

8 August 2013

Mr John Pierce
Chairman
Australian Energy Market Commission
Level 5, 201 Elizabeth Street
Sydney NSW 2000

Dear Mr Pierce

The NSW DNSP's Response to the Draft Rule Determination – National Electricity Amendment (Network Service Provider Expenditure Objectives) Rule 2013.

The NSW Distribution Network Service Providers, Ausgrid, Endeavour Energy and Essential Energy (the NSW DNSPs) welcome the opportunity to provide this joint response to the *Draft Rule Determination – National Electricity Amendment (Network Service Provider Expenditure Objectives) Rule 2013*.

The NSW DNSPs support the AEMC's decision to make a more preferable Rule that gives effect to the key objectives of the Standing Council of Energy and Resources (SCER) Rule change proposal by amending its original drafting of the relevant clauses. In particular, we support the key reasons underpinning the AEMC's decision; namely, that:

- While there is a need to clarify in the Rules how the existing expenditure objectives relating to reliability, security and quality of supply work together, SCER's drafting is too prescriptive and complex.
- It is appropriate that primacy is given to jurisdictional standards relating to reliability, security and quality of supply as these measures have been set by a body allocated to the role.
- There is a risk of inefficiency if the decision of the standard setting body is not given effect in the regulatory process, particularly if one standard is used to assess compliance with regulatory obligations, but a different standard is used to assess regulatory proposals.
- Giving effect to the standards set by the allocated standard setting body will provide greater clarity to NSPs in preparing their regulatory proposals and the AER in assessing these proposals. This is because the draft Rule provides that the expenditure allowance determined by the AER would be based on regulatory obligations or requirements for these measures.
- If part of an NSP's network is subject to a regulatory obligation or requirement for reliability, security or quality and another part is not then the draft Rule allows for a different standard or benchmark to be assigned to each of these parts.
- It is not appropriate to amend the expenditure objectives for safety or remove expenditure objectives 3 and 4.

Consequently, the NSW DNSPs share the AEMC's view that the amended draft Rule is likely to better contribute to the National Electricity Objective (NEO) than SCER's proposed Rule.

We note that the AEMC's reasons for not accepting the proposed Rule are consistent with the concerns raised in our 7 March 2013 submission, and further reflect the concerns raised by other DNSPs.

While we are very supportive of the amended draft Rule, we would like to clarify two aspects of the AEMC's assessment of the Rule proposal. The first relates to the AEMC's comments regarding the operation of the expenditure objectives as a whole. We support these statements and consider that they are consistent with the way in which the AER must assess support costs associated with operating a safe, reliable and secure network.

A significant proportion of a DNSP's capital and operating expenditure relates to support function costs (such as IT, property, fleet and finance) that enable a DNSP to meet its network objectives and corporate obligations. As noted in the draft Rule determination, "...the AER must assess proposals against all of the objectives. In doing so it will assess overall efficiency to meet all of the objectives. It must also consider whether the expenditure reasonably reflects the expenditure criteria in the NER. In particular it must assess whether the costs are efficient and that which a prudent operator would incur"¹. Whilst it may be difficult to separately attribute support costs to specific objectives, we would contend that this is not necessary so long as the AER is satisfied that support costs are required to meet the objectives as a whole and meet its overall assessment of efficiency.

The second relates to the proposed objective (4) and the objective of maintaining the safety of the distribution system. In its assessment, the AEMC recognised that it would not be appropriate to limit the expenditure allowed for operating a safe network to the regulatory standards as this may inadvertently reduce the level of safety due to current safety standards being contained in voluntary industry codes, Australian Standards and company rules. We support this approach. We note however that the AEMC included a clarification that retaining the effect of the current NER objectives in respect of safety would not permit DNSPs to increase the level of expenditure they may seek by increasing the safety standard set out in a voluntary code, it would only allow expenditure sufficient for safety standards to be maintained². Whilst we agree with this rationale to a point, we are concerned to ensure that it would not prevent DNSPs from responding to issues it may identify with the safety of their networks.

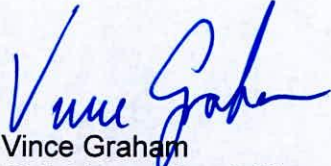
As prudent asset managers, DNSPs constantly review safety risks arising from operating network assets. This analysis may reveal that the current level of risk for a network's assets is too high. This may be as a result of investigation of failure modes, evidence on recent safety incidents or external inquiries such as royal commissions or coronial inquiries. In such circumstances, DNSPs undertake detailed investigations to determine the most effective way to mitigate the risk to an acceptable level. This may include targeted maintenance programmes or replacement of assets. At one level this could be seen as improving the safety of the network, rather than maintaining the level of safety, whereas in fact the improvement should be regarded as maintaining the safety of the network by bringing it up to a standard of safety which could reasonably be expected by consumers and the community more generally. It is of course a matter for the AER to assess and form a view on the efficiency of such expenditure. We urge the AEMC to ensure that its amendments to the expenditure objectives will not result in DNSPs being restricted in responding to identified risks and improving the safety of the network in these circumstances.

¹ AEMC 2013, Network Service Provider Expenditure Objectives, Draft Rule determination, 27 June 2013, Sydney p 22.

² Op Cit p 10 at footnote 24.

If you would like to discuss this matter further, please contact Mr Mike Martinson, Group Manager Regulation at Networks NSW on (02) 9249-3120 or via email at michael.martinson@endeavourenergy.com.au.

Yours sincerely,



Vince Graham

Chief Executive Officer

Ausgrid, Endeavour Energy and Essential Energy