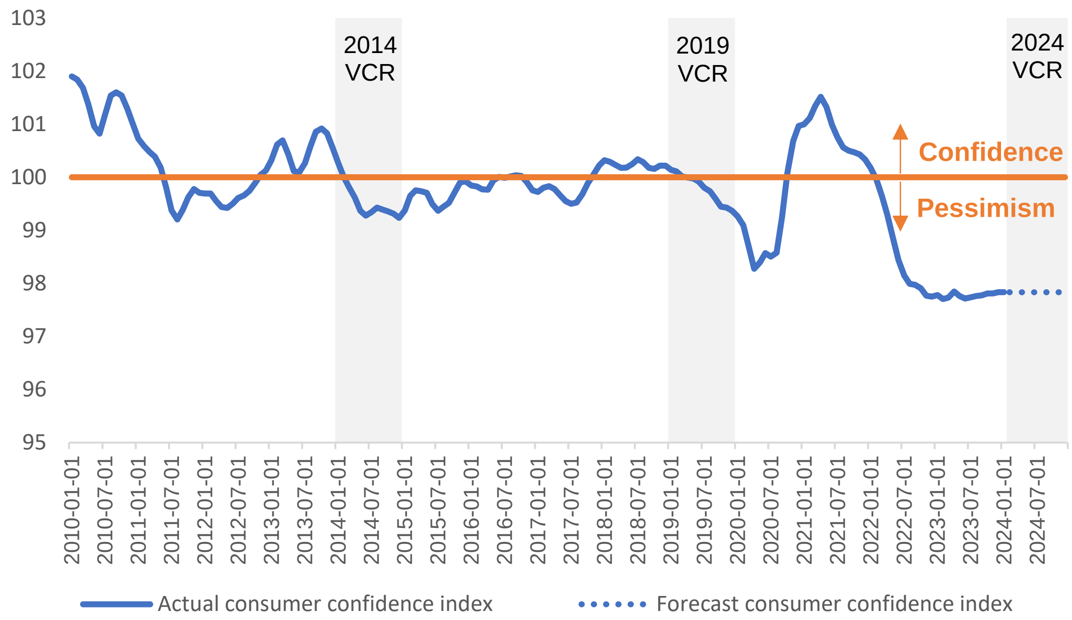
Regarding (1) above, we suggest revisiting VCR within 2 years so that the AER, network business and customers can work collaboratively together to progress the more complex aspects of the VCR assessment. The next review should allow sufficient time to make meaningful progress on these issues, noting the importance of the VCR to electricity consumers.

Potential impact of the current macroeconomic climate

We encourage the AER to be mindful that customer surveys provide insights at a snapshot in time that may not be representative of longer-term attitudes.

In past VCR reviews the timing of customer surveys may not have been a significant issue. In particular, Figure 1 below shows that both the 2014 and 2019 VCR determinations coincided with a near-neutral consumer sentiment (100 index value), indicating neither consumer optimism nor pessimism. The timing of these earlier surveys contrasts sharply with current consumer confidence which is highly pessimistic going into the 2024 VCR survey.

Figure 1: Consumer confidence index in Australia[1]



Network businesses are required to make long-term investment decisions, including investments in assets with lifetimes of 40+ years. Customers' willingness to pay for reliability at any point in time may vary for many reasons, including transitory macroeconomic factors such as consumer confidence. In assessing the VCR, it may be important to distinguish genuine changes in customer preferences from transitory factors that may influence a 'snapshot' assessment of VCR.

We acknowledge that this is a complex issue. With more time, our preference would have been to work collaboratively with the AER and customer representatives on identifying whether relatively short-run changes in economic conditions can materially impact VCR survey results. It may be that no changes are required to the AER method; however, we have not been able to reach a firm view given the tight timing between the AER's Revised Draft Determination (June 2024) and the planned commencements of VCR surveys (August 2024).

Recommendation 3

The AER should consider if transient macroeconomic factors may be under- (or over-) stating a customer's willingness to pay at a particular snapshot in time. This could involve:

- A commitment to reviewing the VCR within 2 years of the 2024 determination when economic conditions and consumer confidence have most likely stabilised; and/or
- Further exploration of this issue with network businesses and customer advocates if the 2024 survey results are materially different to the 2019 VCR.

[1] OECD, Composite Leading Indicators: Composite Consumer Confidence Amplitude Adjusted for Australia [CSCICP03AUM665S], https://fred.stlouisfed.org/series/CSCICP03AUM665S, June 21, 2024.

Current wording of the baseline scenario could anchor customer responses

The AER's Revised Draft Determination acknowledges the current baseline scenario is a relatively benign outage that many customers may not find it worthwhile to avoid and may report zero customer willingness to pay.[2] This is supported by the AER's 2019 VCR study where 41% of respondents were willing to spend zero to avoid the baseline scenario, which is: 'two unexpected outages per year on a random weekday in winter that each last for one hour in off-peak times and only affects the local area'.

Our concern is that the baseline scenario, as currently worded, may anchor later responses provided by customers. Anchoring occurs where an early piece of information influences subsequent answers. This is potentially an issue as customers providing a zero willingness to pay to avoid the baseline scenario may 'set the tone' for their responses to subsequent questions when the AER uses choice modelling to estimate the willingness to pay for other scenarios.

If anchoring is occurring, then the following statement from the AER may need further consideration: 'even if survey participants chose zero willingness to pay response for the baseline scenario, it does not imply they would indicate zero willingness to pay for other scenarios in the choice modelling'.[3] Anchoring doesn't necessarily mean that customers would continue to indicate zero willingness to pay for other scenarios. However, anchoring could in fact influence later willingness to pay responses to different scenarios put to customers.

Recommendation 4

We acknowledge that it is unlikely that the AER could amend the wording of its survey questions in time for its August 2024 surveys. To consider this issue, we recommend:

- Ongoing engagement on the survey questions after August 2024; and
- Bringing forward the next VCR review (i.e. within 2 years) so that any improvements in the wording of survey questions do not have to wait the usual 5 year period to be implemented.

Quantifying the impact of safety

Reliability has important safety implications that should be factored into the VCR. To address this issue, the AER could apply Energy Networks Association's (**ENA**) on-going research seeking to quantify the safety consequences of losing the supply of electricity.[4]

The ENA's project builds upon previous CSIRO research for estimating safety risks due to electricity supply interruptions. It also addresses the trade-offs that electricity network operators must make in managing risks such as bushfires and public safety, which can sometimes lead to an increased safety risk from the loss of supply. This information will be useful in enhancing the

[2] AER, *Revised draft determination: Values of customer reliability method*, June 2024 p.27.
[3] AER, *Revised draft determination: Values of customer reliability method*, June 2024 p.27.
[4] CSIRO, *Quantifying the safety impacts of loss of electricity supply during extreme heat and bushfire weather*, March 2024.

AER's valuation framework, so that it accurately reflects the safety dimensions of electricity supply reliability.

Incorporating the safety consequences of losing electricity supply into customer valuation metrics is essential for developing a comprehensive approach to energy reliability. We recommend that the AER considers the ENA's ongoing research as a foundation for this initiative, leveraging their findings to address the trade-offs and safety risks inherent in electricity supply management. If required, the ENA's work could be supplemented by surveys that align to the AER's willingness to pay method.

Recommendation 5

The AER approach to valuing a customer willingness to pay for a reliable supply of electricity should incorporate the safety consequences of losing supply. This could involve leveraging ENA research or incorporative safety related questions into AER surveys.

Capturing electrification in annual adjustments

We would welcome the opportunity to work with the AER to calculate an annual adjustment for growth in electrification via the 'CPI-X' method. This issue was raised as an area for further exploration during the 2019 VCR review, noting that the AER considered that there was insufficient information to enable a non-zero X to be set at that time.

While we recognise that the introduction of an electrification adjustment mechanism is a complex issue, the growth in electrification since the 2019 VCR review and the likely growth over the next 5 years reinforces the importance of progressing this issue in the current review. As noted in recommendation 1, our view is that progress on this issue could be made if the AER extended the current timetable or continued to consider this matter in consultation with stakeholders after surveys have commenced, with a view to finalising the AER's position by December 2024. The introduction of an adjustment mechanism in this review will provide the initial groundwork for further developments in the next and subsequent reviews.

Recommendation 6

We recommend that the AER extends the time for making its 2024 VCR determination to design a method for annual updates for electrification. In the alternative, the AER should consider:

- Continue engaging on the development of an annual adjustment mechanism with a view to finalising an approach by December 2024; or
- Undertaking a VCR review within 2 years after the 2024 determination to provide more time to collaborate with stakeholders.

Prescribing VCRs for CBDs

We suggest that the AER consider prescribing a separate VCR for CBDs. CBDs contain a unique mix of customers with significant economic impacts when there is an outage, which could result in a higher VCR if all impacts are accounted for.

We consider it is uncontroversial that the VCR is likely to have a higher value in CBDs than other network areas, given the extent of economic activity in CBDs. This point was acknowledged by the AER's consultant in deciding a dispute on Ausgrid's application of the RIT-D to proposed reliability investments for the Sydney CBD in 2018. At that time, the AER's consultant noted that uniqueness of CBDs in terms of the customer mix; the dominance of high-rise buildings; and the high number of business customers who rely on e-commerce, all of which depend on a reliable electricity supply.

An estimate of the VCR for CBDs depends on understanding how many millions of people rely on the CBD for business, entertainment, transport, recreation and tourism. In this context, the value of a reliable electricity supply cannot be captured by focusing only on the customers' willingness to pay. Instead, an assessment of VCR needs to account for the potential loss in economic value that would arise if users of the CBD were unable to rely on the transport systems, hospitals or other infrastructure on which the proper functioning of the CBD depends.

We acknowledge that estimating the VCR for CBDs creates methodological challenges in capturing the full value of reliability. The question of 'who pays' is also relevant, if the VCR for CBDs is assessed using a different method that captures the wider community and economic benefits of a reliable electricity supply in addition to the private benefits obtained by electricity customers. Notwithstanding these challenges, and as noted in relation to electrification, our strong preference is to commence the analysis required to introduce a VCR for CBDs in this review and thereby establish the groundwork for future refinements in subsequent reviews of the VCR.

Recommendation 7

The AER should incorporate the calculation of a separate VCR for CBDs. This is likely to require standalone economic analysis of the community and economic impacts that result when electricity customers in CBDs lose supply. Our expectation is that this analysis can be finalised by December 2024 or soon after.

Ausgrid welcomes the opportunity to continue to work closely with the AER as it completes the final stages of this important review. If you have any questions regarding this submission please contact Shannon Moffitt, Strategy Manager, at shannon.moffitt@ausgrid.com.au or 0468 616 512.

Regards,

Fiona McAnally
Head of Regulation