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Review of Economic Benchmarking of Transmission Network Service Providers – Positions Paper

Energy Networks Australia appreciates the opportunity to make a submission to the Australian Energy Regulator's (AER) Review of Economic Benchmarking of Transmission Network Service Providers – Positions Paper (August 2017).

Energy Networks Australia is the national industry body representing businesses operating Australia's electricity transmission and distribution and gas distribution networks. Member businesses provide energy to virtually every household and business in Australia.

Background

Energy Networks Australia supports robust benchmarking arrangements as a tool to assist the AER to determine efficient revenue and price outcomes for customers under an incentive-based regulatory regime. However, as stated in our recent submission on the AER's related Issues Paper (April - May 2017), shortcomings have arisen when applying benchmarking methodologies to Australian Transmission Network Service Providers (TNSPs) mainly due to the small sample size available and the geographical diversity and varied operating environments relevant to these businesses.

In essence, these are fundamentally different businesses operating, managing and maintaining electricity transmission networks with diverse market and climatic conditions, as well as distinct network densities and configurations. This has been recognised by the AER in its own previous reports[1].

The limitations of these measures should be clearly recognised with a view to ensuring they are considered in a robust way and are made fit-for-purpose.

[1] Refer Final Annual Benchmarking Report, Electricity Network Service Providers, 2016, p.13

General observations

Given this background, industry understands that economic benchmarking can be used to measure an individual TNSP's relative performance over time. As recognised in previous reviews, applying economic benchmarking to Australia's transmission networks can be a significant challenge. Therefore, TNSPs consider that economic benchmarking should be applied as a diagnostic tool to assess reasonableness of forecast expenditures in networks' revenue proposals, rather than being used deterministically.

In this context, economic benchmarking by the AER can play an important role in identifying areas of higher than expected forecast expenditures in networks' revenue proposals. This may assist a regulator to focus upon areas for further investigation and review, reducing regulatory costs and increasing benefits for consumers.

In respect of the benchmarking methodology, Energy Networks Australia notes that adopting alternative model specifications can lead to significant variations in measured Multilateral Total Factor Productivity (MTFP) and relative rankings across the businesses[2]. It is therefore important for any potential changes to the transmission output measures to be given due and proper consideration by the AER, regulated businesses and other interested stakeholders.

Specific Issues on AER's Positions Paper

Energy Networks Australia transmission members are of the following consensus views:

- That capping the contribution of a supply reliability measure, is a reasonable and sensible move to mitigate against the significant impacts on transmission output results, of one-off outages. This should help to address instances where previous disproportionate results negatively impacted not only individual, but also industry transmission output. This was exemplified by AusNet Services' experience in Victoria during 2009. Therefore, we support the proposed application of a reliability cap of 5.5 per cent of gross revenue on the output share of energy not served.
- That the AER must utilise a stable Total Factor Productivity model. Given, the proposed changes to output cost share weights derived from a Leontief cost function model (applied to data for 2006 to 2015). The use of the Leontief model is supported, as long as the modelling and outcomes are robust, and is retained by the AER for a number of years.

[2] Nunn, O. and Whitfield, A. (2015). Review of the AER transmission network benchmarking study & its application to setting TransGrid's opex rate of change - A report prepared for TransGrid. Sydney: Houston Kemp, p.13.

- Further development of operating environment factors (OEFs) analysis should be an AER priority. However, we caution against a *carte blanche* approach to Economic Insights' proposal to expanding the TNSP EB RIN data collection to include the MVA rating of each TNSP entry and exit point[3]. This could be a potentially significant and costly exercise that should only be undertaken if it will result in the collection of consistent and meaningful data that is 'fit for the purpose' for benchmarking, such that the costs of collection are outweighed by the benefits.

A Way Forward

Transmission network businesses remain keen to engage and work collaboratively with the AER to capture opportunities to improve the AER's economic benchmarking approaches. We also consider that this current consultation should not be a lost opportunity for the AER to further consider existing definitions and whether the current suite of parameters still accurately reflect what was originally intended to be measured. A more cooperative process should allow the AER and networks to streamline and refine the suite of data requirements for transmission benchmarking.

Ultimately, an improvement in the quality and consistency of the data provided by TNSPs should be an important regulatory objective. Such improvements are expected to deliver better information for decision-making over time and more efficient regulatory processes, both of which *ceteris paribus*, should strongly benefit consumer interests.

Energy Networks Australia maintains its support for the AER undertaking a wider review that can facilitate collaboration, shared capacity development and the identification of principles and techniques, which may enhance the development and use of economic benchmarking. Energy Networks Australia notes that both the Issues Paper[4] and the Positions Paper flags the AER's intention to consider material OEFs and the impact of differences in capitalisation policies separately to the current review process. Energy Networks Australia welcomes this initiative by the AER, and our members look forward to participating constructively in that process which should desirably occur in the near future.

Recommendation

Independent testing and evaluation is critical to examining whether benchmarking techniques are at best-practice levels. It is therefore recommended that the AER obtain an independent expert peer review of the methodology, models and data choices proposed ahead of any implementation.

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[3] As outlined on page 37 of the Positions Paper.

[4] Issues Paper, p.2.

Energy Networks Australia understands that our transmission members will be providing their own individual submissions on related issues for the AER's further consideration.

Should you have any additional queries, please contact Norman Jip, Energy Network Australia's Senior Program Manager – Transmission on (02) 6272 1521 or njip@energynetworks.com.au.

Yours sincerely

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