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office of the tasmanian economic REGULATOR

Mr Chris Pattas
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Dear Mr Pattas

SERVICE TARGET PERFORMANCE INCENTIVE SCHEME

Thank you for providing OTTER with the opportunity to comment on the AER's proposed amendment to the national service target performance incentive scheme (STPIS). OTTER has a particular interest in this issue as in its last distribution price investigation, the Tasmanian Regulator moved away from an s-factor service incentive scheme (SIS), which was applied in the 2003-07 regulatory period, to a new scheme that provides a more targeted approach to reliability issues. The new scheme has the support of the Tasmanian Government and Tasmania's sole distribution network service provider, Aurora Energy. All three parties would, I believe, consider it a retrograde step if Tasmania's new scheme could not be accommodated in the STPIS for application in the next distribution price determination for Aurora Energy.

The STPIS uses network-wide performance as the basis for its service incentive scheme. Its focus is on addressing the worst performing feeders to bring SAIDI and SAIFI for the three categories of feeders (CBD, urban and rural) to acceptable levels of performance whilst ensuring that overall network-wide performance does not deteriorate. This approach was used in Tasmania in the 2003-07 regulatory period with reliability standards set in the Tasmanian Electricity Code (TEC). However, it had its limitations and these were noted in OTTER's *Investigation of Prices for Electricity Distribution Services and Retail Tariffs on Mainland Tasmania – Final Report and Proposed Maximum Prices*, September 2003:

> The Regulator is of the view that the TEC specifications are poorly targeted in that performance may vary greatly along feeders, and a reported average performance may mask areas of significant under-performance. They take no account of the variation of the customer or load density within feeder classes (which are indicators of both cost to serve and revenue per feeder kilometre) and it may be an efficient economic and equitable outcome that the performance on certain low-density feeders is less than the specified minimum. Conversely, minimum performance on feeders with a relatively high customer or load density may be below an economically efficient level.

A joint working group comprising OTTER, the Tasmanian Government and Aurora Energy developed new distribution reliability standards, which formed part of the price/service package of the Regulator's price determination. The standards apply to customers aggregated into one of five community categories[1] (critical infrastructure, high density commercial, urban and regional centres, higher density rural and lower density rural). The application of performance standards to these categories recognises that like communities

[1] Categorisation was based on electricity consumption density which is seen as a significant indicator of the social and commercial importance of electricity to a community - connected kVA being used as a proxy.

will have similar requirements and expectations. Performance targets for SAIDI and SAIFI are set for each category of community and for each individual community within the category. For example, maximum acceptable SAIFI for the 'higher density rural' category of communities (33 communities fall within this category) is 4.0 and maximum acceptable SAIFI for each of the 33 communities is 6.0. This ensures that communities receiving poor reliability are not masked by averaging.

The performance targets set for each of the five categories vary, recognising that areas of high cost provision of service (such as lower density rural) can expect to receive lower reliability than areas of low cost provision, thus reducing the extent of cross subsidy between categories. This balancing of infrastructure costs against reliability is appropriate in Tasmania where uniform distribution charges apply to small customers.[2]

The table below, drawn from OTTER's *Tasmanian Energy Supply Industry Performance Report 2007-08,* shows the performance standards that apply to categories of communities and the number of communities that failed in 2007-08 to meet the standards.

Community category	**Average number of interruptions**		**Average minutes off supply**		**Total no of communities below the limit for either frequency or duration**	**Total no of communities below the limit in both frequency and duration**
	TEC Community limit	Number of non-complying communities	TEC Community limit (mins)	Number of non-complying communities		
Critical Infrastructure	0.2	1/1	30	0/1	1/1	0/1
High Density Commercial	2.0	0/8	120	1/8	1/8	0/8
Urban and Regional Centres	4.0	1/32	240	14/32	14/32	1/32
Higher Density Rural	6.0	2/33	600	9/33	10/33	1/33
Lower Density Rural	8.0	1/27	720	5/27	5/27	1/27
		5/101		29/101	31/101	3/101

Of the 101 identified communities in the five categories, 31 did not meet the reliability standards of frequency and/or duration of supply outages. It is on these communities that Aurora Energy will need to target reliability improvements. This scheme provides for a more targeted approach to reliability issues and better outcomes for customers than one based on feeder performance and average network-wide performance.

It should be noted that the design of these new distribution reliability standards and monitoring of performance against these standards, has been made possible through advances in technical capability. In particular, Aurora Energy is now able to record reliability data at the distribution transformer level and has mapped individual customer connections to those transformers.

Aurora Energy is now required by OTTER to report on its performance against the new standards. It is no longer required to report on feeder performance; this may have implications for application of the STPIS in the next price determination and, as a side issue, may make interstate comparisons of performance difficult. This highlights a disconnect between the setting of standards by the jurisdiction and the application of a service incentive

[2] *Electricity Supply Industry (Price Control) Regulations 2003*

scheme to a different set of standards (that is, different parameter segments and performance targets as contained in the STPIS).

In the 2007 Electricity Pricing Investigation Final Report, the Regulator listed several reasons for discontinuing the SIS which placed financial incentives on network-wide performance, including:

- the lack of consistent historical data, especially for SAIDI, on which to establish a starting point for the new regulatory period and for the new categories;
- the difficulty in establishing the impact of past reliability improvement programs, leading to uncertainty about the actual current performance levels, and thus the starting point for such a scheme;
- the difficulty in forecasting the impact of future reliability improvement programs, leading to potentially unachievable or too easily attainable targets with the consequent financial implications;
- the risk of incorrectly matching performance targets to capital expenditure forecasts; and
- volatility in recorded network performance due to variability of weather conditions.

With respect to linking financial incentives to performance against the new distribution reliability standards, the Regulator considered that on balance:

> ... reporting on performance against the network reliability standards rather than imposing financial incentives on State-wide SAIDI and SAIFI is the most appropriate measure available without placing inappropriate risks on Aurora or its customers.

That said, OTTER supports the application of a Guaranteed Service Levy scheme to provide incentives on the DNSP to improve reliability to individual customers receiving poor performance, and this is a feature of the Regulator's 2007 price determination. However, Tasmania's present GSL scheme is linked to the categories of communities mentioned above and is, therefore, not compatible with the STPIS.

In closing, OTTER strongly recommends that Tasmania's present performance scheme be accommodated in the application of the STPIS to the AER's distribution price determination for Aurora Energy. OTTER notes that this is not beyond the realms of possibility as clause 2.2 of the STPIS makes provision for the DNSP to propose a variation of the application of the scheme; clause 3.1(d) provides for alternative methods of segmenting the network area; and clause 2.7 provides for suspension of the scheme at the DNSP's request. Given that a jurisdiction may set the standards, perhaps the STPIS should also make provision for suspension of the scheme, or its variation, at the request of the jurisdiction.

Thank you for providing OTTER with the opportunity to comment on the STPIS.

Yours sincerely

Glenn Appleyard
REGULATOR

18 March 2009