7 November 2014

Mr Matt Zema
Chief Executive Officer
Australian Energy Market Operator
GPO Box 2008
MELBOURNE VIC 3000

Dear Mr Zema

Value of customer reliability – Response to Application Guide Draft Report

ActewAGL Distribution (ActewAGL) welcomes the opportunity to respond to the Australian Energy Market Operator's (AEMO's) Draft Report on the application guide for its value of customer reliability (VCR) review (draft application guide).

ActewAGL views consumer research, including value estimates such as the VCR, as crucial to the process of moving towards customers' preferred balance between cost and reliability. It is for this reason that we commissioned two choice modelling studies conducted in the Australian Capital Territory (ACT) by NERA and ACNielsen in 2003 and by the Australian National University (ANU) in 2012. We therefore welcome finalisation of the AEMO review of VCR across the National Electricity Market (NEM).

ActewAGL noted in its response to the Directions Paper that AEMO was intending to estimate VCR at the NEM region level and that this approach would not fully capture local variations in preferences. We expressed the view that VCR estimates from targeted, local studies, such as those undertaken in the ACT, should supersede NEM region VCR estimates for network-specific applications.[1]

ActewAGL notes that the VCR estimates in the draft application guide are at the NEM region level as planned by AEMO. Consistent with the position in our response to the Directions Paper, we are therefore of the view that AEMO's VCR estimates should not be used for applications that are specific to distribution networks in the ACT. The extent of potential differences between local and NEM region estimates is highlighted by the fact that AEMO's VCR estimate for the New South Wales (NSW) NEM region of around $38/kWh (excluding direct connects) is significantly different to the estimate derived by ActewAGL for the ACT of around $67/kWh.[2]

[1] ActewAGL 2013, *Value of customer reliability – Response to Directions Paper*, 3 July, p2.
[2] ActewAGL 2014, *Regulatory Proposal for 2015-19 subsequent regulatory control period – Attachment F1 STPIS reliability incentive rates 2015-2019*, June.

ActewAGL notes that the draft application guide outlines an approach to estimating locational VCR by reweighting customer types.[3] While this approach goes some way towards capturing variation in VCR across areas, it does not capture the potentially significant variation in VCR within each customer type across areas within NEM regions. For example, a locational VCR for the ACT based on the AEMO study would use a NSW residential VCR of around $27/kWh, which is significantly different from the residential VCR derived by ActewAGL from the ANU study of around $40/kWh.

It does not appear possible to derive valid ACT-specific VCR estimates for each customer type from the AEMO data. For example, assuming the 304 respondents from the NSW NEM region in the AEMO residential survey were stratified across areas according to population, only around 15 respondents would be from the ACT.[4] Similarly, we estimate that the number of ACT business customers included in the AEMO sample is likely to be less than 21.[5] Given the number of parameters being estimated, VCR estimates derived from these sample sizes would be statistically insignificant.

There are reasons to expect that VCR would differ between ACT and NSW; for example, due to differences in climate and socioeconomic characteristics. The AEMO study found climate to be insignificant as a predictor of VCR in NSW, but the climate in the ACT is more extreme than the climate in the populated areas of NSW. The value of reliability in winter in the ACT is likely to be higher than in NSW, since winter temperatures in the ACT are more comparable with temperatures in Tasmania – a NEM region for which AEMO found a statistically significant preference for avoiding winter outages.[6] Energy demand in the ACT has historically peaked in winter, whereas energy demand in NSW peaks in summer. The value of reliability in summer in the ACT is also likely to be relatively high, since mean daily maximum temperatures in January are greater in the ACT than they are in Sydney.[7] With respect to socioeconomic characteristics, mean annual income and proportion of persons with post-school qualifications are higher in the ACT than in NSW ($60,987 versus $53,917 in 2012 dollars and 64.5 per cent versus 57.2 per cent, respectively).[8]

We would be keen to discuss these issues relating to the application of VCR estimates to distribution network planning, regulation and reliability standards in the ACT. Please contact Dr Ben McNair, Principal Economist, on (02) 6248 3386.

Yours sincerely

David Graham
Director Regulatory Affairs and Pricing

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[3] AEMO 2014, *VCR review – Application guide draft report for consultation*, October, pp11-12.
[4] Based on 2014 population estimates obtained from the Australian Bureau of Statistics (ABS) (Cat. No. 3101.0).
[5] Based on 2013 gross business numbers obtained from the ABS (Cat. No. 8165.0).
[6] AEMO 2014, *Value of customer reliability review Final Report*, September, p20.
[7] Based on mean historic temperatures taken for the airports at Sydney, Canberra and Launceston (which has a more severe winter than Hobart) using Bureau of Meteorology data.
[8] Based on ABS Data by Region 2012.