Australian Energy Regulator

Comments on the

AER Distribution Guidelines

**Service Target Performance Incentive Scheme
STPIS**

by

The Major Energy Users Inc

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Executive Summary

The Major Energy Users Inc. (MEU) welcomes the opportunity to provide its comments to the AER's proposed distribution guidelines on the 'Service Target Performance Incentive Scheme'.

Major energy users, particularly in certain States (such as New South Wales) have experienced poor levels of service performance from distribution businesses for a number of years. Frequency interruptions and voltage dips have become more frequent.

In other States, such as Victoria, service performance of distribution businesses have been improving, spurred on by the introduction of a 'best practice' service performance scheme by the jurisdictional regulator.

The AER is, accordingly, urged to put into place guidelines for a 'best practice' service performance scheme. Not to do so, will consign consumers, especially in certain NEM regions, to continued poor service performance standards and reliability. These add considerable costs to industrial operations.

The MEU has provided, below, comments on each of the issues raised by the AER.

1.   Introduction

1.1 The MEU

The Major Energy Users (MEU), which comprises some 20 major energy using companies in NSW, Victoria, SA, Tasmania and Queensland, welcomes the opportunity to provide comments on the AER's draft performance incentive scheme (STPIS). In particular, the submission represents the views of the Energy Markets Reform Forum (NSW), Energy Consumers Coalition of South Australia, the Energy Users Coalition of Victoria, the A3P and the Cement Industry Federation.

Analysis of the electricity usage by the members of MEU shows that between them they consume about 5% of the electricity generated in the NEM. Many of the members are located in regional parts of Australia, some distance from the regional nodes. As such, they are highly dependent on the transmission network to deliver efficiently the electricity so essential to their operations. Being regionally located, those members also have an obligation to represent the views of their local suppliers and of the regionally based workforce on which the companies are dependent. With this in mind, the members require their views to not only represent the views of large energy users but also those of smaller power usage facilities and residences located near to their regional operations.

The companies represented by the MEU (and their suppliers) have identified that they have an interest in the **cost** of the energy networks services as this comprise a large cost element in their electricity and gas bills.

Although electricity is an essential source of energy required by each member company in order to maintain operations, a failure in the supply of electricity or gas effectively will cause every business affected to cease production, and members' experiences are no different. Thus the **reliable supply** of electricity and gas is an essential element of each member's business operations.

With the introduction of highly sensitive equipment required to maintain operations at the highest level of productivity, the **quality** of energy supplies has become increasingly important with the focus on the performance of the distribution businesses because they control the quality of electricity and gas delivered. Variation of electricity voltage (especially voltage sags, momentary interruptions, and transients) and gas pressure by even small amounts now has the ability to shut down critical elements of many production processes. Thus member companies have become increasingly more dependent on the quality of electricity and gas services supplied.

Each of the businesses represented here has invested considerable capital in establishing their operations and in order that they can recover the capital costs invested, long-term **sustainability** of energy supplies is required. If sustainable supplies of energy are not available into the future these investments will have little value.

Accordingly, MEU is keen to address the issues that impact on the **cost, reliability, quality** and the long term **sustainability** of their gas and electricity supplies.

1.2 Distribution services

The members of MEU have identified that distribution plays an important role in the electricity market and equally, consumers recognise that the cost of providing the distribution system is a significant element of the total cost of delivered electricity. Of all the individual elements of the electricity supply chain, distribution is the element that has the largest impact on the quality of supply. Distribution has the longest and most frequent outage time, it provides the greatest exposure to voltage variation (spikes and dips), and is the source of the "hash" (harmonics and the like) which affects consumers sensitive monitoring and control equipment. Overall, the reliability of the electricity supply is most impacted by the performance of the distribution businesses

It is the performance of distribution businesses (DBs) that have the greatest impact on consumers, both from a reliability viewpoint, from a quality viewpoint and in regard to personal interaction.

The jurisdictional regulators have devoted some attention to ensuring that the DBs do meet their part of the regulatory bargain – that the cost of the service provided matches the quality of the service expected for the price awarded by regulators.

In Victoria and SA where the distribution businesses have been privatized, the jurisdictional regulators have expended considerable effort into developing a performance scheme that rewards high quality service and penalizes low quality service by the DBs. The regulators of regions where the DBs are government owned have been less diligent in establishing meaningful performance measures and as a result consumers in those regions have tended to have a lower standard of service than do consumers where the DBs are privately owned.

With this in mind, the MEU recommends to the AER that it uses the work of the jurisdictional regulators which have the most advanced service standard measures and performance rewards as the basis for the AER guidelines for its STPIS. Additionally the AER should examine in detail the manner by which the jurisdictional regulators reached the current level of monitoring and performance.
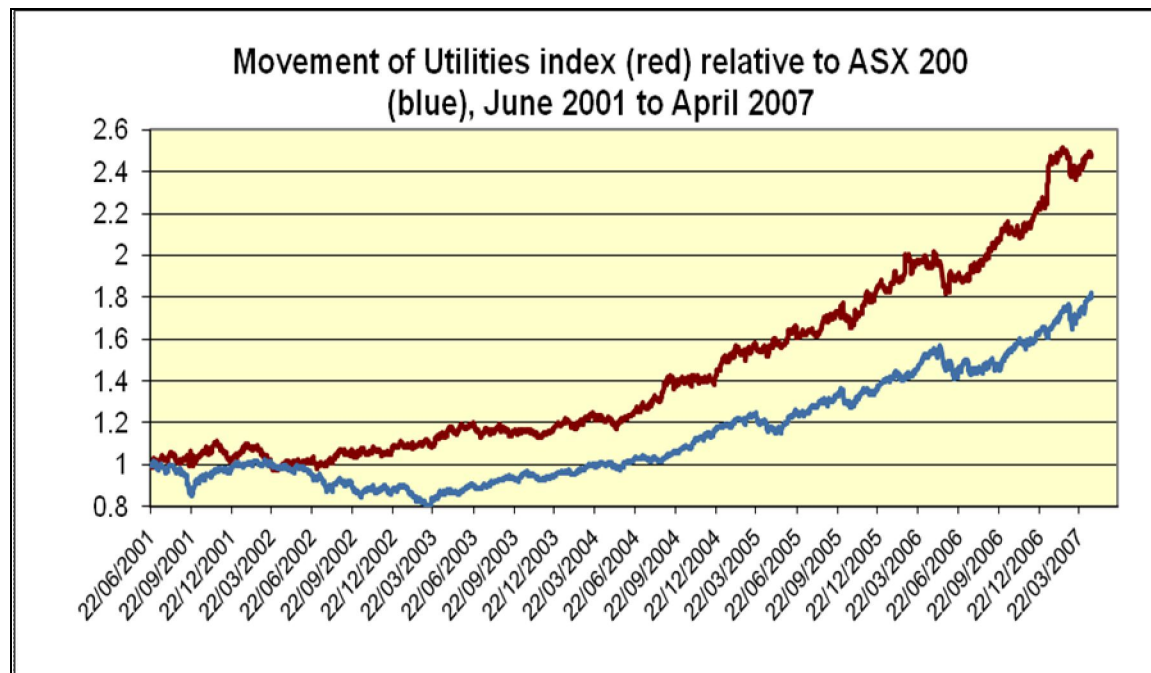
As the MEU on behalf of the EMRF noted in its response to the AER transitional guidelines for NSW and ACT, the AER must institute a STPIS now for all DBs and not delay the opportunity in giving consumers the benefits of a performance incentive scheme.

1.3 Rewards for risk and the regulatory bargain

Consumers have observed that network companies have a low risk in their market operations, especially compared to down stream industry which by and large is greatly exposed to competition (which drives industry to consistently seek lower cost approaches to reduce their costs and so remain competitive). The MEU sees that with their guaranteed (regulated) revenue stream and their unique natural monopoly position regulators must ensure that there is optimum pressure on distribution network businesses to perform their functions to achieve the maximum benefit for consumers but maintaining a low cost base reflecting the protected nature these businesses have. Regulators must also ensure there are adequate (but not excessive) returns to these businesses.

In this regard, it is pertinent to highlight that businesses such as electricity distribution businesses have achieved very good financial performances. Yet, these businesses have returned to their shareholders a dividend and market price growth that vastly exceeds that of industry in a competitive environment. This can be demonstrated by comparing the market performance of these businesses compared to those subject to strong competition.

Since 2001, the ASX has developed an index which tracks the market performance of electricity and gas transport businesses under the generic title of "Utilities" which provide essential services and are either the totally dominant or monopoly provider for the services they provide. The following chart shows the performance of the Utilities sector of the ASX 200, compared to all businesses in the sector.

Source: CommSec

At the same time the dividends paid by Utilities have exceeded those paid by all ASX 200 companies by over 20%[1]. Thus it is quite clear that the Utilities are enjoying both yields and growth in excess of the industry average. The AER should bear this significant out performance position when setting the guidelines for transmission reviews.

As network businesses are as profitable as they are, it is essential that the AER recognise that the introduction of a scheme which drives a monopoly business to provide excellent service to its customers is only part of the regulatory bargain where the DBs receive a virtually guaranteed income for providing a service that has effectively no competition. In the absence of incentive to perform at superior levels consumers will be left with a service which is mediocre at best.

1.4 Conclusion

It is against the above background, that the MEU makes its comments regarding the AER development of a STPIS.

The MEU notes that it appreciates the opportunity to review and comment on the draft guidelines for a STPIS to be included in the regulation of electricity distribution businesses.

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[1] See appendix A

2.   Essential elements of a STPIS

2.1 Introductory remarks

The electricity network is purely a tool for delivering power – it is a form of transport. Other than providing this connection between generator and consumer, it adds little as far as value to the electricity supply system is concerned. Yet, in performing its function, it can have a massive impact on consumers and generators.

As such, the MEU supports the AER in developing a STPIS. When considering a service performance incentive scheme there are three elements that must be considered:

- What are the key elements of service performance that will add value to those offering the incentive for better performance. As consumers are the beneficiaries of the improved service and will pay the incentive, there must be a focus on what consumers seek from the DNSPs as an improved service?
- Should the incentive be one way (ie a bonus only) or two way (a penalty if the targets are not met, combined with a bonus if they are exceeded)?
- The amount of DNSP revenue at risk?

When developing a service performance assessment program the **first** issue that must be determined, is what a reasonable service standard is for the basic revenue granted. From this point, increased revenue should be available to a DB only if it provides a service *better than* the basic service expected for the base payment.

The **second** issue is that if service performance is *averaged* then this implies that some customers may be receiving better service than others for the same payment. Therefore, whilst average performance is important, it is also essential to assess service performance for the worst service provided, so that efforts can be devoted to bringing the worse service performance to the average.

The **third** issue is to identify what are the services that should be rewarded for improved performance. These fall generally into two categories:

- The first is related to the direct supply – reliability (how often does a consumer lose supply and for how long each time) and quality (how often does the supply voltage change and by how much, and how much "hash" is included with the supply which reduces the benefit of the supply). Different consumer classes have different needs (eg for one customer a transient dip in voltage might trip off sensitive control equipment causing an outage yet for another the only observed outcome is light flicker).

- The second category is related to customer service – the personal touch – like the time to respond to queries, being on time for meetings, etc. It must be remembered that a monopoly does not have to seek custom, but the customer has only one source of supply. This drives the monopoly to consider only it own needs and puts those needs of the customer as a second order issue. The STPIS is an attempt to rebalance this attitude.

A competent STPIS must be able to address all of the wide variety of service interfaces involved and as most consumers are connected to the DNSP (rather than to TNSPs) the STPIS for a DNSP must be more encompassing and cover more issues than a STPIS for a TNSP.

The AER posits three alternatives for a STPIS. These options are:-

1. Public reporting (a "shame" file).
2. Guaranteed service levels (GSLs) which are effectively a penalty only.
3. An S-factor scheme which applies both reward and penalty for exceeding/failing set performance standards

In fact these are not alternatives but rather all can (and should) be used in combination. The MEU observes that the most advanced STPIS used in the NEM for distribution is that established by ESCoV. This scheme encompasses all three of the options – public reporting, GSLs and a penalty bonus arrangement for performance against set standards. This allows a\all aspects of the distribution business performance to be benchmarked relating to the service standard set.

The MEU recommends that the AER use the ESCoV set of service standards as a base and modify them to reflect the lesser degree of information on performance that is available for other DBs. This is especially important as we do not wish to see a 'best practice' scheme downgraded.

2.2 Customer service standards

The MEU sees that the direct implementation of the customer performance standards (GSLs) is directly applicable to all DBs and could be implemented immediately.

These GSLs provide an incentive for the DB to act as if it needed to be customer responsive. The GSL effectively is a payment made by the business to the affected customer if the DB does not meet its agreed customer service level. In part, the payment makes some restitution to the customer for the inconvenience caused by the monopoly provider.

For example, the following GSL service performance is incorporated into the SP AusNet decision[2].

Table D.65: GSL payments scheme, thresholds and payments, other customer service measures, 2006-10 regulatory period, SP AusNet

		Threshold	Payment
Connection time	Final Decision	10 business days	$50 per day (max. $250)
	Distributor proposed	15 business days for GSL payments, 20 business days for Electricity Distribution Code	$50 per day (max. $250)
	2001-05 reg. period	20 business days	$50 per day (max. $250)
Appointment window (customer present)	Final Decision	2 hrs	$20
	Distributor proposed	Specific appointment time	$20
	2001-05 reg. period	—	$20
Appointment window (customer absent)	Final Decision	1 day	$20
	Distributor proposed	—	—
	2001-05 reg. period	—	—
Repair of public lighting	Final Decision	2 business days	$10
	Distributor proposed	2 business days	$10
	2001-05 reg. period	2 business days	$10

In addition to these, there is a service standard for answering telephone calls to the DB call centre for 75% of all calls to be responded to within 30 seconds.

The MEU considers that the AER assumption that GSLs are essentially a penalty only is to a degree misleading. It is considered that by the DB failing to meet the standard of service, it will cause a cost to the customer involved. In the case where competition applies, the DB would lose custom if it failed to meet certain standards for inter-personal relationships. When viewed in this light, the GSL becomes less of a penalty and more of a recompense for costs incurred by the customer who has no alternative but to use the monopoly provider.

The MEU considers that service standards such as these guaranteed service levels (GSLs) are readily translated into every DB immediately.

2.3 Network service performance

The MEU notes that average performance as measured by a DB network regardless of its location, size and ownership cover SAIDI, CAIDI, SAIFI and MAIFI (both planned and unplanned). These measures have been used by distribution networks for many years (even before deregulation) so that setting

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[2] ESCoV, Electricity Distribution Price Review 2006-10, Final Decision, Part D: Summary of Final Decision by Distributor, SP Ausnet

individual network averages against each of these measures is quite feasible. The MEU does accept that unless these are measured currently for rural and suburban areas or on a feeder basis, (as has been required of the Victorian DBs) then to move beyond network averages for STPIS at this time, is not feasible.

The ESCoV (and its predecessor ORG) initially used network averages for these standards until there was adequate historical data available to move to more detailed performance covering rural and urban with identification of individual feeder performance.

The decision of ORG/ESC to implement a STPIS at the commencement of regulation was based on the (very realistic) assumption that unless there was a financial incentive, DBs would not even attempt to improve the quality of service. Having the financial incentive drove the DBs to improve the service, and as a result the ORG/ESC has been able to adjust the set points for the STPIS over time to reflect the improved service being provided.

The MEU considers that the ORG/ESC approach was sound, and it directly resulted on improved service for consumers. Using a paper trial approach (as has been suggested by the AER for NSW/ACT DBs) will not improve standards at all, and the MEU sees that DBs would have an active incentive to have worse performance so that when the financial incentive is implemented, the DB has a low set point against which to perform and so maximise its financial benefit by "picking the low hanging fruit".

The MEU considers there is no reason not to implement a STPIS immediately based on average performance. Not to implement such a program immediately condemns consumers to an extended period of less than optimal service performance. Even if the performance standards are initially set too low, and a financial benefit is granted, the fact that the incentive has provided realistic and achievable set points for the next review period is seen by consumers as an overall positive. To delay implementation on the basis that the set points are unknown is not in the consumers' interests and provides a DB with an opportunity to increase its revenue.

Overall the MEU considers that the AER would be letting an opportunity (to action the interests of consumers) to pass by not immediately implementing a financially driven incentive scheme.

There is no doubt that a GSL approach can be implemented now, and a network service performance can be implemented using current levels of SAIDI, CAIDI, SAIFI and MAIFI, averaged over the network. Even if these are set a little conservatively now, they will encourage an immediate change in approach by the DBs so that when the next review is commenced, there are "hard" numbers to be used in the STPIS.

The MEU notes that the ESCoV scheme grew organically. In the first years the scheme was based exclusively on averages, and has been refined at each review to provide a greater insight of each DB performance. This refinement has allowed the ESCoV to identify the differences between performance on rural and urban feeders, to provide measures of performance on worst performing feeders, and to increase the understanding and ability of the DB to manage quality issues in their networks.

The MEU considers that that the AER can readily implement a STPIS immediately based on:-

- **GSLs for customer service (eg such as established by ESCoV**
- **Network performance using average network performance levels that are already measured.**
- **If the AER is concerned that using such an approach might result in un-measurable risks, it might initially limit the exposure of the DB to 1% of revenue on the same basis that it decided this level of risk for TNSPs.**

Failure to implement a financially driven STPIS but use less intrusive measures and controls (such as a paper trial approach) will result in worsening of performance by DBs and cause increased costs for consumers.

3.   National Framework

The Major Energy Users Inc. provides comments to each of the questions raised in the AER's Issues Paper on Electricity Distribution Network Service Providers Service Target Performance Incentive Scheme.

Comments below address each section of the AER Issues Paper.

<u>3.a AER Section 2</u>

Objectives in establishing a service target performance incentive scheme

Q. The AER would like views on whether it is feasible and appropriate to establish a common approach within a national framework?
Yes, this is consistent with the AEMA in establishing a national framework for economic regulation of DNSPs. The scheme itself should be consistent but the individual set points for performance and the various individual costs might vary between DBs depending on their degree of development of performance measurement.

The ultimate goal should be that all DBs will be measured for the same standards, and that there is consistency of approach across all DBs, allowing consumers to make decisions based on the proven performance of each DB.

Q. The AER would also like views on the issues it may need to consider in establishing this framework. In particular:

What should be the key elements?
Quality and reliability indicators, including dips and frequency interruptions, time involved in restoring services all should be measured in increasing depth into the networks over time.

Initially averaged figures can be used, but with better measures being implemented performance on individual feeders should be measure, with the goal being that performance on worst performing feeders will be improved to match the average.

Networks already use a range of measures for assessing performance - SAIDI, CAIDI, SAIFI and MAIFI – and the STPIS should use these and any new measures developed over time

How might a national scheme deal with differences between regions/jurisdictions?
Provide a short time frame for convergence.

What are the possible obstacles to achieving an effective national framework?
None.

3.b AER section 3

Types of service incentive scheme

3.1 Public reporting schemes

Q. The AER would like views on whether it should require DNSPs to report on key aspects of their service performance for public reporting purposes

Yes, of course. There is no reason not to. This should be an element of each financially driven part of the STPIS.

As the DBs enjoy a monopoly, their performance must be made public to drive efficiency.

Q. If so, should DNSPs be required to report just on those aspects of service performance measured for an incentive scheme (e.g. GSL scheme or s-factor scheme) or on a common set of agreed measures?

Both aspects should be reported in the same detail as the measures are established

Q. The AER would also like views on how future reporting arrangements which may be multi-faceted (i.e. reporting to the AER in relation to an incentive scheme and potentially for public reporting purposes) could be simplified or rationalized to reduce compliance costs

Similar reporting dates would reduce the compliance costs. However, compliance costs are a small element of the costs that consumers carry as a result of poor performance. It must be recognised that it is service that consumers are paying for so they need to understand how well that service is being provided. To provide data for the use of AER runs contrary to the concept that consumers must be able to see how well their payment for service matches the service standards other might be getting.

3.2 GSL schemes

Q. The AER would like views on whether it should develop a national GSL scheme.

Yes. There is little difference between DBs with regard to these personal interactions and therefore all DBs should be exposed to the same level of penalty regardless of where it is located.

Q. The AER would also like views on issues associated with the implementation and operation of a national GSL scheme.
The MEU sees that a GSL scheme is not impacted by national considerations. When the GSLs are identified, they are independent of size or location of the DB. The only difference between DBs might be some of the set points within the GSL.

This means that the architecture of the GSLs is common, but there might be minor differences within the set points used, eg between a remote rural network and an urban network.

3.3   Financial incentive (s-factor) schemes

Q. The AER would like views on the overall design of a national s-factor scheme. In particular:

the form that a national s-factor scheme might take
The form of the S-factor scheme would be the same and aggregate all of the various performance measures used. This means that out performance in one aspect might mitigate the financial premium of another measure. There should be one payment which draws together all performance measures.

The architecture would be similar to the TNSP STPIS.

Whether the scheme should be symmetrical
Yes

the number of measures that should be included
The ESCoV STPIS already provides a number of measures for its STPIS. These have increased over time to include measures not previously used.

The MEU would expect that the measures would be increased over time as better tools become available, and more measuring equipment is installed by the DBs.

An example of this is the move in Victoria to measure performance by feeder, rather than across all supplies. This trend has allowed DBs to identify worst performing feeders and to take action to improve the quality of supply.

It should be noted that a STPIS must be designed to improve the overall quality of supply within the network. Therefore to eliminate the ability to measure performance will result in no overall improvement.

Any other relevant threshold matters not dealt with elsewhere in this paper.
The ability to measure performance and identify the worst performing feeders is critical and must be seen as a reason to implement STPIS. It is seen that that this whole scheme must be considered as a program of continuous improvement.

This means that the architecture of the STPIS must be flexible to allow those DBs who have not had a STPIS to catch up with those that have, and that the STPIS will continue to grow to measure increasingly those aspects which impact consumers.

As noted above, an example is the measurement of performance by main feeder, and this trend can be implemented into even sub feeders as the measuring equipment is installed.

As an end game, the target should be that performance be measured at every supply point, because every consumer pays the same amount for each type of supply point, and it is inequitable that one consumer of the same class as another receives better or worse supply performance even though both pay the same amount for the service.

Q. To what extent should existing s-factor schemes form the basis of a national scheme?

The architecture should be the same, although there may be different set points and in the early days there may even be some different measures reflecting the degree to which measurements cam be made (eg in the early days one DB might be measured on network average measures whereas another DB might be measured on a main feeder basis and an third DB be measured on a sub feeder basis.

3.4   Interaction between GSL schemes and s-factor schemes

Q. The AER invites views on the establishment of both GSL and s-factor schemes in a national framework. In particular:

should both types of schemes be implemented
Yes, and used for incentivizing different performance assessments.

is the value to customers of having both types of schemes sufficient compared to the additional costs associated with having to implement and administer multiple schemes
Yes. In fact the question implies that the AER considers that there is a cost premium for implementing both. If so then the AER is wrong.

The MEU considers that the two are complementary and address different types of performances. The way the ESCoV implemented the two schemes shows that they are complementary and therefore not in competition with each other.

how should information requirements be set to minimize compliance and collection costs
By having similar collection and reporting dates.

3.c AER section 4

Types of service performance measures in s-factor schemes

4.1   Reliability indicators

Q. The AER would like views on which measures of reliability to include in a national s-factor scheme.

The measures that should be addressed are those which impact on consumers.

From a consumer's viewpoint, any disturbance which results in a power failure is an issue. Further it is the duration of an outage (whether planned or unplanned) is of importance, and just as important is the frequency with which supply is disrupted.

As most residences have little or no electrical protection from voltage spikes (ie excessively high voltages) the impact and frequency of voltage spikes is of concern. Many industrial consumers use sensitive protection equipment and these tend to trip when voltage dips, effectively causing a power loss. Thus when voltage of supply is

outside of normal operating ranges (eg +/- 10%) then these disturbances are of concern.

The MEU suggests that the S-factor scheme should be assessed on the following criteria:-

- *Power outages viewed from duration and frequency, both planned and unplanned*
- *Voltage variation outside normal operating ranges viewed from duration and frequency*

SAIFI, SAIDI, CAIDI and MAIFI are all measures that are used widely and can be used for the S-factor. Equally, these same standards can be more focused and used for individual feeders as well, allowing measures to be made of worst performing feeders.

Q. The AER would also like views on the classification of feeders by type and whether the AER should distinguish between planned and unplanned interruptions.

The classification of CBD, urban, rural short and rural long are seen as appropriate to segregate those areas of the network which are subject to differing standards of supply.

The architecture of the scheme should be structured to allow these categories to be augmented if a need is identified.

From the viewpoint of a consumer, the only difference between loss of supply from a planned outage compared to an unplanned outage is that some notice can be provided for a planned outage, and the consumer can take some action to minimise its losses. Therefore the severity of planned outages should be less than for unplanned outages. The s-factor scheme might therefore reflect a weighting on these two elements, providing a greater penalty/reward in relation to unplanned outages.

Mapping the performance between unplanned and planned outages is useful to the DB and to the regulator in managing where actions are needed to improve on poor performing feeders and the resultant capex that might be needed. Because of this mapping between planned and unplanned outages is supported.

4.2   <u>Quality indicators</u>

Q. The AER would like views on the appropriateness of incorporating quality indicators in a future s-factor scheme, including the likely costs and benefits of incorporating quality indicators, the possible types of measures that could be used, and the availability of historical data.

Where the quality of supply impacts the supply stability of a consumer, then this needs to be assessed within the s-factor scheme. Eg if a voltage dip is severe enough to cause a consumer to lose supply then this must be measured as a supply loss. Equally if the dip only causes light flicker, then this is hardly reason to penalize a DB.

One of the main problems is that there is insufficient measuring equipment within the network to confirm whether a quality of supply has caused the problem. AS the DBs are aware they do know through reports from consumers and their locations where "hot spots" do occur in a network. Some DBs then install measuring equipment to assess the cause and extent of the problem.

The refinement of an s-factor scheme to accommodate such less obvious issues (but no less real because of this) should be implemented over time, rather than attempting to implement it at the start of the program. In this regard the attention of the AER is drawn to the experience of the Victorian experience where the incentive scheme has been under continuous development for three regulatory cycles.

The MEU suggests that the AER implement an architecture for the scheme which can accommodate continuous adjustment and integration of more detailed elements over time

Q. Should supply quality be addressed in a different way such as through a GSL scheme or some other scheme?

Many of the issues of quality of supply are consumer dependent. For example where harmonics are of sufficient concern to one consumer, they might not be so for another. A power spike might cause one consumer significant loss, but another almost nothing.

With such variety of outcomes for consumers for instability of supply, it becomes most difficult to introduce such outcomes into the s-factor arrangement. Thus a GSL becomes the best way to address issues of quality which are effectively consumer specific.

4.3   Customer service indicators

Q, The AER would like views on customer service indicators to be included in an s-factor scheme, including the likely costs and benefits, and feasibility, of incorporating a range of indicators.

As noted above there will be a need to increase the customer service indicators over time, so the architecture should allow for this to occur. In particular the AER should establish a customer advisory body to monitor what service issues are important.

Other issues such as managing the outcome of voltage spikes, fixing the impact of harmonics and frequent voltage dips for those consumers who are impacted, should be assessed in terms of GSLs.

On an overall basis the regional energy Ombudsman schemes could provide the data necessary for assessing the frequency of customer service complaints, and the ease of their resolution. However such data only reflects the complaints of those prepared to take action, and in such issues, this provides an under stated level of complaints. As a result such an approach would be more qualitative and quantitative and open to dispute between the Ombudsman and the DB.

It is therefore recommended that the AER establish close ties with the Ombudsman schemes to establish a methodology for implementing customer service as an s-factor element

Q. Would customer service indicators be more appropriately addressed in a GSL or other scheme?

A. Because of the difficulty in developing a measure, the MEU considers that probably the answer to the question is Yes.

However, the AER working with the Ombudsman schemes could develop a measure for customer service so that such a measure could be developed to allow customer service to be integrated into the s-factor scheme

3.d AER Section 5

Approaches to setting rewards and penalties in an s-factor scheme

Q. The AER would like views on the above approaches for setting incentive rates and other possible approaches.

The MEU considers that all consumers are entitled to a minimum performance level and that this relates to the regulatory bargain. Consumers wishing to have a better service than that which they receive under the regulatory bargain should accept that they will have to pay a premium, and that this premium can be assessed by the individual seeking the premium service against the improvement in supply.

On this basis the MEU considers that the network wide s-factor scheme should only relate to the service expected under the regulatory bargain. This creates the challenge of determining what the base level service that should be provided under the regulatory bargain needs to be. As there are consumers who already receive better service than others, this creates disparity between consumers.

The MEU view is that, as a matter of equity, all consumers of each class should receive, as a right, the average service standards for the network as related to that class of consumer. Therefore those consumers receiving service less than the average, these consumers are entitled to have the quality of service improved to the average at no additional individual cost.

Q. The AER would like views on the above approaches for setting incentive rates and other possible approaches

Different consumer classes have different needs and therefore different incentives will result. Equally the actual amounts also have different impacts. Eg for a restaurant it might see that if durations of outages were relatively short (eg measured in a few minutes), that frequency of outages was the main concern, but as the durations of outages increase, this has a greater impact as it causes loss of food stored in refrigerators. For a plastic film maker, the business is impacted greatly by frequency of outages and duration of outage tends not to be as big an issue as the frequency.

The impact of loss of power is far reaching, and well beyond the cost of supplying it and that the value of lost load for distribution supply probably on average needs to be higher than the VoLL (price cap) needed for the electricity spot market..

The MEU considers that the incentive should relate primarily to underperforming feeders. The MEU would not be opposed to using a VoLL of between $20,000-30,000/MWh purely as the basis for assessing the viability of improving those feeders which underperform the average supply conditions.

However, it must also be noted that an incentive arrangement provides for a payment for improving the overall reliability and quality of supply. Thus the bonus is expected to provide the bulk of the funds for the necessary upgrade of underperforming feeders. It is not expected that all of the bonus is to be a profit for spending approved capex and opex to improve the supply arrangements.

Q. The AER would also like views on how it should determine relative weightings for measures.

The MEU sees that it can only be by surveying different consumer classes that it will obtain data giving it an indication of the relative weightings for each element of the measures used.

The MEU points out that different consumer classes will have different views (eg one class might consider frequency of occurrence more disturbing than overall duration, so that weightings need also to reflect the relative numbers and consumption patterns of the different consumer classes connected.

3.e AER section 6

Approaches to setting performance targets under an s-factor scheme

Q. The AER would like views on the possible approaches outlined above to setting targets in an s-factor scheme.

The ultimate goal is to achieve a national framework and to be able to report on a common basis. To achieve this requires the framework to be standard and for the measures to be standard across all jurisdictions. It is accepted that the actual values might vary between jurisdictions and even between DBs in the same jurisdiction.

There will be a need to transition between existing schemes and the national scheme, so there is merit in the Victorian approach which allows for the transition.

Once the transitional period is complete, a target measure should be set as it in on the basis of a specific performance that the regulatory bargain has been made. This implies that at each regulatory reset, the targets should be re-evaluated in light of the performance achieved, and then new targets be set for the operation of the bonus/penalty arrangements for the next regulatory period.

As a matter of principle, any reduction in setting from the previous period must be justified on very specific criteria which will be unique o the new period. For example, it may be that the during the new period, capex has been provided for upgrading the feeder which has been underperforming. This may necessitate increased outage time for a specific part of the new period. It would be reasonable to assess whether the upgrading works will impact on the measure and if so for this to be included in the

new measure. Such an approach will require the measure for the next period to be set in relation to the expected outcome of the up\grade work.

3. f AER section 7

Allowing for risks

Q. The AER would like views on mechanisms to deal with additional risk introduced by an s-factor type scheme and whether it is appropriate for such risks to be wholly borne by DNSPs and/or customers.

The regulatory bargain is based on a minimum performance. Thus any lower performance is penalizing the consumer in that it has paid for a level of service and is not receiving it.

The purpose of the STPIS is to provide an incentive on a DB to improve its level of service. In the absence of the scheme the DB will only provide the minimum service imposed by the regulator.

An incentive scheme (especially a symmetrical one as is proposed) provides a reward for providing better service, and penalizes the business for poor service. In a competitive environment better service is rewarded by more custom and therefore higher profits – poor service is penalized by a loss of custom and lower profits. A monopoly by definition does not need to seek greater custom, thus the STPIS is an attempt to replicate this competitive pressure.

When viewed in this way, the only risk for a DB and consumers that is not one normally faced by a business is that related to the value(s) put on the base level of service. However the DBs have been providing service for many years and therefore the base level of service that has been provided is well known.

The MEU does not consider that the s-factor scheme really increases the risk for a DB that is not faced by a business in a competitive environment, particularly as the set points for the scheme are based on historical performance.

The MEU considers that if anything consumers face a higher risk than the DBs in that they are likely (especially in the early days of the scheme) to be required to pay a premium for service improvement that is probably readily available to be provided by the DBs for very little effort.

The MEU therefore does not consider that the DBs should be provided any additional protection from the risks they might face from such a scheme, when the DBs are rewarded by the payment of a bonus for better service.

3.g AER section 8

Allowing for exclusions

8.2   Quantitative measures

Q. What approach should the AER take in applying exclusions?

There are two principles that are implicit in exclusions. The first is that consumers have paid for a service with minimum standards of supply. From a consumer viewpoint, it is immaterial what causes the outage, because the consumer still suffers to the same extent regardless of the cause.

On the other hand a supplier of a service should not be held responsible for something which is or was outside of their ability to manage or control. However in assessing the ability to manage or control, care needs to be taken.

For example, if the delay was due to a shipping problem but the DB could have avoided this risk by using local manufacture, was this shipping problem avoidable? In this regard it is necessary to identify if the DB took the action to import based on it attempting to improve its profits by exposing the consumer to greater risk. If the DB took the action to import for profit motives and did not seek approval from the consumer for the action, then the action of the DB was within its control and so it should not be protected.

The suggestions included in the AER paper for using statistical measures for limiting risk for the DBs is biased against the consumer. To exclude an incident because its very magnitude might reduce an incentive payment is totally wrong if the incident was caused by a failure of the DB to act properly. Equally to include an incident which was totally outside the power of the DB to do anything about it is also totally wrong.

When reference is made to the purpose of the incentive scheme, it must be remembered that the scheme is intended to replicate commercial pressures. If the commercial environment does not provide any protection by exclusion then the s-factor scheme should also not do so.

When considered from this viewpoint, using statistics to exclude "outrider" issues is totally against the concept of the incentive. Equally the incentive should exclude matters against which the DB can not be expected to manage or control.

The MEU is totally opposed to using a statistical basis which excludes "outriders" which are within the control of the DB.

Q. Should exclusions cover reliability indicators and customer service indicators?

If the cause of the poor performance is beyond the control of the DB then an incident should be excluded. For example, if the telephone system collapses, the DB should not be penalized for failing to meet its call centre standards.

Q. Should exclusions be determined by reference to qualitative or quantative measures?

They should only be permitted if the cause is totally outside of the ability of the DB to manage or control it. Implicitly this means that quantitative measures are less appropriate than qualitative assessments.

The MEU considers that the "force majeure" principle is the only one which has validity in providing any exclusions to the performance incentive mechanism, as this is the only measure that has validity in a competitive commercial environment.

Q. How appropriate is a standard such as IEEE 1366-2003?

The MEU considers that it is inappropriate for use as a control in measures for incentive payments as it is biased against the interests of consumers.

8.3   Options to limit the contribution of an excludable event

Q. Where an exclusion threshold is exceeded what action should the AER take to limit the contribution of events?

Where the cause of an incident is beyond the ability of the DB to control or manage (ie a force majeure incident) then it should be excluded in its entirety from the measure used for setting the incident.

For example, where a bush fire has destroyed a feeder, then this would be considered to be excluded from the performance measure in total.

3.h AER section 9

Implementation issues for the transition to a national scheme

9.1   Issues for jurisdictions currently without an s-factor scheme

Q. Are there any other issues that the AER needs to consider?

There should be no delay in introducing a scheme. If there is minimal data available then the scheme should not be deferred in seeking extensive data, but the data available should be used as the basis for the scheme.

As the AER notes, all DBs have collected some data over the years and even if there is some doubt on the data it is better to introduce a scheme so that when the next review is carried out, better data will be available.

To delay introducing a scheme condemns those consumers to an extended period of suboptimal performance. Even using current average data discounted for concerns about its accuracy is better than not implementing a scheme. The very implementation of a scheme will cause accurate data to be produced, and this sets the stage for the introduction of a more comprehensive scheme at the next reset.

The ORG/ESCoV used this principle to very good effect, by following a staged program of getting hard data from within a scheme and then extending it as the data became available.

The MEU is totally opposed to using paper trials as there is much less pressure to perform implicit in such an approach and they provide a mechanism for the DB to set low targets in the first period of a scheme and so garner "low hanging fruit" at the expense of consumers.

9.1.1   Issues relating to the availability of data

Q. The AER invites comments from interested parties on the current and future availability of data on reliability and quality of supply measures for DNSPs currently without an s-factor scheme.

As noted above the data that is available now should be used. All DBs have collected the basic average performance data over many years, including before the periods when they were corporatized in the mid to late 1990s.

If there is concern about the data it is better to use this now (with some discount if proven to be necessary) than to wait until a more detailed and comprehensive scheme might be introduced.

9.1.2   Issues relating to the accuracy of data

Q. The AER invites comments from interested parties on the current and future accuracy of data for reliability and quality of supply measures.

It is now and will be the responsibility of the DBs to collect the data needed. The AER needs to implement some method of being able to verify the accuracy of the data collected.

In this regard the MEU recommends an audit process following approaches established by the quality assurance or financial industry codes of practice.

Q. How could the AER take changes in performance data, due to changes in recording systems, into account in setting targets and incentive rates?

Data which is now available should be used as the basis for the first period of the scheme. As additional data can be identified for collection then this should be implemented and used as the scheme is expanded over time for each DB.

9.1.3   Issues relating to the interaction

Q. The AER invites submissions on issues relating to the interaction between mandatory jurisdictional service standards and a national STPIS for DNSPs currently without an s-factor scheme.

Mandated jurisdictional performance sets a floor for the set points within the scheme. The purpose of the scheme is to improve the standards of service over time, so in the initial stages the DB is encouraged to out perform the mandated standards.

As the AER demonstrates the effectiveness of its approach, it can request the jurisdictions to eliminate the mandated standards as these will become superseded by the higher levels of performance which have resulted from the incentive scheme

Q. For example, what benefits and limitations could the existing mandatory jurisdictional service standards place on the implementation of a national s-factor scheme?

The MEU considers that the existence of mandated standards is a result of their being no other scheme in place to encourage better performance. As noted above, the mandated standards provide a floor for the incentive scheme, and the incentive scheme is to provide an incentive to exceed the mandated standards.

Operating a concurrent incentive scheme with the mandated standards is feasible and sensible, as it provides a reason for the DB to exceed the mandated levels.

9.2 Transitional issues for jurisdictions with an s-factor scheme

Q. Are there any other issues that the AER needs to consider?

The ESCoV introduced a modification to its own scheme – effectively a transitional approach. The AER should follow this same pattern and use the existing schemes as the basis for the current periods and then to introduce its refinements as a transitional approach.

9.2.1 The availability and accuracy of data

Q. The AER invites submissions from interested parties on current and future data availability and accuracy in relation to DNSPs currently with an s-factor scheme. In particular, the AER would like views on the availability and accuracy of service reliability and quality data, including the level of the network at which this data is recorded.

As a matter of principle a monopoly des not want to be accountable for the service it provides. Accordingly they will provide extensive reasons why the data available is inadequate for the purpose.

It is by implementing a scheme now that the AER will obtain the accurate data it needs. The MEU has consistently maintained that it is only by the operation of the scheme that the AER will source the data it requires to implement its scheme. The MEU strongly recommends that the scheme be immediately implemented so that the accurate data needed can be gathered.

9.2.2 Changing the structure of schemes (definitions/exclusions)

Q. The AER invites comments from interested parties on whether changes in reporting and the incentive mechanisms themselves should be taken into account in developing targets for DNSPs currently with an s-factor scheme.

Yes

9.3   Transitional issues in relation to guaranteed service levels

Q. If the AER were to develop a national GSL scheme, what issues arise regarding existing GSL schemes (that are mandated under jurisdictional electricity legislation) operating concurrently with a national scheme.

There are three approaches that can be taken. The AER can implement a parallel GSL scheme, it can request the jurisdiction to cease their GSL scheme when the AER implements its scheme, or the AER can do nothing.

The MEU sees that option three (do nothing) is not acceptable and therefore recommends a mix of options one (parallel scheme) and two (get the jurisdictional scheme suspended)

Q. In relation to existing GSL schemes that are not mandated, what issues arise in relation to transitioning these schemes to a national scheme, should this be considered appropriate?

There is no reason not to introduce GSLs immediately. By and large the setting of GSLs does not require extensive data, and as noted above, regional ombudsman schemes should be used as sources for data on customer service performance and for advice on what levels of GSLs might be appropriate.