

19 November 2021

Mr Sebastian Roberts  
General Manager, Expenditure  
Australian Energy Regulator



Submitted via email to: [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au)

Dear Mr Roberts,

### **Essential Energy - Cost Pass Through Application 2019-20 Bushfires**

The Public Interest Advocacy Centre (PIAC) is a leading social justice law and policy centre. Established in 1982, we are an independent, non-profit organisation that works with people and communities who are marginalised and facing disadvantage. PIAC builds a fairer, stronger society by helping to change laws, policies and practices that cause injustice and inequality. The Energy and Water Consumers' Advocacy Program (EWCAP) represents the interests of low-income and other residential consumers of electricity, gas and water in NSW. The program develops policy and advocates in the interests of low-income and other residential consumers in the NSW energy and water markets.

PIAC welcomes the opportunity to respond to the Australian Energy Regulator's (AER) consultation on Essential Energy Cost Pass Through Application - 2019-20 Bushfires.

PIAC supports allowing Essential Energy to recover efficient costs incurred as a result of the bushfires that were not provided for in the revenue allowance, and the proposal that cost recovery from consumers be smoothed across two years. We expect the AER to determine the efficient and prudent amount to allow and the specifics of how to smooth the recovery.

### **Resilient and fair cost recovery and risk allocation in a changing climate**

Essential Energy's application is a reminder that damage to network infrastructure from extreme weather events is likely to increase and that the impact of extreme weather events needs to be considered and planned for across a number of regulated processes.

The impact of bushfires has been demonstrated in several recent cost pass-through applications. It highlights the importance of risk management for extreme weather events and how standards for reliability consider such events.

With a changing climate and projections of more common and severe extreme weather events, we need mechanisms that result in a resilient energy system where costs and risks are determined and distributed fairly. Essential Energy's application to the AER highlights the core issues of risk management and how standards for reliability are to be treated.

The questions of who pays for the damage caused by extreme weather events and how are also about how risk is managed by regulated businesses.

### **Understanding consumer preferences in cost recovery for extreme weather events**

In general, risk should be borne by those best placed to manage it, and consumer preferences regarding trade-offs should inform how risks and associated costs are allocated. For bushfire and weather-related expenditure, this should be understood as consumer preference for either:

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- lower long-term average price with the trade-off of higher year-on-year volatility, with costs predominantly recovered through cost pass through events and consumers carrying more risk. Under this approach consumers would carry the risk of repair or replacement costs being passed through as damage occurs.
- lower year-on-year volatility with the trade-off of higher average price, with costs predominantly fixed in revenue determinations and the DNSP managing consumer exposure to risk. Under this approach network businesses would be expected to internalise much risk of extreme weather events through planning and decision making.

In this submission PIAC is not commenting on which approaches are (or were) more appropriate for Essential Energy, but emphasising the need to understand and apply consumer preferences. PIAC recommends Essential Energy uses its program of community engagement for the pending revenue period to do so.

### **Efficient allocation of network expenditure for extreme weather events**

Under either approach to applying consumer preferences for cost recovery, Network Service Providers (NSP) must still consider the probability and consequence of different types of events and different types of assets to determine how to optimally allocate capex and opex to manage these risks.

Where infrastructure could be made materially more resilient at less cost than the value-at-risk of extreme weather events, the businesses may justify augmenting certain infrastructure with the expense recovered under their normal revenue allowances.

However, as it is difficult to predict where, when and how extreme weather will strike and how it will impact infrastructure, it may often be more cost effective to improve the NSP's operational capacity to respond to extreme events. Unlike capital spend, some resources for emergency repairs can also be shared with other NSPs, improving efficiency and resilience.

### **Other matters regarding expenditure and cost recover for extreme weather events**

All approaches rely on assumptions about the nature and recoverability of major outages. Other factors to consider include the role of insurance, the willingness of insurers to manage climate risk and the extent of network businesses' and regulators' responsibility to use climate modelling in predicting infrastructure vulnerability to extreme weather events.

### **Continued engagement**

PIAC welcomes the opportunity to meet with the AER, Essential Energy, and other stakeholders to discuss these issues in more depth.

Yours sincerely

**Craig Memery**

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