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Ms Claire Preston  
Australian Energy Regulator  
GPO Box 520  
Melbourne VIC 3001

E: [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au)

Dear Claire

### **Feedback on the 2020 Draft Annual Benchmarking Report for Electricity Distribution Network Service Providers**

Essential Energy appreciates the opportunity to comment on the Draft 2020 Distribution Network Service Provider Benchmarking report (Benchmarking Report).

The Australian Energy Regulator (AER) has adopted an incremental approach to improving benchmarking of which Essential Energy supports. In this respect, the incremental improvements to refine and improve the assessment of relevant operating environment factors over the last 12 months is a positive step, though we appreciate that not all stakeholders will be supportive of all these changes.

#### **Corrected non-reliability output weights**

Essential Energy wholeheartedly supports the change in output weights proposed in this year's Benchmarking Report. We agree that the reduction in weight placed on both customer numbers and energy throughput, offset by increases in the weights placed on circuit length and ratcheted maximum demand, more closely reflects the cost drivers for distribution networks from both an economic and engineering perspective.

Given the largely fixed costs of operating and maintaining the physical assets of a distribution network, rural networks were consistently disadvantaged under the previous combined weighting of more than 42 percent placed on customer numbers and energy throughput. The reduction in the combined weightings for these outputs to closer to 19 percent and uplift to the weightings for circuit length and ratcheted maximum demand to a combined amount of about 73 percent provides a better representation of the cost drivers for Essential Energy.

#### **Value of Customer Reliability (VCR) changes**

Given the distortion that high VCR-based output weights can create in the Total Factor Productivity results, Essential Energy fully supports Economic Insights intention to scope a link to capping the weight applied to the reliability output with the STPIS parameters<sup>1</sup>. Robust benchmarking should not allow for perverse outcomes and create distortions. We look forward to seeing this improvement, which has already been undertaken for transmission networks, in the 2021 Benchmarking Report.

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<sup>1</sup> Economic Benchmarking Results for the Australian Energy Regulator's 2020 DNSP Annual Benchmarking Report, Economic Insights, October 2020, p.12

### Operating Environment Factors (OEFs)

Failing to properly control for OEFs will undermine the objective of the AER's benchmarking as the true scope for efficiency improvements will not be apparent. Whilst we appreciate that competing priorities have resulted in limited progress in advancing OEFs over the last 12 months, this must be seen as a priority area for the AER and distribution networks over the coming year if incremental improvements are to continue to be achieved.

Essential Energy reiterates our desire to participate in discussions with the AER and other distribution networks to improve the robustness of the AER's benchmarking and to ensure comparability in OEF assessment. We recommend that an industry working group is formed to:

- > test the robustness of existing OEFs;
- > identify other equally significant OEFs that have yet to be accounted for; and
- > determine and agree the definition for the data variables that would best represent those OEFs.

The specific OEFs we would like to recommend the AER consult and collect appropriate data on are detailed in the Attachment to this letter.

### Future changes to benchmarking

Given the quite significant changes to results and on-going refinements to the benchmarking model, Essential Energy maintains concerns with the limitations of the model and therefore agrees with maintaining the benchmark comparison score at 0.75 (adjusted for OEFs).

At a minimum, the comparison score should not be adjusted until stakeholders are confident that:

- > all reasonable OEFs are adequately accounted for in the AER's benchmarking;
- > the implication of cost allocation and capitalisation differences on the benchmarking results is considered and understood; and
- > the output specifications are adjusted to account for the impact of Distributed Energy Resources (DER). It is worth noting that the Independent Pricing and Regulatory Tribunal of NSW (IPART) has recently released its draft report on distribution reliability standards which recommends the introduction of new DER reporting standards. Essential Energy encourages engagement between the AER and IPART to ensure that inconsistent or duplicative reporting is avoided.

### Other suggestions

The Attachment to this letter includes additional feedback around wording changes and visual enhancements to improve the stakeholder interpretation of some aspects of the Benchmarking Report.

Should you have any questions or concerns about this submission, please contact [REDACTED]

Yours sincerely



Chantelle Bramley  
**General Manager Strategy, Regulation and Corporate Affairs**

## Attachment

### Extending the work on OEFs

We would like to see the AER consult on the following OEFs to either improve their existing assessment or include them in the 2021 Benchmarking Report. Indicative data and more detailed explanations around many of these OEFs can be found in the Frontier Economics report that was submitted as part of Essential Energy's 2019-24 Regulatory Proposal (see attachment 13.1 [here](#)).

#### Subtransmission

We would appreciate an industry discussion around the adequacy of the existing quantification of the subtransmission OEF. Essential Energy is not convinced that the existing Sapere Merz analysis gives adequate regard to the mix of subtransmission assets at different voltage levels. In particular:

- > the length of circuit by feeder configuration, which is a key driver of fault and emergency costs; and
- > the number of feeders by feeder configuration, given there are higher costs associated with operating at multiple voltages, owing to multiple tooling requirements, increased complexity and the need for specialised skills at each different voltage level.

#### Network accessibility

This OEF has been included in the Benchmarking Report for the first time, but has only been assessed and applied to Ergon Energy. The assessment should be expanded to include all networks. As the operator of Australia's largest rural distribution network, servicing NSW customers across all manner of terrain and climates, this OEF would similarly apply to Essential Energy and other networks for whom accessing a large portion of assets is difficult.

#### Vegetation Management

As one of the largest operating expenses for most distribution networks, the 2018 Sapere Merz Report highlighted this as a probable OEF candidate for a significant portion of distribution networks, including the reference firms<sup>2</sup>. Given its likely material influence on the reference point, and the associated OEF outcomes, particularly for those networks with the highest (or lowest) vegetation management expense as a proportion of total operating expense, establishing a means to assess this OEF should be a priority for the coming year.

#### Weather events

Only cyclones are considered as an OEF at present and are only applied to Queensland networks, despite the fact that the associated rainfall from these events does cause flooding in NSW.

Essential Energy reiterates that there are many other weather events that have yet to be considered in the OEF assessment and these cannot be adequately captured from the existing data on Major Event Days in the Regulatory Information Notices. As requested by Sapere Merz<sup>3</sup>, the [Frontier Economics](#) report that formed attachment 13.1 of our 2019-24 regulatory proposal provides positive evidence of the materiality of this as a potential OEF when lightning strikes, wind, heavy rain and floods and bushfire mitigation are each considered, especially for large footprint networks that necessarily cover a wide range of terrains and climates.

#### Fauna

Outages caused by fauna are outside the control of a network, but are a driver of operating costs. Indicative data for this OEF was also presented in the Frontier Economics report referred to above.

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<sup>2</sup> *Independent review of Operating Environment Factors used to adjust efficient operating expenditure for economic benchmarking*, Sapere Research Group and Merz Consulting, August 2018, p. 65.

<sup>3</sup> *Ibid*, p. 25

## Suggested wording and visual improvements to the Benchmarking Report

### On page 31 in the 'Total cost per customer' heading within section '5.2.1 Total cost PPIs'

- > The second sentence in the first paragraph says:

*"Customers numbers are one of the main outputs DNSPs provide."*

To ensure consistency with the change in output measure weightings in the Economic Insights model, we suggest this sentence is deleted. The next sentence appropriately captures the relevance of this measure, namely

*"The number of customers connected to the network is one of the factors that influences demand and the infrastructure required to meet that demand."*

- > The third sentence in the second paragraph requires the following addition (see bold text):

*"Both Ergon Energy and Essential Energy have a relatively higher total cost per customer compared to DNSPs with similar customer densities, including SA Power Networks, Powercor, AusNet and TasNetworks, **though customer density, which is an average of customers spread across the network, is not uniformly dispersed for these large scale networks.**"*

This provides context for the result and is similar to this sentence which is already included at the end of the '5.2.2 Cost Category PPIs', 'Emergency Response' section:

*"There may be higher costs associated with responding to emergencies in more customer dense networks due to the costs of managing congestion (e.g. closing roads and managing traffic)."*

To provide further context for this addition, Essential Energy suggests the inclusion of network maps, overlaid with customer density from the Australian Bureau of Statistics website, in the Benchmarking Report for the low customer density networks (see Essential Energy example below). We believe such pictures demonstrate to stakeholders the scale of network assets serving areas with very low customer density, thereby highlighting the relative economies of scale that can be achieved by the various networks to assist with interpreting the cost per customer measures.

