Submission to the AER Draft amended service target performance incentive scheme

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Introduction

The Public Interest Advocacy Centre

The Public Interest Advocacy Centre (PIAC) is an independent, non-profit legal centre based in New South Wales. Established in 1982, PIAC tackles systemic issues that have a significant impact upon disadvantaged and marginalised people. We ensure basic rights are enjoyed across the community through litigation, public policy development, communication and training.

Our work addresses issues such as:

- access to affordable, sustainable energy and water services;
- homelessness;
- access for people with disability to basic services like public transport, education and online services;
- Indigenous disadvantage;
- discrimination against people with mental health conditions;
- the exercise of police power;
- the rights of people in detention, including the right to proper medical care; and
- government accountability, including freedom of information.

PIAC is funded from a variety of sources. Core funding is provided by the NSW Public Purpose Fund and the Commonwealth and State Community Legal Services Program. PIAC also receives funding from the NSW Government for its Energy and Water Consumers Advocacy Program and from private law firm Allens for its Indigenous Justice Program. PIAC also generates income from project and case grants, seminars, donations and recovery of costs in legal actions.

Energy and Water Consumers’ Advocacy Program

The Energy + Water Consumers’ Advocacy Program (EWCAP) represents the interests of low-income and other residential consumers of electricity, gas and water in New South Wales, developing policy and advocating in energy and water markets. PIAC receives policy input to the program from a community-based reference group whose members include:

- Council of Social Service of NSW (NCOSS);
- Combined Pensioners and Superannuants Association of NSW;
- Ethnic Communities Council NSW;
- Salvation Army;
- St Vincent de Paul Society NSW;
- Physical Disability Council NSW;
- Anglicare;
- Good Shepherd Microfinance;
- Financial Rights Legal Centre;
- Affiliated Residential Park Residents Association;
- Tenants Union; and
- Mission Australia.

AER draft amended service target performance incentive scheme

PIAC welcomes the opportunity to comment on the AER's draft amended service target performance incentive scheme (STPIS).[1]

PIAC considers that STPIS and related reliability metrics should allow clear and consistent measurement of network performance against appropriate targets and provide an incentive to distribution network service providers (DNSPs) to efficiently meet these targets. However, the cost and revenue impact of the scheme must not exceed consumers' willingness to pay.

Over recent years, PIAC has repeatedly heard from NSW and other consumers that affordability is their number one concern in energy, and (with the exception of those in the worst served parts of the network) that they are generally well served in terms of network reliability.

This is reflected in consumer research commissioned in 2017 by Essential Energy in regional NSW. In seven deliberative forums, participants were presented with a cost/reliability trade-off question after an educative process to help them understand the interaction of energy cost and reliability. According the published results from these forums, 66% of Essential's customers wished to pay $40 less a quarter and accept a lower level of reliability in return.[2] Essential Energy, however, has no long-term plan to allow reliability levels (expressed as SAIDI and SAIFI) to return to the lower level that better reflects consumers' expressed willingness to pay, and has advised PIAC that STPIS arrangements disincentivise them from doing so.

This suggests that current STPIS arrangements may have the effect of locking in excessive levels of reliability arising from historical deterministic reliability standards.

In PIAC's view, the AER should ensure that STPIS incentives are appropriately targeted to maintain or improve reliability levels only to the extent that consumers are willing to pay. This may require further changes that extend beyond that scope of this review. PIAC asks the AER to consider what rule changes, or other changes, might be needed to fully achieve this outcome.

Recommendation 1

PIAC recommends that the AER consider if any rule changes, or other changes, may be required to ensure STPIS does not result in DNSPs maintaining or improving reliability levels beyond what consumers are willing to pay for.

1 AER, Draft Electricity distribution network service providers Service target performance incentive scheme, December 2017, <https://www.aer.gov.au/system/files/AER%20-%20Draft%20amended%20service%20target%20performance%20incentive%20scheme%20-%20December%202017.pdf>.

2 See: "Due to the current satisfaction with reliability, a consistent finding was that the vast majority were not willing to pay more to reduce their outage duration. In fact, in the forums two thirds (66%) wished to pay $40 less a quarter to have 1-2 more outages a year showing that they were willing to accept slightly lower levels of 'reliability' for a slightly lower 'cost'" - Woolcott Research & Engagement, *Engagement Programme Summary Report – Phase 1, Prepared for Essential Energy*, June 2017, 8, <http://www.woolcott.com.au/EssentialEnergy/EssentialEnergyEngagementProgrammePhase1SummaryReport.pdf>.

Ratio of SAIDI and SAIFI incentive rates

PIAC supports the AER's proposal to change the ratio of SAIDI/SAIFI incentives from 50/50 to 60/40 in the STPIS.

PIAC concurs with the AER that the current equal weighting of STPIS payment value between SAIFI and SAIDI has not incentivised DNSPs to efficiently invest in network reliability. As the AER notes, the current weighting has resulted in a bias towards capex to improve supply reliability and reduce SAIFI over the opex required to decrease outage duration and reduce SAIDI.[3]

In the context of PIAC's concerns about consumers' willingness to pay for increasing reliability, a bias towards capex on costly network assets is not in the long-term interests of consumers. These assets will remain in the regulated asset base, and therefore earn a rate of return from consumers, for the life of the asset.

PIAC supports the AER's proposal as a means of removing the bias of preferring expensive SAIFI-related network augmentation over SAIDI-improving opex.

Recommendation 2

PIAC recommends that the AER proceed with the proposed amendment to change the SAIDI/SAIFI ratio from 50/50 to 60/40.

Exclusions and treatment of major event days

PIAC supports the AER's proposal to exclude the following load interruptions from calculating distribution reliability measures under STPIS:

- Load interruptions caused by the exercise of any obligation, right or discretion imposed upon or provided for under jurisdictional electricity legislation and national electricity legislation applying to a DNSP;
- Load interruptions caused or extended by a direction from state or federal emergency services where that direction is not in response to a fault in, or operation of, the network; and,
- Load interruptions by a failure of transmission connections assets where the interruption is not due to insufficient connection planning or any act or omission by the DNSP.[4]

In all cases, these load interruptions are outside of the DNSP's control and should therefore not impact on the STPIS incentives designed to reward, or penalise, DNSPs for their control of network reliability.

Furthermore, the AER should adopt the AEMC recommendation to create a new exclusion for catastrophic events.[5]

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3 AER, Explanatory Statement – Proposed amendment of the Service Target Performance Incentive Scheme (STPIS), December 2017, 13, <https://www.aer.gov.au/system/files/AER%20-%20Explanatory%20statement%20-%20Draft%20amended%20service%20target%20performance%20incentive%20scheme%20-%20December%202017.pdf>.

4 Ibid, 17.

5 AEMC, Review of Distribution Reliability Measures, Final Report, September 2014, 26-31.

In PIAC's submission to the AER's issues paper regarding STPIS and the *Distribution Reliability Measures Guideline*, we noted that the current inclusion of catastrophic events has the potential to skew a network's overall reliability measure and be used to justify reliability-related expenditure that consumers are not be willing to pay for.[6]

In the explanatory statement associated with the STPIS amendment, the AER directly responded to PIAC's concerns, stating:

> …we consider that separately discounting of catastrophic days' effects would make the distributor's supply reliability measures appear better than not separately discounting catastrophic days. Hence, such treatment of catastrophic days is unlikely to be a basis for more expenditure to maintain the network.[7]

In PIAC's view, the purpose of separately discounting the effects of catastrophic events would be to reflect the ability of DNSPs to efficiently control the reliability of their networks.

Catastrophic events are outside of the control of a DNSP, infrequent and, over the long term, unpredictable in terms of the location and nature of impact. The types and extent of network capex measures required to limit the likelihood of outages associated with these events (such as undergrounding powerlines and building in higher levels of redundancy) are unlikely to ever reflect the value consumers place on reliability; therefore, they are unlikely to proceed as efficient or justified investments.

By including such events in the calculation of DNSPs' reliability measures, the AER is likely to underestimate the success of DNSPs in maintaining a secure, reliable network. DNSPs then would be incentivised to spend more on assets to ensure a higher reliability level than consumers are willing to pay for.

Further, including the impact of catastrophic events in wider reliability outcomes has been shown to trigger political reactions of a nature that are usually expensive and rarely in the long term interest of consumers.

It would be consistent with the AER's priority of limiting the incentive for inefficient capex that catastrophic events should not be included in measurement of DNSP's effectiveness in controlling reliability.

The main reason given by the AER for not separately discounting catastrophic events is that there is no method to identify these events in a manner that would apply consistently for all DNSPs.[8] PIAC acknowledges that this would make it difficult for the AER to include catastrophic event discounts in the current amendment but does not accept this as a reason to do so.

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6 PIAC, *Submission to Draft Distribution Reliability Measures Guideline*, August 2017, 1, <https://www.piac.asn.au/wp-content/uploads/2018/02/17.08.10-PIAC-sub-to-draft-distribution-reliability-measures-guideline.pdf>.

7 AER, Explanatory Statement – Proposed amendment of the Service Target Performance Incentive Scheme (STPIS), December 2017, 15.

8 Ibid, 19.

PIAC concurs with the AER that substantial further research is needed to find an alternative method and is of the view that the AER should undertake this research with a view to separately discounting catastrophic events from distribution reliability measures.

Recommendation 3

PIAC recommends that the AER proceed with the three proposed amendments to include new STPIS exclusions.

Recommendation 4

PIAC recommends that the AER work to exclude catastrophic events from distribution reliability measures as soon as possible to ensure that DNSPs are not incentivised to invest in reliability-related assets beyond what consumers are willing to pay for.

Further engagement

PIAC would welcome the opportunity to discuss these issues in more depth. For any queries please contact:

- Policy Team Leader, Energy and water, Craig Memery at cmemery@piac.asn.au or on (02) 8898 6522; or
- Policy Officer, Energy and water, Tim Harrison at tharrison@piac.asn.au or on (02) 8898 6518.