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**REF: EPR0028 Review of the national framework for transmission reliability – Issues Paper**

Dear Commissioners,

Thank you for the opportunity to comment on the Issues Paper of your review of the national framework for transmission reliability.

As the peak body for the community services sector in South Australia, SACOSS has a long-standing interest in the delivery of essential services and particular the cost of basic necessities like electricity because they impact greatly and disproportionately on vulnerable disadvantaged people.

**Background and Introduction**

The AEMC's review of transmission reliability frameworks is one of a number of network related reviews and inquiries currently in play in the NEM. SACOSS does not have the capacity to engage in all of these processes nor to necessarily go into detail when it does engage.

The Issues Paper confirms a preference for an 'economic redundancy approach' similar to what is already in place in South Australia. For this reason SACOSS feel it important to contribute its perspective to the AEMC's work.

This short submission only responds to two of the Issues Paper topics. Firstly, in relation to flexibility provisions and secondly, in relation to the use of the Value of Customer Reliability (VCR).

**Flexibility**

The Issues Paper discusses the issues associated with providing flexibility “...such that TNSPs could advance or defer the timing of an investment that would be otherwise needed to meet reliability standards, where it can be shown that the economics of the investment have changed since the standards were set.”<sup>1</sup>

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<sup>1</sup> AEMC Issues Paper, page 27

**Question 5 Providing for flexibility in transmission reliability**

- a) Is there merit in having a flexible approach to reliability standards under the national framework?
- b) Should Grid Australia's proposed criteria of the need to conduct a RIT-T and a material change in circumstances be used to determine when TNSPs are able to undertake a further economic assessment which would allow them to depart from their transmission reliability standards?
- c) How should a "material change in circumstances" be defined?
- d) Should any other requirements be met before TNSPs are able to depart from their standards?

SACOSS is of the view that there is some merit in having a flexible approach as long as the benefits of doing so are shared with consumers. SACOSS is acutely aware of the incentives apparent to network businesses and is experienced in the ability of these businesses to respond to them. It would be naive to assume otherwise. In this context, the inherent incentive is to extend the time lag between revenue raised (under the formal revenue regulation process with the AER) and expenditure incurred.

SACOSS asks the AEMC to proceed on the basis that this underlying incentive exists and that the consumer interest is served when any benefits of investment deferral are shared with them.

**Question 7 Potential use of the contingent project mechanism**

- a) If a change in the revenue determination process is required, would the use of the contingent project mechanism be an appropriate way to address this?
- b) What implications could the increased use of the contingent project mechanism have for the role of ex ante revenue determinations in incentivising efficient investment?

The AER's very recent final decision<sup>2</sup> on ElectraNet's 2013-18 regulatory control period approves a list of 11 contingent projects for a contingent capex of \$1490m over the period, more than twice the final decision's approved capex allowance of \$690m. While SACOSS accepts that there is some merit in using the contingent project mechanism, the outturn in this recent case is that consumers are left with a potentially significant uplift on what otherwise appears to be a modest revenue determination. Applying the WACC of 7.5% to the full contingent project list would add over \$110m pa to allowable revenue over-and-

<sup>2</sup> <http://www.aer.gov.au/node/16617>

above the otherwise approved Maximum allowed revenue of an average \$315m pa – around 35%.

SACOSS harbours concerns over this potential and the different level of scrutiny that may apply to contingent projects as opposed to what would be the case under the formal regulatory determination. As noted by the Issues Paper at page 32:

“Therefore, if the scope of the contingent project mechanism was extended such that a flexible approach could be taken to investments lower than the current \$30m threshold, this might lead to more projects being subject to lower levels of regulator[y] scrutiny. This could occur as the AER has less time to assess proposed expenditure under the contingent project mechanism than it would if this expenditure was being considered as part of the revenue determination process. The increased use of the contingent project mechanism could also increase the administrative burden on the AER.”

In summary, SACOSS is supportive of flexibility but concerned as to how the consumer interest can be preserved.

## **VCR**

In general terms, SACOSS is of the view that the interests of residential consumers should be interpreted as:

- Households should only pay for the reliability they want, and;
- Households should get the reliability they pay for.

The matters raised in the Issues Paper have a strong relationship to the NEM’s treatment of the Value of Customer Reliability (VCR). VCR represents the dollar value that customers place on the reliable supply of electricity – an indicator of customers’ *willingness to pay* for not having supply interrupted.

VCR is not a parameter that can be measured directly and it is not a parameter that has a single value applicable to all customers across Australia’s National Electricity Market. It is a parameter that must be approximated or estimated and the methods by which this is done will impact on the uncertainty with which it can be determined. In turn, the uncertainty with which it can be determined should influence the way in which it is used.

In submissions<sup>3</sup> to ESCOSA during the 2011 Review of the ETC, concerns were raised about the use of a state-wide average VCR (as a measure of consumer’s willingness to pay) of \$46k/MWh by AEMO and ElectraNet as compared to the \$15-20k assessed for residential consumers:

“... the implication of this is that significant transmission investment will exceed the willingness to pay of the most numerous customer class. This represents a significant challenge to the economic efficiency of these investments.”

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<sup>3</sup> <http://www.escosa.sa.gov.au/library/120215-ElectricityTransmissionCodeDraftDecisionSubmission-StKitts.pdf>

It is also noted that ESCOSA support a more deeply considered approach to the use of VCR in network reliability matters<sup>4</sup>:

“The Commission is keen that an appropriate VCR is developed for South Australia, but is also interested in the need for the development of exit point-specific VCRs; or at least, regional VCRs in respect of the seven SA distribution regions as defined in the Electricity Distribution Code.”

**Question 10 Use of the value of customer reliability**

**a) Should a range of values around the VCR be used to assess reliability levels at connection points?**

**b) What range of VCR values should be used?**

In relation to the Issues Paper Question 10 ‘Use of the value of customer reliability’, SACOSS would like to re-state its view that the range of VCR values used must include that attributed to households. Further, the use of VCR must reflect the uncertainty with which it has been determined.

Submissions to past AEMC<sup>5</sup> and AEMO<sup>6</sup> processes by Andrew Nance, SACOSS Member and end-use consumer representative on the AEMC’s Reliability Panel, have outlined these matters in more detail.

SACOSS notes the Productivity Commission concerns over the historic approach to VCR derivation and use<sup>7</sup>:

“From a methodological perspective, the existing Australian data seem to have several major flaws. ... Theoretically, a single VCR also fails to account for differences in the mix of customers affected by an investment for reliability. ... AEMO uses the same weighted customer costs in areas with different customer profiles.”

SACOSS also notes that AEMO’s most recent publication on the matter of VCR acknowledges matters relevant to low income consumers<sup>8</sup>. The AEMO paper also refers to

<sup>4</sup> <http://www.escosa.sa.gov.au/library/130405-AmendmentsToRevisedElectricityTransmissionCode-DraftDecision.pdf>

<sup>5</sup> St Kitts Associates submission to EPR0027 at <http://www.aemc.gov.au/Media/docs/St-Kitts-Associates---120711-3a99b294-f470-476d-8223-e9d49e8e0905-0.PDF>

<sup>6</sup> AEMO’s 2011-12 inquiry into VCR at <http://www.aemo.com.au/Electricity/Policies-and-Procedures/Planning/National-Value-of-Customer-Reliability-VCR> includes two submissions from St Kitts Associates: <http://www.aemo.com.au/Electricity/Policies-and-Procedures/Planning/~media/Files/Other/planning/0409-0013%20pdf.ashx>, <http://www.aemo.com.au/Electricity/Policies-and-Procedures/Planning/~media/Files/Other/planning/0409-0016%20pdf.ashx>

<sup>7</sup> Productivity Commission Inquiry into Network Regulation, Draft Report Chapter 14 page 476 ([http://pc.gov.au/\\_data/assets/pdf\\_file/0014/120065/17-electricity-draft-chapter14.pdf](http://pc.gov.au/_data/assets/pdf_file/0014/120065/17-electricity-draft-chapter14.pdf))

<sup>8</sup> [www.aemo.com.au/Consultations/National-Electricity-Market/Value-of-Customer-Reliability-Issues-Paper](http://www.aemo.com.au/Consultations/National-Electricity-Market/Value-of-Customer-Reliability-Issues-Paper), section 6.2.5 at page 22.

recent comments made by the Productivity Commission on the relationship between VCR and income<sup>9</sup>.

## Summary

SACOSS welcomes the opportunity to contribute to the AMECs review of transmission reliability frameworks. SACOSS is encouraged by recognition of the South Australian framework as having many desirable attributes. In our experience, two key topics deserve specific attention.

Firstly, in the provision of flexibility mechanisms: SACOSS is supportive of flexibility but concerned as to how the consumer interest can be preserved. SACOSS asks the AEMC to proceed on the basis that underlying incentives exist for regulated entities to maximise the time lag between revenue raised and expenditure and that the consumer interest is served when any benefits of investment deferral are shared with them.

SACOSS is unable to support any changes to the regulatory arrangements that will not confidently ensure consumers share in the benefits of the proposed changes.

Secondly, in the derivation and use of the value of customer reliability: SACOSS remains concerned the investments continue to be made based on VCR values that are multiples of that expressed by households, especially low-income households.

SACOSS would be pleased to engage further in progressing these matters. We thank you in advance for your consideration of our comments. If you have any questions relating to the above responses, please contact SACOSS Senior Policy Officer, Jo De Silva on 8305 4211 or via [jo@sacoss.org.au](mailto:jo@sacoss.org.au).

Yours sincerely,



Ross Womersley  
Executive Director

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<sup>9</sup> Productivity Commission Inquiry into Network Regulation, Draft Report Chapter 14 page 480