

# ATTACHMENT 5.7

## PASS THROUGH EVENTS

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## 1. PURPOSE

The purpose of this paper is to present to the Australian Energy Regulator (AER) Essential Energy's response to the issues raised by the AER in the *Draft decision Essential Energy distribution determination (2015-16 to 2018-19) – Attachment 15: Pass through events*.

Essential Energy submitted Attachments 4.6 and 4.7 in support of its substantive regulatory proposal on nominated pass through events. These attachments remain Essential's regulatory proposal on pass through events except for the definitions of 'pass through events', replaced by those outlined within this attachment.

## 2. SUMMARY

Issues raised by the AER regarding Essential Energy's pass through event proposal and Essential Energy's response are highlighted in the table below:

AER issue	Summary of AERs reasons and findings	Essential Energy's response
Insurance cap event, natural disaster event, terrorism event	Accepted as nominated pass through events for 2015-19 regulatory control period.	Essential Energy accepts the AER's draft decision
Insurer's credit risk event	The AER did not accept insurer's credit risk event because it considered a prudent service provider could reasonably prevent an event of that nature from occurring.	<p>Essential Energy's risk management methodology or attachment 4.7 (EY treatment of regulatory risk) has not been reviewed by the AER</p> <p>Even the most prudent risk management approach could not mitigate against the collapse of a large insurer, making a pass through a necessary risk management approach to cover such events</p>
Aviation hazards event	The AER considers that there is no need for an additional specific pass through event to cover the potential costs of this event, beyond those set out in the NER or approved in this determination.	Essential Energy considers that, if the Government does not make a decision to pass the proposed legislative protection, it will then be both justifiable (to preserve commercially acceptable insurance terms) and efficient to invest resources in undertaking a feasibility study to develop a risk register prioritising assets where prudent action is necessary to mitigate the risk of line strike in order to reduce exposure to liability and protect Essential's competitive position relative to the purchase of reasonable and commercial insurance on a competitive basis.
Modifications to Essential Energy's proposed definitions to accepted nominated pass through events	The AER amended the definitions to include the factors that the AER will have regard to when assessing a claim for pass through.	<p>Essential Energy considers it unnecessary to include the AER's definition in either the definition of insurance cap event, natural disaster event and terrorism event or as factors in the assessment of a pass through application</p> <p>These matters are neither needed to define the events nor needed as assessment factors as they have already been covered in the relevant provision of the Rules.</p>

AER issue	Summary of AERs reasons and findings	Essential Energy's response
Application to alternative control services	The AER's draft decision appears silent on this aspect of Essential Energy's substantive regulatory proposal.	Essential Energy asks that the AER makes a decision consistent with the proposal and its determinations for other network service providers in its final determination for Essential Energy.

### 3. BACKGROUND

In its substantive regulatory proposal, Essential Energy put forward its pass through event proposal for the next regulatory control period. This pass through event proposal was supported by Attachment 4.6 and 4.7 to the substantive proposal. Essential Energy nominated five pass through events including an insurance cap event, natural disaster event, terrorism event, insurer's credit risk event and an aviation hazards event

The AER's draft decision determined:

- > not to accept the insurer's credit risk event or the aviation hazards event;
- > to change the definition of the natural disaster, terrorism and insurance cap events.

### 4. DISCUSSION

In this section, the specific issues raised by AER are discussed:

- > insurer's credit risk event;
- > aviation hazards event;
- > definitions of nominated pass through events;
- > application to alternative control services.

Essential Energy also discusses the application of pass through provisions to alternative control services.

#### 4.1 Insurer's credit risk event

The AER did not accept insurer's credit risk event because it considered a prudent service provider could reasonably prevent an event of that nature from occurring. This is on the basis of part c of the nominated pass through event considerations<sup>1</sup>:

*Whether a prudent service provider could reasonably prevent an event of that nature or type from occurring or substantially mitigate the cost impact of such an event.*

The AER considers that a prudent service provider would use an insurance provider that has the capacity to satisfy any claims under a policy. The AER claims that NSPs can assess the viability of an insurer by reviewing its track record, size, credit rating and reputation. The AER claims that the inclusion of this event removes the incentive for Essential Energy to obtain insurance from a reputable provider who is able to pay a claim. The AER considers that Essential Energy is able to take steps to mitigate or prevent this event from occurring.

Essential Energy does not concur with the AER's decision and reasons. It is considered the AER has made an error of fact in that it has not demonstrated an understanding or interpretation of the material provided. It is not obvious that the AER, in reaching its decision to not approve the Insurer's Credit Risk Event, has

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<sup>1</sup> NER, cl. 6.5.10(b); NER glossary, definition of 'nominated pass through event considerations'.

considered all the material put before it by Essential Energy. For example, the AER in making a statement that 'NSPs can assess the viability of an insurer by reviewing its track record, size, credit rating and reputation' fails to demonstrate that it has considered Essential Energy's risk management methodology or that it reviewed the external Ernst & Young regulatory treatment of risk report (Attachment 4.7 of Essential Energy's substantive proposal). This material highlights that Essential Energy's insurance arrangements encompass a robust and thorough renewal and review process; and the nominated pass through events (including the Insurer's Credit Risk Event) proposed by Essential Energy are appropriate because they capture the risks which are beyond the control of the NSW DNSPs to prevent or mitigate.

In particular, Essential Energy seeks to mitigate the risk of any insurers becoming non-viable by regular monitoring and reporting by its broker, Aon and Marsh, of insurer Standard & Poor (S & P) rating movements. Essential Energy's minimum acceptable insurer S & P rating is A-. Essential also keeps liability insurance exposure to A- insurers to less than 7.5%. Essential's brokers monitor insurer ratings to ensure that any changes are flagged as soon as possible. They cannot and do not guarantee the security of Essential Energy's insurers.

An excerpt of the Ernst & Young report<sup>2</sup> is provided below. This excerpt demonstrates the prudent risk management framework in place at Essential Energy.

*Under the NSW DNSPs' risk management framework:*

- *the framework uses a Bow-Tie methodology to identify and assess any relevant risks and to understand the nature of these risks (e.g. likelihood, impacts)*
- *the framework identifies and implements risk controls which are either preventative controls (to lower the chance of the hazardous event happening) or mitigation controls (to lessen the consequences if it does)*
- *the NSW DNSPs maintain comprehensive insurance arrangements, which are regularly reviewed to align with the Bow-Tie risk assessments. In addition:*
  - *the insurance arrangements encompass a robust and thorough renewal and review process including forward strategic planning and gathering of updated risk information (including Bow-Tie updates) in order to 'sell' their risks appropriately to the global insurance market*
  - *advice is obtained from external risk and insurance brokers/consultants (currently Aon and Marsh) and the DNSPs' own insurance specialists to establish the appropriate levels of coverage, implement appropriate insurance market negotiation strategies and to efficiently and effectively manage any claims. The insurance market is cyclical and subject to change, therefore the appropriate levels and types of coverage can vary each year in order to obtain insurance coverage on optimal terms from the market to align with risk treatment strategies.*
  - *the NSW DNSPs take a coordinated approach to insurance, with a Group Insurance Committee (GIC) overseeing the insurance renewal and review process. GIC membership is made up of senior group executives and senior executives from each network business, including the Group CFO, Group Executive Network Strategy, Board Secretary, General Managers Finance and Compliance and insurance specialists.*

Moreover, the AER's contention that DNSPs will always be able to assess the viability of an insurer does not take into account how severely impacted the NSW DNSPs were by the unforeseen collapse of HIH – Australia's second largest insurer at the time and the largest corporate failure in Australia's history. Essential Energy submits that even the most prudent risk management approach could not mitigate against such an occurrence, making a pass through a necessary risk management approach to cover such events.

Essential Energy considers its approach to nominating this pass through event was based on sound reasoning and satisfied the nominated pass through event considerations of the Rules. Essential Energy

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<sup>2</sup> Attachment 4.7 to Essential Energy substantive regulatory proposal - EY – Regulatory Treatment of Risk, p 9.

could neither do anything further to prevent an insurer's credit risk event from occurring, nor could Essential Energy substantially mitigate the cost impact of such an event.

Essential also notes the AER's draft decision is inconsistent with its previous approaches or decisions. Notably, the AER has approved a similar pass through event in several of its determinations for the Victorian DNSP's and Aurora.<sup>3</sup>

Accordingly, the AER should approve the Insurer's Credit Risk Event as a nominated pass through event having regard to the considerations and evidence described above.

For the reasons above, Essential Energy has not incorporated the AER's draft decision on this event in its revised proposal. The revised proposal maintains this event as a nominated pass through event; with the definition of the event described below in section 4.3.

## 4.2 Aviation hazards event

The AER did not accept aviation hazards event because it considered a prudent service provider could reasonably prevent an event of that nature from occurring. This is on the basis of part a) and part c) of the nominated pass through event considerations<sup>4</sup>:

*(a) whether the event proposed is an event covered by a category of pass through event specified in clause 6.6.1(a1)(1) to(4) (in the case of a distribution determination) or clause 6A.7.3(a1)(1) to(4) (in the case of a transmission determination);*

*(c) Whether a prudent service provider could reasonably prevent an event of that nature or type from occurring or substantially mitigate the cost impact of such an event*

The AER considers Essential Energy should insure against line strikes and that it has not provided an explanation of whether insurance for this type of event could be obtained. Further, the AER claims the event is already covered by another category of pass through event, possibly a regulatory change event, in the event that the NSW Government required Essential Energy to satisfy a higher standard in relation to these powerlines.

The AER noted this event was accepted for ACTEWagl in its 2009 determination<sup>5</sup>. Essential Energy wishes to clarify that this event was accepted for Essential Energy in its 2009 determination.

The AER considers there is no need for an additional specific pass through event to cover the potential costs of this event, beyond those set out in the NER or approved in this determination.

Essential Energy considers the pass through event in line with the below definition should be accepted. Aviation hazards event: this event occurs if:

1. Essential Energy pursues legislative protection from the government for potential liabilities (related to the findings in *South West Helicopters and anor v Essential Energy*, *Sheather v Country Energy* or the subject of the coronial inquests in the Mudgee Court 30.04.07 to 4.5.07 and Forbes Court 21.7.08 to 1.8.08) arising from powerlines, where those powerlines otherwise comply with Australian and industry standards, and
2. the relevant government authority advises that Essential Energy will not be provided with legislative protection from liability for these events, and
3. a strategy and feasibility study is completed by or for Essential Energy, in consultation with CASA and the relevant regulatory authorities to identify actions necessary to mitigate the risks of aviation hazards.

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<sup>3</sup> AER, *Victorian electricity distribution network service providers distribution determination 2011-2015, Final Decision*, October 2010; AER, *Final Distribution Determination*; AER, *Aurora Energy Pty Ltd 2012-13 to 2016-17*, 30 April 2012.

<sup>4</sup> NER, cl. 6.5.10(b); NER glossary, definition of 'nominated pass through event considerations'.

<sup>5</sup> Essential Energy draft decision : Attachment 15 Pass through events, page 15

Essential Energy's exposure is much higher and less easily mitigated than other NSW DNSPs due to the unique scale and characteristics of its network. As a decision has not yet been made by Government on the submission proposing legislative protection, Essential Energy requests the AER to accept the 'aviation line strike' event pass through event for the 2015-18 regulatory control period.

Essential Energy submits that due to the uncertainty around the possible legislative protection, it cannot reasonably predict or accurately forecast the potential significant costs at this time, which is why the pass through mechanism is appropriate based on the definition above.

In its proposal to the AER, Essential Energy noted the outcomes in two coronial inquiries and the Sheather decision. The decision in *South West Helicopters and anor v Essential Energy* (Supreme Court of New South Wales [2014] NSWSC 1758) handed down on 19 December 2014, introduces further uncertainty regarding the scope of Essential Energy's duty and what would be required to discharge the duty.

His Honour Justice Bellew found that Essential Energy breached its duty of care to both the deceased occupant and the owner of the helicopter which collided with a line near Parkes in 2006. While the line was not in breach of relevant Australian Standards, His Honour considered the fire prone status of the land (Essential Energy has around 150,000 kilometres of overhead line in fire prone areas), the distance of the span and the proximity of a roadway (found to be used as a navigational aid to pilots) as relevant factors. This decision goes further than the previous decision of Sheather, because direct knowledge of low flying was not required on the basis that the fire prone status of the land was a factor 'from which it must have been known that low level flying in the area would be likely' and raises new queries regarding the extent of Essential Energy's duty and what would be required to discharge the duty.

The AER's draft determination does not accept the 'aviation strike event' and points to the availability of insurance as a central reason for its position. The AER's draft determination seems to consider that the current insurance available to Essential Energy is, and will remain, a commercially acceptable position and an appropriate policy response to the issue.

Although Essential Energy acknowledges its current insurance program potentially offers some protection against this liability, its pass through application relates to the potentially significant investment required to undertake a strategy and feasibility study that identifies actions necessary to mitigate the risks of aviation hazards and the cost of taking such action. If Essential Energy does not invest in these efficient and prudent risk management initiatives and as a result claims occur, this may directly and adversely impact the availability of commercial insurance on a reasonable basis (that is whether the risk remains insurable for Essential Energy and, if so, the terms on which the insurance is offered).

An insurer's response to an adverse claims experience, without evidence of an insured party taking reasonable action to mitigate this risk, is to exclude coverage for such events, force increased retention levels and significantly increase premiums. In the recent decision in *South West Helicopters and anor v Essential Energy*, the Court found that the fire prone status of land can comprise the basis on which Essential Energy is taken to have known that low flying is 'likely'. This finding appears to expand (that is, expand beyond the previous decision in Sheather, for example, because Essential Energy's knowledge is *inferred* from the fire prone status of the land, the circumstances in which Essential Energy could face liability issues for wire strikes. The decision may also significantly expand the scope of liability issues, because a significant amount of land in NSW (and therefore, Essential Energy's network) is designated as fire prone. Given this and in order to demonstrate to insurers that there is or will be reasonable action to mitigate this risk, Essential Energy must consider what action is reasonable and appropriate to avoid or minimise the impact of further claims.

Essential Energy considers that, if the Government does not make a decision to pass the proposed legislative protection, it will then be both justifiable to preserve commercially acceptable insurance terms and efficient to invest resources in undertaking a feasibility study to develop a Risk Register prioritising assets where prudent action is necessary to mitigate the risk of line strike in order to reduce exposure to liability and protect the business's competitive position relative to the purchase of commercial insurance on a competitive basis.



### 4.3 Definitions of nominated pass through events

The AER accepted Essential Energy's nomination of insurance cap event, terrorism event and natural disaster event as pass through events. As noted above, Essential Energy accepts this decision.

In accepting these events as pass through events, the AER has amended the definitions of these events as proposed in the substantive proposal. The AER amended the definitions to include the assessment factors that the AER will have regard to when assessing a claim for pass through.

Essential Energy notes its proposed definitions of insurance cap event and natural disaster event in the substantive proposal also included factors for assessing these pass through events. Essential adopted these definitions simply to be consistent with the AER's definitions for these events approved in its previous determinations.

We have given further consideration to the inclusion of assessment factors within the relevant definitions and on further reflection we do not agree that these assessment factors should be included in the definitions.

This is because these factors are not actually relevant to defining events but rather are relevant to other aspects of the AER's assessment of pass through events. These other aspects relate to (a) the AER's assessment of the approved pass through amounts under 6.6.1 (d) or 6.6.1 (g) and (b) the nominated pass through events considerations. We note that the nominated pass through events considerations are only relevant as criteria for the AER's draft decision on whether to accept Essential Energy's nominated events as pass through events.

Essential Energy notes that defining the events nominated to be pass through events is necessary to ensure an appropriate description of the event is captured upfront, so that when the event has occurred (and the DNSP in its application must be able to demonstrate the event, as defined beforehand, has occurred), the pass through application and assessment process can be triggered. The occurrence of an approved nominated pass through event itself does not automatically mean the DNSP can pass through the costs to customers. The DNSP must demonstrate, and the AER must determine, that:

- a) A positive change event has occurred – that is the pass through event has resulted in material increase in costs.
- b) If the AER is satisfied that a positive change event has occurred, the approved pass through amounts, based on the factors in clause 6.6.1(j) of the Rules.

Inclusion of the factors in the definition of the event is also inconsistent with four pre-defined pass through events under the Rules. Chapter 10 of the Rules defines these four events (regulatory change event, service standard event, tax change event and retailer insolvency event) and none of the definitions include assessment factors.

For all of these reasons Essential Energy submits that assessment factors should be excluded from the definition and we have revised our proposed definitions accordingly. Our more detailed analysis of the AER's proposed definitions and our reasoning and justification in relation to the individual definitions is set out below.

The AER's amended definition includes:

For insurance cap event:

*Note for the avoidance of doubt, in assessing insurance cap event cost pass through application under rule 6.6.1(j), the AER will have regard to:*

- i. The insurance policy for the event; and*
- ii. The level of insurance that an efficient and prudent NSP would obtain in respect of the event*
- iii. The extent to which a prudent provider could reasonably mitigate the impact of the event.*



For natural disaster event:

*Note: In assessing a natural disaster event pass through application, the AER will have regard to, amongst other things:*

*Whether Essential Energy has insurance against the event:*

- i. The level of insurance that an efficient and prudent NSP would obtain in respect of the event.*
- ii. Whether a relevant government authority has made a declaration that a natural disaster has occurred; and*
- iii. The extent to which a prudent NSP could reasonably mitigate the impact of the event.*

For terrorism event:

*In assessing a terrorism event pass through application, the AER will have regard to, amongst other things:*

*Whether Essential Energy has insurance against the event:*

- i. The level of insurance that an efficient and prudent NSP would obtain in respect of the event.*
- ii. Whether a declaration has been made by a relevant government authority that a terrorism event has occurred*
- iii. The extent to which a prudent NSP could reasonably mitigate the impact of the event.*

Essential Energy's considers these parts of the definitions are unnecessary as they do not define the events themselves, but rather they are factors that go to the assessment of the cost impact of the event or the assessment of whether the event proposed by the NSP should be accepted by the AER as pass through events in its determination. These parts of the AER's amended definitions are already covered in various provisions of the Rules dealing with assessment of the costs to be passed through or the acceptance of the event as a pass through event.

- > Under clause 6.6.1(c)(6) of the Rules, an NSP must include in its pass through application evidence of (a) the actual and likely increase in costs and (b) that such costs occur solely as a consequence of a positive change event. Satisfying these requirements would require the NSP to provide details of the insurance policies and the level of insurance.
- > Clause 6.6.1(j)(3), (5) and (7) respectively state that:
  - *(3) In case of a positive change event, the efficiency of the DNSP's decisions and actions in relation to the risk of the positive change event, including whether the DNSP has failed to take any action that could reasonably be taken to reduce the magnitude of the eligible pass through amount in respect of that positive change event and whether the DNSP has taken or omitted to take any action where such action or omission has increased the magnitude of the amount in respect of that positive change event.*
  - *(5) the need to ensure that the DNSP only recovers any actual or likely increment in costs under this paragraph (j) to the extent that such increment is solely as a consequence of a pass through event.*
  - *(7) whether the cost of the pass through event have already been factored into the calculation of the DNSP's annual revenue requirement for the regulatory control period in which the pass through event occurred or will be factored into the calculation of the DNSP's annual revenue requirement for a subsequent regulatory control period.*

In making a determination on the approved pass through amounts, the AER must take into account the above provisions (and others specified under 6.6.1(j)). This exercise would entail the consideration of:

- i. the insurance policy for the event; and*

- ii. *the level of insurance that an efficient and prudent NSP would obtain in respect of the event*
- iii. *the extent to which a prudent provider could reasonably mitigate the impact of the event.*

In addition, the nominated pass through event considerations in the Rules also require the following consideration as to whether the AER approves the events nominated by a DNSP as a pass through event:

*(c) whether a prudent service provider could reasonably prevent an event of that nature or type from occurring or substantially mitigate the cost impact of such an event (emphasis added).*

For the above reasons, Essential Energy considers it unnecessary to include these parts of the AER's definition in either the definition of insurance cap event, natural disaster event and terrorism event or as factors in the assessment of a pass through application. This is simply because these matters are neither needed to define the events nor needed as assessment factors as they have already been covered in the relevant provision of the Rules.

The AER also amended Essential Energy's proposed definition of natural disaster event to include a caveat:

*Provided the fire, flood or other event was not a consequence of the acts or omissions of the service provider.*

Essential Energy considers that this caveat is not necessary in defining the event. This caveat goes to the assessment of the approved pass through amounts and is encapsulated within the Rules provision 6.6.1(j)(3). This is a factor the AER must take into account in determining the approved pass through amounts. It may well be the case that the approved pass through amount proposed by a NSP is significantly reduced because of its acts or omission.

This fact, however, does not mean that a natural disaster event has not occurred (a definition issue). Moreover, the caveat is a departure from the AER's previous determination and Essential Energy considers there is no sound basis for such departure.

The AER also added to the definition of natural disaster event an element - 'whether a relevant government authority has made a declaration that a natural disaster event has occurred'. Essential Energy does not support this additional element as it does not enhance or further clarify the definitional boundaries of a 'natural disaster event'. A major fire could occur within Ausgrid's network area that materially increases the costs to Essential Energy of providing direct control services and yet it may not be declared by a relevant government authority as a natural disaster event. Essential Energy has no control or influence over the decision to be made by a relevant government authority and considers that it should not be limited in the business's ability to pass through the costs of a natural disaster event simply because it has not been declared as a natural disaster event by a relevant government authority (despite all other elements for the pass through of costs under the Rules being satisfied).

For similar reasons, Essential Energy does not concur with the inclusion of the additional element 'whether a declaration has been made by a relevant government authority that a terrorism event has occurred'. The reference to a relevant government authority is too vague and may lead to unintended exclusion of events which are in fact a terrorism event under the definition. It is not clear what may be regarded as 'relevant'. Some legislative provisions may be directed at triggering insurance caps or other types of relief and are not concerned with whether there has been a terrorism event as such, but a certain type of event or an event with certain insurance consequences.

#### **4.3.1 Revised definitions**

Following are Essential Energy's revised definitions for insurance cap event, terrorism event, natural disaster event and insurer's credit risk event. For avoidance of doubt, Essential Energy accepts the AER's draft decision that insurance cap event, terrorism event and natural disaster event are pass through events for the 2015-19 regulatory period.

Essential Energy has only revised the definitions of these events in response to the AER's draft decision and reasons. In relation to insurer's credit risk event, the business has not accepted the AER's draft decision to reject this event as a pass through event. The revised proposal includes this event as a nominated pass through event.

#### 4.3.1.1 Insurance cap

An insurance cap event occurs if:

*Essential Energy makes a claim or claims and receives the benefit of a payment or payments under a relevant insurance policy,*

*Essential Energy incurs costs beyond the relevant policy limit, and*

*the costs beyond the relevant policy limit materially increase the costs to Essential Energy in providing direct control services.*

For this insurance cap event:

*the relevant policy limit is the greater of:*

- *Essential Energy's actual policy limit at the time of the event that gives, or would have given rise to a claim, and*
- *the policy limit that is explicitly or implicitly commensurate with the allowance for insurance premiums that is included in the forecast operating expenditure allowance approved in the AER's final decision for the regulatory control period in which the insurance policy is issued.*

*A relevant insurance policy is an insurance policy held during the 2015-19 regulatory control period or a previous regulatory control period in which Essential Energy was regulated.*

#### 4.3.1.2 Natural disaster

A natural disaster event is defined as:

*Any major fire, flood, earthquake or other natural disaster beyond the reasonable control of Essential Energy that occurs during the 2015-19 regulatory control period and materially increases the costs to Essential Energy in providing direct control services.*

*The term 'major' in the above paragraph means an event that is serious and significant. It does not mean material as that term is defined in the Rules (that is 1 per cent of the DNSP's annual revenue requirement for that regulatory year).*

#### 4.3.1.3 Terrorism event

A terrorism event is defined as:

*An act (including, but not limited to, the use of force or violence or the threat of force or violence) of any person or group of persons (whether acting alone or on behalf of or in connection with any organisation or government), which from its nature or context is done for, or in connection with, political, religious, ideological, ethnic or similar purposes or reasons (including the intention to influence or intimidate any government and/or put the public, or any section of the public, in fear) and which materially increases the costs to Essential Energy in providing direct control services.*

#### 4.3.1.4 Insurer credit risk event

For completeness, Essential Energy also includes below the definition of insurer's credit risk event it considers the AER should accept in its final decision (both in terms of the event being a nominated pass through event and the corresponding definition).

*The insolvency of a nominated insurer of Essential Energy, as a result of which Essential Energy:*

*i. incurs materially higher or lower costs for insurance premiums than those allowed for in its Distribution Determination; or*

*ii. in respect of a claim for a risk that would have been insured by Essential Energy's insurer's, is subject to materially higher or lower claim limit or a materially higher or lower deductible than would have applied under that policy.*

## 4.4 Application to alternative control services

Essential Energy's substantive proposal also considers the pass through provisions of the Rules to apply to alternative control services. Reasons in support of this proposal were outlined in section 10 of Attachment 4.6. It is noted the Essential Energy proposed application of pass through provisions is consistent with previous determinations by the AER.

The AER's draft decision appears silent on this aspect of Essential Energy's proposal. Essential asks that the AER makes a decision consistent with its proposal and its determinations for other network service providers in its final determination for Essential Energy.

## 5. CONCLUSION

In developing the Essential Energy Regulatory Proposal (2014-2019), Essential Energy submitted Attachments 4.6 and 4.7 in support of its substantive regulatory proposal on nominated pass through events. These attachments remain Essential Energy's regulatory proposal on pass through events except for the definitions of pass through events replaced by those outlined within this attachment.

In summary, Essential Energy:

- > agrees with the AER's draft decision on nominated pass through events including insurance cap event, natural disaster event and terrorism event, however the AER's modifications to Essential's proposed definitions are not accepted
- > does not accept the AER's draft decision on the insurer's credit risk event, due to the lack of consideration given to Essential's risk management methodology
- > does not accept the AER's draft decision on the aviation hazards event, given the potential significant costs Essential Energy will face if legislative protection is not enabled
- > requests the AER make a decision with our substantive regulatory proposal and its determinations for other network service providers in its final determination for Essential Energy.