grid australia
BACKBONE OF THE NEM

17 October 2012

Mr Chris Pattas
General Manager, Network Operations and Development Branch
Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Via email: AERinquiry@aer.gov.au

Dear Chris

Draft Service Target Performance Incentive Scheme

Grid Australia appreciates the opportunity to provide feedback on the AER's September 2012 draft Service Target Performance Incentive Scheme (STPIS) for Transmission Network Service Providers, and accompanying explanatory statement.

Grid Australia also appreciates the AER's consultative approach on the review and considers that the draft decision reflects a substantially sound incentive scheme. However, Grid Australia proposes a number of changes to the draft scheme, in general to provide clarity or to take account of practicability matters in implementing the scheme.

On a separate matter, Grid Australia notes that the AEMC is currently consult on transitional arrangements for the Economic Regulation of Network Service Providers rule change. This submission proposes a way in which transitional arrangements may apply to the STPIS.

Grid Australia notes that there are a number of matters of detail to be resolved with implementation of the amended scheme and would appreciate the opportunity to discuss these further with the AER. If you would like to discuss any of the matters raised in the accompanying submission, please do not hesitate to contact Andrew Kingsmill on 02 9284 3149 or at andrew.kingsmill@transgrid.com.au.

Yours sincerely

Rainer Korte

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Chairman
Grid Australia Regulatory Managers Group

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Service Target Performance Incentive Scheme

Response to AER Draft Determination

October 2012

Powerlink QUEENSLAND | TransGrid | ElectraNet electricity transmission | TRANSEND | SP AusNet A member of Singapore Power Group

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1. Introduction

In its September 2012 draft Service Target Performance Incentive Scheme (STPIS) for electricity Transmission Network Service Providers (TNSPs) and explanatory statement, the Australian Energy Regulator (AER) has proposed changes to the existing STPIS which are aimed at increasing the effectiveness of the scheme for the benefit of consumers.

Grid Australia appreciates the AER's consultative approach with a range of market participants on the review of the scheme, and considers that the draft decision reflects a substantially sound incentive scheme that can achieve the scheme's objectives and principles in Clause 6A.7.4(b) of the National Electricity Rules.

Grid Australia proposes a number of minor changes to the draft scheme, in general, to provide clarity or to take account of practicability matters in implementing the scheme.

On a separate but related matter, Grid Australia notes that the AEMC is currently undertaking consultation on transitional arrangements for the Economic Regulation of Network Service Providers rule change. This submission proposes a way in which transitional arrangements may apply to the STPIS.

Grid Australia is also willing to provide further information on TNSPs' experience with the STPIS on request, or to assist the review in any other way.

2. Service Component

Grid Australia observes that the proposed change to the service component creates substantial overlap of unplanned outages between sub-parameters to the extent that unplanned outages may be counted in up to five sub-parameters. Grid Australia suggests the service component could be further simplified while still providing a similar incentive.

2.1 Average Circuit Outage Rate

With regard to the inclusion of reactive plant in this parameter, Grid Australia requests the AER consider the use of a seasonal window for the application of this parameter to each TNSP. The availability of certain reactive plant may not be critical at certain times of the year, such as capacitor banks at times of moderate demand. In such circumstances it would not be efficient for TNSPs to incur additional costs, such as overtime, to restore plant that is not urgently required. The use of a seasonal window would appropriately incentivise TNSPs to respond to fault outages during times when the use of reactive plant is most highly valued by customers.

To achieve this outcome, Grid Australia proposes the following addition to the parameter definition: "Unplanned Outage Events of certain reactive plant under the reactive plant sub-parameter are only required to be measured during defined times that the plant is required for use in managing the network. TNSPs are to propose and substantiate in their Revenue Proposals, times when reactive plant sub-parameters should apply to certain reactive plant."

Grid Australia also suggests that, given the different relative importance of reactive plant in different networks, TNSPs have the ability to propose alternative weightings for this sub-parameter in their revenue proposals to better reflect the value customers place on availability of reactive plant.

2.2 Loss of Supply Event Frequency

Grid Australia supports the AER's proposal to retain TNSP-specific x and y system minutes that recognise that physical characteristics of networks such as geography, layout and topography and contribute to differences in the performance of individual networks. Such an approach supports the strength of the incentive and will most effectively influence TNSP behaviour.

2.3 Average Outage Duration

The draft scheme proposes a change in the definition of the average outage duration parameter, from including all unplanned outages to only outages that interrupt supply to customers. This dramatically reduces the number of qualifying outage events. As a result, Grid Australia considers that this parameter is likely to be volatile, which could weaken the incentive performance improvement under the scheme.

Grid Australia also notes that the parameter definition allows the impact of events to be capped at seven days. While the period of seven days is sensible if the parameter definition includes all unplanned outages, it is not sensible for outages that interrupt supply to customers. Grid Australia proposes that a much smaller cap is required given the change of definition of the parameter.

Grid Australia questions the value of sub-parameters for single and multi-circuit outages. The distinction between the two effectively applies the incentive across smaller data sets, which increases the volatility of the parameter without improving the strength or nature of the incentive. Grid Australia therefore recommends retention of a single average outage duration parameter, with no sub-parameters. If the AER does not support this recommendation, Grid Australia considers that there are a number of definitional issues to be resolved with respect to the proposed sub-parameters.

2.4 Proper Operation of Equipment

Grid Australia considers there is insufficient benefit from incentives or incentive reporting relating *specifically* to protection and control systems. Better incentives on TNSPs are achieved by other parameters under the service component, with businesses prioritising effort to deliver service outcomes.

Protection and control systems are designed with duplication to withstand the failure of a single component. This is both good electricity industry practice, and required by the National Electricity Rules. As such, if in future the Proper Operation of Equipment parameter was to have a non-zero weighting, Grid Australia would encourage the AER to measure failure of the system rather than individual components.

3. Market Impact Component

Grid Australia supports the AER's proposed change to the method for setting targets and measuring performance against the market impact component. The introduction of rolling averages addresses the concern of the design of the existing parameter that may incentivise outage sharing. The retention of an asymmetric scheme is appropriate as it provides an incentive for TNSPs to incur expenditure to respond to the scheme whilst not creating a perverse incentive where market impacts can be minimised but not completely avoided. It also allows TNSPs to undertake works on the parts of the network that are most likely to incur constraints, where there are drivers such as net market benefits, without the risk of incurring a net penalty under the incentive as a result.

Grid Australia proposes two changes to Section 4.2 of the scheme that describes this parameter.

Paragraph 4.2 (a) requires each TNSP to submit in its revenue proposal a performance target for the market impact parameter. As the performance target will be set using a rolling average based on future years at the time of submitting the revenue proposal, it will not be possible for a TNSP to submit performance targets in a revenue proposal. Grid Australia proposes that the AER amend paragraph 4.2 (a) to account for this.

Paragraph 4.2 (d) specifies matters for which the proposed performance target may be reasonably adjusted. Grid Australia proposes the addition of a fourth matter, namely, "the acquisition or disposal of assets for which constraints exist in the market systems". This matter was raised during Powerlink's 2013-2017 revenue determination process. Specifically, Powerlink requested "an offset for dispatch intervals affected by network outages on assets it intends to acquire prior to the commencement of the next regulatory control period"[1]. This proposal was rejected by

[1] AER Draft decision | *Powerlink revenue proposal 2012-13 to 2016-17*– page 17.

the AER on the grounds that "it is not allowed under the market impact component."[2] Grid Australia considers that as targets under the MIC are set based on historical performance, the targets for incentivised assets should be calculated using those same assets.

4. Network Transfer Capability Component

Grid Australia supports the introduction of the Network Transfer Capability component to the scheme. This component aligns well with the requirements of the scheme in Clause 6A.7.4 of the National Electricity Rules and the objectives of the scheme.

4.1 Measurement of improvement

Grid Australia considers that the design of the network capability component proposed by the AER may be overly complex. Any simplification to scheme design that can achieve the stated outcomes should therefore be considered. Additionally, provision of worked examples would assist to demonstrate the scheme's intended operation.

4.2 Design and implementation

Grid Australia seeks further clarity on the implementation of the Network Capability Incentive component, as follows.

The proposed component involves the establishment of a Network Capability Improvement Parameter Action Plan (NCIPAP) at the time of the revenue proposal and determination. However, during a regulatory control period circumstances may change such that the original plan is no longer applicable or relevant; e.g. in recent times the closure of some major industrial loads and connection of new generation. Grid Australia proposes that the parameter provide for TNSPs to amend the NCIPAP annually where this is prudent, with an approval process for amendments.

Grid Australia also recommends provision of a worked example of the component to provide helpful guidance to TNSPs and other stakeholders in its initial implementation.

5. Parameters and Weightings

In principle, Grid Australia supports unified application of parameters to TNSPs. This reflects that the needs of all consumers across the NEM are broadly similar. However, there may be some circumstances in which particular parameters or sub-parameters apply differently to individual TNSPs.

[2] AER Draft decision | *Powerlink revenue proposal 2012-13 to 2016-17*– page 295.

Grid Australia therefore recommends that if the STPIS guideline includes standard weightings, it also permits TNSPs to propose alternative weightings in their Revenue Proposals, which the AER can accept where justified.

With respect to the operation of weightings, the draft STPIS states that "where there is insufficient accurate and reliable data available for determining the values of a parameter or sub-parameters applying to a TNSP under this service component, the AER may reduce the weighting for that parameter or sub-parameter to zero." Grid Australia seeks clarification as to whether the reduction of a sub-parameter weighting to zero means that the total weighting of the parameter is reduced by the weighting of the sub parameter, or the weighting of the sub-parameter is distributed over the remaining sub-parameters such that the total parameter weighting remains the same.

6. Exclusions

6.1 Standardisation across TNSPs

The draft decision standardises exclusions across TNSPs for individual sub parameters. Grid Australia supports the introduction of common exclusions while noting that difference in TNSP exclusions have typically been due to historic data recording practices. However, Grid Australia notes that such a move may mean that historic data may not be presented on a comparable basis to future data.

The following exclusions are common across all components:

1. Outages on assets that are not providing *prescribed transmission services*
2. Outages shown to be primarily caused or initiated by a fault or other event on a third party system – e.g. inter-trip signal, generator outage, customer installation
3. Any outages caused by a direction from *fire (emergency)* services or AEMO
4. Force majeure events
5. Transient interruptions (less than one minute duration)

Grid Australia would like to point out that TNSPs may be required to operate the network due to directions from any emergency service, not just fire. GA therefore proposes that exclusion number 3 above be amended to refer to all emergency services.

6.2 Clarifications to the definition of unplanned outages

Grid Australia proposes that the definition of the average circuit outage rate parameter clarify, for the avoidance of doubt, that rescheduled planned outages are not included in the parameter. When a planned outage is rescheduled it may appear

in the Network Outage System as having less than 24 hours notice. However, it is not a forced outage. This allows TNSPs to reschedule outages prudently where required, such as when work is delayed due to weather or outages are rescheduled due to market impact.

6.3 Force Majeure

Grid Australia supports the harmonisation of force majeure events across TNSPs and views the common definition provided in the draft STPIS as encompassing the differences in TNSPs, particularly in the areas of recording of data, network susceptibility and operation. Grid Australia supports the AER's decision to use reporting requirements to verify the application of force majeure events rather than the application of a cap.

7. Timing of Performance

The setting of parameters and reporting of parameters for STPIS is based on the calendar year. For the calendar year that overlaps the end of one regulatory period and the beginning of the next regulatory period the current and draft STPIS requires TNSPs to derive targets and report performance separately for each 6 month period. Grid Australia suggests that the complexity of the STPIS could be reduced by extending the target, caps and collars from the first six month period for the full overlapping year and commencing new targets, caps and collars in the first full calendar year of a regulatory period. However, this issue would require further consideration by the AER and TNSPs to ensure that the incentives remain consistent across regulatory periods, given that the expenditure allowances may be set on a different basis.

8. Incentives at the Performance Frontier

In the existing STPIS, paragraph 3.3 (j) permits a TNSP to propose an alternative methodology for determining performance targets where it is operating at the performance frontier on a parameter. This paragraph has been removed from the revised STPIS with no explanation in the explanatory statement.

Grid Australia considers that it is still relevant for the scheme to provide for alternative methodologies to be used when a TNSP is operating at the performance frontier. This is because the statistical approach that has previously been used to set the cap and collar in the past assumes a normal distribution, whereas performance results do not necessarily follow a normal distribution. Further, the use of only five historical data points is insufficient to properly create a distribution. Thus, when a TNSP is at the performance frontier, this may result in a non-sensible cap (for example, greater than 100%).

Grid Australia does not consider that a method should be prescribed in the scheme, but rather than the option be available for TNSPs to propose in their revenue proposals if they can substantiate performance at the performance frontier. Grid Australia proposes the following paragraph for inclusion in section 3.2 of the revised scheme:

Where the performance history described in clause 3.2 (g) is available, the AER may approve a *performance target, cap and collar* based on an alternative methodology proposed by the TNSP if it is satisfied that:

1. the methodology is reasonable
2. the TNSP's performance as measured by the relevant parameter has been consistently very high over at least every calendar year of the previous five years
3. it is unlikely that the TNSP will be able to improve its performance during the next regulatory control period (or any potential improvement would be marginal), and
4. the proposed methodology is consistent with the objectives in clause 1.4 of the scheme.

Grid Australia also proposes that paragraph 3.2 (e) be amended to insert "Subject to clause 3.2 (ref)" to refer to the additional paragraph.

9. Review Process

Grid Australia supports the AER's decision to conduct regular reviews of the STPIS, thus ensuring the incentive responds to developments in the NEM. Grid Australia supports the use of defined review cycles using the *transmission consultation procedures*. Grid Australia proposes a five yearly review cycle, which aligns with the lengths of most regulatory control periods, however would like to reinforce the importance of allowing TNSPs to propose changes to the scheme at times other than the AER's STPIS review cycle.

The ability for TNSPs to propose changes does not necessarily create divergence in a scheme; it is the design of the scheme that drives divergence or convergence. The benefits of allowing TNSPs to propose changes to the scheme exist regardless of the extent of harmonisation of the scheme across the TNSPs. Any proposed changes must be considered by the AER and would only be accepted if they aligned with the scheme's objectives. Therefore, the ability to propose changes should be seen as encouraging innovation rather than differences between TNSPs.

10. Information Gathering

Grid Australia does not consider that the use of Regulatory Information Notices (RINs) is required for the operation of the STPIS, but that sufficient prescription of

information requirements in the scheme itself is more appropriate. The AER's proposed use of Regulatory Information Notices for gathering data may increase the evidentiary burden of data compliance on TNSPs, whereas the existing regime of clear guidelines and systematic audits is more efficient and has not proven to be problematic. There would appear no justification for going beyond this.

11. Early implementation of the Network Capability Component

In April of 2009 Grid Australia proposed a Rule change to introduce transitional provisions to the Rules to enable TNSPs to apply to become subject to the Market Impact Component of the STPIS earlier than was provided for under the Rules. The AEMC subsequently allowed an amended form of this Rule change as it was considered to contribute to the achievement of the National Electricity Objective.

Grid Australia considers that the early implementation of the proposed Network Capability Component of the STPIS is also likely to contribute to the achievement of the National Electricity Objective and will consider lodging a Rule change proposal to allow individual TNSPs to seek the early application of this new component.

12. Transition to New Economic Regulation Rules

The Australian Energy Market Commission is currently deciding on transitional arrangements to apply to the Economic Regulation of NSPs Rule change. Grid Australia recommends that the STPIS continue to apply to TNSPs during the transitional arrangements. Grid Australia proposes that the STPIS be applied based on principles such as the following:

1. as the service component values are set in the revenue determination, the existing service component could continue for year 1 of the transitional regulatory period with existing parameters, weightings, targets, caps and collars for the first year of the upcoming regulatory period, and the new service component apply from year 2;

2. the new market impact component to apply from the start of the upcoming regulatory period, as its targets are based on rolling average periods and are not set in the revenue determination; and

3. the new network capability component to apply from the start of the regulatory period, with the network capability improvement parameter action plan submitted and approved prior to the upcoming regulatory period, which could be ratified in the revenue determination if required to formalise the incentive.

The transition to the service component could be further simplified by changing the timing to the start of a calendar year, rather than the start of year 2 of the transitional regulatory period.

If the AER requires, TNSPs could also start recording data against new service component measures, including reporting only parameters, from year 1 of the transitional period.

However, such a transition would need to ensure that the incentives remain appropriate and consistent.