



Ref.: TP/CP

13 March 2009

Mr Chris Pattas
General Manager
Network Regulation South
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3000

61 Mary Street
Brisbane QLD 4000
PO Box 15107
City East QLD 4002
Phone 07 3228 8222
Fax 07 3228 8118
Website www.ergon.com.au

Dear Mr Pattas

Electricity Distribution Network Service Providers - Service Target Performance Incentive Scheme - Version 1.1

Ergon Energy Corporation Limited (Ergon Energy) appreciates the opportunity provided by the Australian Energy Regulator (AER) to respond to the AER's Electricity Distribution Network Service Providers - Service Target Performance Incentive Scheme (STPIS) Version 1.1

The attached submission represents Ergon Energy's response to the AER's proposed amendments to the STPIS.

Ergon Energy looks forward to providing continued assistance to the AER in its Review of the STPIS.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Tony Pfeiffer', enclosed in a circular scribble.

Tony Pfeiffer
General Manager Regulatory Affairs

Enc.:

c.c.: Carmel Price

Telephone: 3228 7711
Facsimile: 3228 8130
Email: tony.pfeiffer@ergon.com.au

Ergon Energy Corporation Limited

**Proposed Amendment - Service Target
Performance Incentive Scheme - Submission**

**Australian Energy Regulator
19 March 2009**

Service Target Performance Incentive Scheme Guidelines – Submission

Australian Energy Regulator

19 March 2009

This submission, which is available for publication, is made by:

Ergon Energy Corporation Limited
PO Box 15107
City East
BRISBANE QLD 4002

Enquiries or further communication should be directed to:

Tony Pfeiffer
General Manager Regulatory Affairs
Ergon Energy Corporation Limited
Email: tony.pfeiffer@ergon.com.au
Ph: (07) 3228 7711
Mobile: 0417 734 664
Fax: (07) 3228 8130

Or

Carmel Price
Manager Regulatory Affairs – Network Regulation
Ergon Energy Corporation Limited
Email: carmel.price@ergon.com.au
Ph: (07) 4121 9545
Mobile: 0408 702 814
Fax: (07) 3228 8130



TABLE OF CONTENTS

Overview	3
Introduction	3
1 Proposed amendments - Adjustments to Allowed Revenue	4
1.1 Applying the s-Factor to the Control Mechanism.....	4
1.2 Removing the Effect of the s-Factor	4
1.3 The Operation of the s-Bank Mechanism	4
1.4 Revenue at Risk	4
1.5 The Service Standard Factor – s-Factor Formula	5
1.6 Overlap Between Regulatory Control Periods.....	5
1.7 Timing and Equation Notation	6
2 Proposed Amendments – Major Event Day Definition	6
2.1 Steps for Establishing the Major Event Day Boundary.....	6
2.2 Frequency of Calculating the Major Event Day Boundary.....	6
2.3 Application of the IEEE Exclusion	7
3 Proposed Amendments – The Value of Customer Reliability	7
4 Other Amendments and Clarifications	7
4.1 Calculating Incentive Rates	7
4.2 Deletion of Clauses 1.8(b) and 1.8(d).....	8
4.3 Insertion of Clauses 3.2.1(a)(1A), 5.3.1(b)(1A), 5.3.1(b)(1B) and 5.3.1(b)(1C).....	9
4.4 Amendment to Clauses 5.1(e) and 6.2(4)	9
4.5 Insertion of Appendix E	9

Overview

Ergon Energy Corporation Limited (Ergon Energy) welcomes the opportunity to make this submission to the Australian Energy Regulatory (AER) on its proposed amended “Electricity Distribution Network Service Providers - Service Target Performance Incentive Scheme” Version 1.1 (the STPIS). This submission is provided by Ergon Energy in its capacity as a distribution network service provider (DNSP) in Queensland.

Introduction

Ergon Energy generally supports the amendments to the proposed amended STPIS. However, Ergon Energy believes that the following issues warrant further clarification or amendment:

- the adjustments to account for the overlap between regulatory control periods should only apply to those s-Factors calculated in years four and five of a regulatory control period, and not to the s-Factor calculated in the first year of the next regulatory control period;
- the timing and equation notation for equations (1A), (5A) and (5B) in Appendix C of the proposed amended STPIS should align with the worked example set out in Appendix E of the proposed amended STPIS;
- the provisions in clauses 3.2.1(a)(1A), 5.3.1(b)(1A), 5.3.1(b)(1B) and 5.3.1(b)(1C) of the proposed amended STPIS should not apply to Ergon Energy in setting the STPIS performance targets for the 2010-11 to 2014-15 regulatory control period;
- how adjustments in accordance with clauses 3.2.1(a)(1A), 5.3.1(b)(1A), 5.3.1(b)(1B) and 5.3.1(b)(1C) of the proposed amended STPIS are likely to be made, and whether the AER requires Ergon Energy to propose these adjustments in future regulatory proposals; and
- the worked example in Appendix E of the proposed amended STPIS should escalate the Annual Revenue Requirement (ARR) by CPI as per equation (1A) in Appendix C of the proposed amended STPIS

These issues are detailed in the following sections of this submission.

1 Proposed amendments - Adjustments to Allowed Revenue

1.1 Applying the s-Factor to the Control Mechanism

Clause 5.1.1 of the Explanatory Statement and Appendix C of the proposed amended STPIS detail how the s-Factor is incorporated into the various forms of control currently applied to Standard Control Services. Specifically, the s-Factor is incorporated into the general form of the control mechanisms as another multiplier alongside the CPI minus X adjustment.

Ergon Energy supports the additional clarification and equations relating to the application of the s-Factor to the control mechanism provided in Appendix C of the proposed amended STPIS.

1.2 Removing the Effect of the s-Factor

Clause 5.1.2 of the Explanatory Statement and Appendix C of the proposed amended STPIS outline changes to the application and retention of s-Factors during the regulatory control period. Specifically, the effect of the s-Factor is now removed after one year, whereas previously the s-Factor was applied cumulatively, thereby altering revenues (and prices) until the end of the regulatory control period.

Ergon Energy supports the proposed amendment to remove the effect of the s-Factor after one year rather than apply the s-Factors cumulatively.

1.3 The Operation of the s-Bank Mechanism

Clause 5.1.3 of the Explanatory Statement and Appendix C of the proposed amended STPIS outline changes to the operation of the s-bank mechanism. Specifically, the s-bank equation no longer includes the $(1 + \text{pretax WACC})$ term.

Ergon Energy supports the amendment to remove the $(1 + \text{pretax WACC})$ term from equation (3) provided in Appendix C of the proposed amended STPIS.

1.4 Revenue at Risk

Clauses 5.1.2 and 5.1.4 of the Explanatory Statement and Appendix C of the proposed amended STPIS outline clarifications to the application of the caps on revenue at risk. Specifically, the cap on revenue at risk was increased from +/- three per cent to +/- five per cent. In addition, Equations (4A) and (4B) are now provided in Appendix C of the proposed amended STPIS to mathematically describe the operation of the cap on revenue at risk.

Ergon Energy acknowledges the amendment to increase the cap on revenue at risk from +/- three per cent to +/- five per cent, and understands that the AER has made this change as a result of removing the effect of the s-Factor after one year rather than applying the s-Factors cumulatively.

Ergon Energy notes that the AER's Framework and Approach Stage 2 (F&A Stage 2) proposed that the maximum revenue at risk for the 2010-11 to 2014-15 regulatory control period should be +/- two per cent of the ARR. Ergon Energy believes that this lower amount should be applied to Ergon Energy in its next regulatory control period. Consequently, the AER's proposed amendment should not impact Ergon Energy in the 2010-11 to 2014-15 regulatory control period.

Ergon Energy supports the provision of equations (4A) and (4B) in Appendix C of the proposed amended STPIS to describe mathematically the operation of the cap on revenue at risk.

1.5 The Service Standard Factor – s-Factor Formula

Clauses 5.1.2 and 5.1.5 of the Explanatory Statement and Appendix C of the proposed amended STPIS outline changes to the s-Factor formula. Specifically, the s-Factor is computed primarily on the basis of deviations in performance from the underlying targets, rather than based on changes in the size of the annual performance improvement between years. Equations (5A) and (5B) in Appendix C of the proposed amended STPIS set out the proposed methodology for calculating the sum of the raw s-Factors under the STPIS.

Ergon Energy supports the proposed amendment to compute the s-Factor on the basis of deviations in performance from underlying targets.

In addition, Ergon Energy supports the amended s-Factor formulas and considers that equations (5A) and (5B) in Appendix C of the proposed amended STPIS provide sufficient guidance on calculating the raw s-Factors.

1.6 Overlap Between Regulatory Control Periods

Clause 5.1.6 of the Explanatory Statement and Appendix C of the proposed amended STPIS outline clarifications to the X_0 parameter in the overlap adjustment formula. Specifically, the description of X_0 as applied in equation (6) in Appendix C of the proposed amended STPIS more generally reflects X_0 given the different control mechanisms that may be applied to DNSPs under clause 6.2.5(b) of the NER. In addition, the value of X_0 is to be taken from the PTRM applicable in the next regulatory control period.

Ergon Energy supports the amended description of X_0 as applied in equation (6) in Appendix C of the proposed amended STPIS. Ergon Energy also supports the additional clarification regarding the source of the X_0 value.

However, the final paragraph of Appendix C of the proposed amended STPIS indicates that the overlap adjustment is required for the purposes of calculating the s-Factor for the second last and the last regulatory year of the current regulatory control period **and the first year of the next regulatory control period.**

Ergon Energy does not believe that an overlap adjustment is necessary when calculating the s-Factor in the first year of the current regulatory control period. This is because the s-Factor calculated in year one goes on to affect the ARR in year three of the same regulatory control period. Only the s-Factors in years four and five need adjustment, as these go on to affect the ARR in years one and two of the next regulatory period respectively.

Consequently, Ergon Energy considers that the final paragraph of Appendix C of the proposed amended STPIS should be changed to:

“In this instance, the value of S''_t is used in equation (2) in place of S'_t , for the purposes of calculating the s-Factor for the second last and the last regulatory year of the current regulatory control period.”

Ergon Energy notes that the worked example provided in Appendix E of the proposed amended STPIS aligns with Ergon Energy’s proposed approach.

1.7 Timing and Equation Notation

Clause 5.1.7 of the Explanatory Statement and Appendix C of the proposed amended STPIS outline clarifications to the timing and equation notation.

Ergon Energy considers that the equation time subscripts used in equations (1A), (5A) and (5B) in Appendix C of the proposed amended STPIS are inconsistent with the worked example in Appendix E of the proposed amended STPIS.

To achieve consistency, Ergon Energy considers that equations (1A), (5A) and (5B) in Appendix C of the proposed amended STPIS should be modified as follows:

Equation (1A)

$$AR_{t+z} = AR_{t+1} * (1 + \Delta CPI_{t+z}) * (1 - X_{t+z}) * (1 + S_t)$$

Equation (5A)

$$S_t^{ROS} = \sum_p ir_p * [Tar_{p,t} - Act_{p,t}]$$

Equation (5B)

$$S_t^{CS} = \sum_p \min(\max(ir_p * [Tar_{p,t} - Act_{p,t}], \underline{S}^{ICS}), \bar{S}^{ICS})$$

2 Proposed Amendments – Major Event Day Definition

2.1 Steps for Establishing the Major Event Day Boundary

Clause 5.2.1 of the Explanatory Statement and Appendix D of the proposed amended STPIS outline changes to the methodology for establishing the Major Event Day boundary. Specifically, 'step 2' from Version 1.0 of the STPIS has been removed from Appendix D of the proposed amended STPIS.

Ergon Energy supports the amendment to remove 'step 2' from Appendix D of Version 1.0 of the STPIS to align the steps with the IEEE 1366:2003 standard. This also aligns the STPIS with Ergon Energy's existing methodology for calculating the Major Event Day boundary.

2.2 Frequency of Calculating the Major Event Day Boundary

Clause 5.2.2 of the Explanatory Statement and Appendix D of the proposed amended STPIS outline changes to the frequency of calculating the Major Event Day boundary. Specifically, the Major Event Day boundary will be calculated annually using the last five years of SAIDI data consistent with IEEE standard 1366:2003.

Ergon Energy supports the amendment requiring the annual calculation of the major event day boundary using the last 5 years of SAIDI data (consistent with the IEEE standard). Annual calculation of the Major Event Day boundary aligns with Ergon Energy's existing methodology for calculating the Major Event Day boundary.

2.3 Application of the IEEE Exclusion

Clause 5.2.3 of the Explanatory Statement and Appendix D of the proposed amended STPIS outline clarifications relating to the application of Major Event Day exclusions. Specifically, the entire duration of those outages originating within the midnight to midnight period of a Major Event Day will be excluded.

Ergon Energy supports the clarification that the entire duration of outages originating within the midnight to midnight period of a Major Event Day will be excluded. This aligns with Ergon Energy's existing treatment of outages originating within the midnight to midnight period of a Major Event Day.

3 Proposed Amendments – The Value of Customer Reliability

Clause 5.3 of the Explanatory Statement outlines changes to the Value of Customer Reliability (VCR). Specifically, based on the outcomes of a more recent VCR study for VENCORP, the revised VCRs figures are:

- \$97 700/MWh for CBD segments; and
- \$47 850/MWh for all other parameter segments.

The proposed VCR value must be escalated from the September 2008 quarter to the start of the regulatory control period.

Ergon Energy acknowledges the amendments to the VCR values and supports the retention of the provision allowing Ergon Energy to propose an alternative VCR to the AER in its regulatory proposals (pursuant to clause 3.2.2(d) of the STPIS).

4 Other Amendments and Clarifications

4.1 Calculating Incentive Rates

Average Annual Energy Consumption

Clause 5.4.1 of the Explanatory Statement outlines changes to clauses 3.2.2(h)(1), 3.2.2(i)(1) and Appendix B of the proposed amended STPIS. Specifically, the average annual energy consumption input used to calculate incentive rates for the reliability of supply parameters should be an input according to network type.

Ergon Energy supports the amendment requiring the average annual energy consumption input, used to calculate incentive rates for the reliability of supply parameters, to be an input according to network type.

Annual Revenue Requirement

Clause 5.4.1 of the Explanatory Statement outlines changes to clauses 3.2.2(h)(2), 3.2.2(i)(2) and Appendix B of the proposed amended STPIS. Specifically, the average of the real smoothed ARR (in dollars referenced to the first regulatory year of the regulatory control period) for the regulatory control period determined by the AER in the relevant Distribution Determination must be used in calculating incentive rates for the reliability of supply parameters.

Ergon Energy supports the additional clarification relating to the revenue input used to calculate incentive rates for the reliability of supply parameters.

However, to achieve consistency with the provisions of Clauses 3.2.2(h)(2) and 3.2.2(i)(2) of the proposed amended STPIS, Ergon Energy considers that the definition of the parameter “R” (which represents the average of the smoothed ARR for the relevant regulatory control period) in Appendix B of the proposed amended STPIS should be changed to:

...the average of the smoothed annual revenue requirement for the relevant regulatory control period (in \$, real referenced to the first regulatory year of the regulatory control period).

Other Amendments to Calculating Incentive Rates

Clause 5.4.1 of the Explanatory Statement outlines the following additional changes:

- Clause 3.2.2(i)(4) and Appendix B of the proposed amended STPIS have been amended so that the average of the annual unplanned SAIDI and SAIFI performance targets are used as inputs for calculating incentive rates for any applicable unplanned SAIFI parameters;
- Clause 5.3.2(a) and Appendix B of the proposed amended STPIS have been amended to include a reference to the units of measure that apply to the customer service parameter incentive rate;
- The calculation of SAIFI has been clarified to state that it is expressed per 0.01 interruptions in Appendix A of the proposed amended STPIS; and
- Equations (1) and (2) in Appendix B of the proposed amended STPIS have been provided to illustrate the calculation of incentive rates for the unplanned SAIDI and SAIFI parameters.

Ergon Energy supports the amendment to clause 3.2.2(i)(4) and Appendix B of the proposed amended STPIS to use the average of the annual unplanned SAIDI and SAIFI performance targets as inputs for calculating incentive rates for any applicable unplanned SAIFI parameters.

In addition, Ergon Energy supports the amendments and clarifications in clause 5.3.2(a) and Appendix B of the proposed amended STPIS to include a reference to the units of measure that apply to the customer service parameter incentive rate.

Furthermore, Ergon Energy supports the clarification that SAIFI is expressed per 0.01 interruptions as per Appendix A of the proposed amended STPIS, and the provision of equations (1) and (2) in Appendix B of the proposed amended STPIS to illustrate the calculation of incentive rates for the unplanned SAIDI and SAIFI parameters.

4.2 Deletion of Clauses 1.8(b) and 1.8(d)

Clause 5.4.2 of the Explanatory Statement refers to the deletion of clauses 1.8(b) and 1.8(d) from the proposed amended STPIS as “they unnecessarily restrict both the AER and a DNSP’s ability to amend or apply the scheme which is potentially inconsistent with the NER”.

Ergon Energy supports the amendment to remove clauses 1.8(b) and 1.8(d) from the proposed amended STPIS.

4.3 Insertion of Clauses 3.2.1(a)(1A), 5.3.1(b)(1A), 5.3.1(b)(1B) and 5.3.1(b)(1C)

Clause 5.4.3 of the Explanatory Statement outlines four additional clauses included in the proposed amended STPIS. Specifically, Clauses 3.2.1(a)(1A), 5.3.1(b)(1A), 5.3.1(b)(1B) and 5.3.1(b)(1C) require that the AER take into account any instance where the revenue at risk cap has been breached in the previous regulatory control period in setting reliability of supply and customer service parameter performance targets.

Ergon Energy acknowledges the inclusion of these clauses in the proposed amended STPIS, and notes that adjustments to the performance targets in next regulatory control period are required where a DNSP breached the cap on revenue at risk in the current regulatory control period.

Ergon Energy seeks clarification on how these adjustments are likely to be made, and whether Ergon Energy is required to propose adjustments in accordance with these clauses in its regulatory proposal.

Furthermore, as the STPIS has not operated in Queensland in the 2005-06 to 2009-10 regulatory control period, Ergon Energy seeks confirmation that the provisions in these clauses will not be applied in setting Ergon Energy's STPIS performance targets for the 2010-11 to 2014-15 regulatory control period.

4.4 Amendment to Clauses 5.1(e) and 6.2(4)

Clause 5.4.4 of the Explanatory Statement outlines changes to clauses 5.1(e) and 6.2(4) of the proposed amended STPIS. Specifically, references to 'effective competition' are replaced with the term 'standard control services' to align the terminology used in STPIS with that of the NER.

Ergon Energy supports the amendment to remove the words 'effective competition' and replace them with 'standard control services' in clauses 5.1(e) and 6.2(4).

4.5 Insertion of Appendix E

Clause 5.4.5 of the Explanatory Statement outlines the inclusion of Appendix E in the proposed amended STPIS to provide a detailed worked example of the operation of the equations in Appendix C of the proposed amended STPIS.

Ergon Energy supports the inclusion of the detailed work example in Appendix E of the proposed amended STPIS relating to the operation of the equations in Appendix C of the proposed amended STPIS.

However, Ergon Energy notes that cells D76 to M77 in the worked example do not include the CPI escalation term $(1+\Delta\text{CPI})$ as required in equation (1A) in Appendix C of the proposed amended STPIS. For consistency, Ergon Energy considers that cells D76 to M77 in the worked example should be amended to incorporate the CPI escalation term $(1+\Delta\text{CPI})$.