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Mr Sebastian Roberts
A/General Manager
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Australian Competition and Consumer Commission
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Dear Mr Roberts

SOUTH AUSTRALIAN TRANSMISSION NETWORK REVENUE CAP – DRAFT DECISION

NRG Flinders appreciates the opportunity to respond to the ACCC's Draft Decision on the South Australian Transmission Network Revenue Cap for 2003-2008.

The Draft Determination is largely consistent with the comments made by NRG Flinders across the majority of issues. In addition, NRG Flinders understands that the revenue stream proposed by the ACCC is considered sufficient to enable ElectraNet SA to remain financially viable and meet its minimum Code and regulatory obligations. Accordingly, NRG offers no further comment on the expenditure levels or rate of return parameters proposed in the Draft Determination.

The following comments are therefore confined to the service standards proposed by the ACCC.

Service Standards

The ACCC has proposed a set of service standards and performance incentives in the form of a Service Standards Performance Incentive Scheme, supported by the work of SKM.

NRG Flinders supports the need for financial transmission performance incentives, linked to a set of measurable service standards. This provides an important means of linking regulated revenue to network performance, and improves transparency and accountability in the delivery of services to network users.

It is noted that the ACCC has proposed that the level of reward (or penalty) should be capped at 1% of regulated revenue. NRG Flinders would agree that this level of revenue at risk would not result in any material increase in risk to the organisation, but would query whether there may be scope to safely increase this level by 1 or 2 percentage points, perhaps progressively, without materially altering the risk profile of the TNSP. This would strengthen incentives for improved performance.

NRG Flinders would also submit that there is a need to maintain consistency with the proposed incentive structure to be applied to the relevant DNSP, if there is to be a consistent improvement in outcomes for network users.

In this regard, it is noted that the Essential Services Commission of South Australia (ESCOSA) has commenced consultation on the incentive measures to apply to the South Australian DNSP, noting that recent schemes introduced elsewhere (eg Victoria and the United Kingdom) typically apply incentives of around 2% of regulated revenue. If this is to become the accepted benchmark, this provides a further argument to increase the level of incentive to be applied to the TNSP, to ensure consistent service improvements across the network on the most cost effective basis.

In terms of the specific performance measures proposed, NRG Flinders accepts the use of measures linked to the number of outages and duration of outages (Measures 2 and 3) and the measure of overall availability (Measure 1) which also captures the impact of planned outages.

However, it is noted that the ACCC has proposed to defer the introduction of the proposed network constraint performance measures (Measures 4 and 5) pending the collection of the required data. NRG Flinders would query why sufficient historical data should not be available in the NEM to support the immediate application of these measures, particularly for inter-regional constraints (ie interconnect performance).

NRG Flinders would also note that ElectraNet SA has previously proposed the introduction of an interconnector Available Capacity Factor (ACF) as a measure of interconnect availability. This measure appears to provide a readily measurable indicator of interconnect performance, and if applied would provide the TNSP with clear incentive to maximise the availability of regulated interconnects. Noting that the proposed inter-regional constraint measure is similar in nature to an outage measure, as a measure of overall availability the ACF would appear to provide a valuable adjunct to the performance scheme.

It is also noted that the ESCOSA has proposed to adopt such a measure in any event if the ACCC fails to incorporate an interconnect availability measure in its incentive scheme, via the SA Transmission Code. Clearly it would be preferable for a unified package of incentive measures to be applied to the TNSP by the ACCC as transmission pricing regulator.

In the application of network service standards, the Draft Determination acknowledges the principle that the TNSP should be held to account for risks that it is best placed to manage. This may include factors that are outside the direct control of the TNSP, but that the TNSP is nevertheless in the best position to manage through the design and operation of the network.

Reflecting this principle, it would appear logical to exclude events such as generation failure or shortfall and customer triggered outages from the outage measures. It would also appear reasonable to exclude only climatic events of an extreme nature that could not reasonably be expected or foreseen.

On this basis, the proposed definition of force majeure to be applied for the purposes of the Scheme appears unduly broad in its application. Contrary to the principle above, force majeure is defined to include events beyond the reasonable control of the affected party, including a range of factors such as storms and actions of the elements.

Force majeure for the purposes of the Scheme should arguably capture only those events for which the TNSP is not in a position to effectively manage the level of associated risk. Therefore, force majeure would be expected to include only factors such as extreme weather events that could not reasonably be anticipated. Accordingly, this suggests a narrower definition than that proposed. In addition, it is noted that recent regulatory decisions in Victoria have included (mild) earthquakes as a risk that should reasonably be managed by the network service provider. NRG Flinders would therefore encourage the adoption of a consistent definition of force majeure events across regulators for the purposes of network performance monitoring.

It is also noted that the performance measures put forward by SKM are largely operational in nature, and do not include direct measures of market impact. NRG Flinders would strongly encourage the ACCC to consider the inclusion of service standards and associated performance measures which seek to capture the market impact of transmission operations (eg network outages). As an example, the Draft Determination acknowledged the suggestion that the firmness of settlement residues could be increased by linking TNSP income to these residues in some manner.

Over the longer term, there are arguments for deriving an increasing portion of transmission revenue from market-based sources, thereby linking a greater share of the TNSP revenue base to commercial performance. Market-based income streams could progressively replace regulated revenue sources. In return for bearing an increasing share of market risk, this provides significant upside earning potential for the TNSP, and provides more powerful incentives for efficient performance. In this way, increases in earning potential are linked directly to the level of market risk the TNSP is prepared to accept.

CONCLUSIONS

- There may be scope to safely increase the proposed level of financial performance incentive by 1 or 2 percentage points of regulated revenue, perhaps progressively, without materially altering the risk profile of the TNSP.
- There are strong arguments for applying consistent incentives across network service providers to ensure improvements in outcomes for network users. This provides a further argument to increase the level of performance incentive on the TNSP commensurate with emerging incentives on the DNSP.
- Risks should be allocated to the party best able to manage them. The proposed definition of force majeure therefore appears very broad, and appears to include a range of risks the TNSP might reasonably be in a position to manage.
- It is unclear why sufficient historical data should not be available in the NEM to allow network constraint performance measures to be applied immediately. The ACCC might also consider complementing these standards through the use of an interconnect availability measure such as the Available Capacity Factor (ACF).
- The ACCC is strongly encouraged to consider the adoption of performance measures designed to measure the market impact of transmission operations in the forthcoming regulatory period.
- Building on this, there are arguments for deriving an increasing share of transmission revenue from market-based sources over time, providing upside earning potential and increased commercial incentives for the TNSP. Increases in revenue should be linked directly to the level of market risk the TNSP is prepared to accept.

Should you have any queries, please feel free to contact Simon Appleby on (08) 8372 8706 or myself on (08) 8372 8726.

Yours sincerely

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