1 Small Scale Incentive Scheme

Contents

1 Nature and authority

1.1 Objectives

The Objectives for this scheme are that the scheme:

(a) Is consistent with the national electricity objective in section 7 of National Electricity Law (NEL)

(b) Is consistent with clause 6.6.4 of the NER which requires that in developing and implementing a small scale incentive scheme, the AER must take into account:

   (1) *Distribution Network Service Providers* should be rewarded or penalised for efficiency gains or losses in respect of their *distribution systems*;

   (2) The rewards and penalties should be commensurate with the efficiency gains or efficiency losses in respect of a distribution system, but a reward for efficiency gains need not correspond in amount to a penalty for efficiency losses;

   (3) The benefits to electricity consumers that are likely to result from efficiency gains in respect of a distribution system should warrant the rewards provided under the scheme, and the detriments to electricity consumers that are likely to result from efficiency losses in respect of a distribution system should warrant the penalties provided under the scheme;

   (4) The interaction of the scheme with other incentives that Distribution Network Service Providers may have under the Rules; and

   (5) The capital expenditure objectives and the operating expenditure objectives.

2 The Customer Service Incentive Scheme

2.1 General application of the *scheme*

(a) The parameters and the maximum revenue increment or decrement that a DNSP can receive for a given level of customer satisfaction are prescribed in this scheme.

(b) The AER will, in the distribution determination to which this scheme applies, determine the following in accordance with the NER generally, and with this scheme:

   (1)   Each applicable component and parameter to apply to a DNSP.
   (2)   The revenue at risk to apply to each applicable component and parameter
   (3)   The incentive rate to apply to each applicable parameter
   (4)   The performance target to apply to each applicable parameter in each regulatory year of the regulatory control period

2.2 Structure of the *scheme*

(a) This scheme comprises the following components:

   (1)   The parameters that may apply
   (2)   The requirements with which the parameters must comply
   (3)   The targets which apply to each parameter
   (4)   The incentive rate to apply to each parameter
   (5)   The maximum revenue increment or decrement that a DNSP may receive for each parameter

(a) A DNSP's revenue is increased (or decreased) based on changes in customer satisfaction, as assessed by the AER in accordance with this scheme.

2.3 Revenue at risk

(a) The default maximum revenue increment or decrement (the revenue at risk) for the scheme components in aggregate for each regulatory year within the regulatory control period shall be 0.5% that is, the sum of the H-factors associated with all parameters must lie between +0.5% (the upper limit) and –0.5% (the lower limit).

(b) A DNSP may propose a higher or lower revenue at risk up to a maximum of 1% as allowed in clause 6.6.4(d)(1) of the NER.

(c) A DNSP may propose an individual cap on revenue at risk for each scheme component.

2.4 Transitional arrangements

(a) Transitional issues may arise from one regulatory control period to the next regulatory control period if the scheme's parameters or other attributes are altered or the scheme is discontinued.

(b) The AER will give consideration to an arrangement proposed under this scheme that reduces the impact of any transitional issues.

(c) The AER shall decide on the appropriateness of the arrangement to address a transitional issue on the basis of:

(1) Materiality of the issue

(2) Reasonableness and fairness to the DNSP and customers

(3) Consistency with the objectives as set out in clause 1.5.

(d) To avoid doubt, revenue increments or decrements calculated in relation to performance in the current regulatory period are expected to be applied in the subsequent regulatory period regardless of whether this scheme is discontinued in the subsequent regulatory period.

2.5 Suspension of the scheme

(a) At any time during a regulatory control period in which a scheme applies to a DNSP, the AER may decide whether the scheme or a component of the scheme should be suspended for a regulatory control period or a portion of a regulatory control period.

(b) A DNSP proposing that the scheme or a component of the scheme be suspended must provide in writing its reasons for proposing the suspension.

(c) The AER will publish its reasons for deciding to suspend or to not suspend the scheme. Before making a decision to suspend a scheme, the AER will consult with the relevant DNSP and such other persons as it considers may be affected by and/or have an interest in such a decision.

3 Performance incentive scheme parameters

(a) A DNSP may propose the parameters to apply during the relevant regulatory control period.

(b) The AER may require a DNSP to apply any or all of the parameters referred to in clause 3(a) during the relevant regulatory control period where the AER considers it would satisfy the objectives of the scheme described in clause 1.1.

(c) Performance targets and incentive rates will be applied to each parameter segment.

4 Performance targets

(a) The performance targets to apply during the regulatory control period must not deteriorate across regulatory years and should be based on average performance over the past five regulatory years, modified by the following:

  (1) Any customer satisfaction improvements completed or planned where the customer satisfaction improvements are:

  (i) Included in the expenditure program proposed by the DNSP in its regulatory proposal, or

  (ii) Proposed by the DNSP, and the cost of the improvements is allowed by the relevant regulator, in the DNSP's previous regulatory proposal or regulatory submission, and

  (iii) Expected to result in a material improvement in customer satisfaction.

(b) Where a DNSP proposes a performance target modified in accordance with clause (a), the DNSP must provide in writing an explanation of how the modified performance target has been calculated.

(c) Where five regulatory years of data is not available the AER may approve a performance target based on an alternative methodology or benchmark where the AER is satisfied that the performance target meets the objectives set out in clause 1.1.

(d) A performance target deadband may be approved by the AER. A performance deadband is a level of improvement or deterioration for which no reward or penalty will be applied.

5 Incentive rates

(a) Where practicable, the incentive rates for the parameters should be based on the value that customers attribute to the level of service proposed.

(b) Where the requirements in clause 5(a) cannot be complied with, the DNSP must propose an appropriate alternative methodology for setting an incentive rate that is consistent with the objectives set out in clause 1.1.

(c) A different incentive rate may apply to each scheme parameter.

(d) Incentive rates are calculated at the commencement of the regulatory control period and apply for the duration of the regulatory control period.

6 Exclusions

(a) The DNSP may make a proposal for exclusions, as long as the proposal is consistent with the objectives set out in clause 1.5.

7 Information and reporting requirements

(a) A DNSP must report on its annual performance against the parameters applicable to it as set out in the relevant distribution determination in accordance with any applicable regulatory information instrument.

(b) A DNSP must provide details annually of each of the exclusions under clause 6 that has applied in calculating the revenue increment or decrement made under the scheme.

(c) The AER may review the customer satisfaction information relevant to the scheme that a DNSP is required to provide annually under any applicable regulatory information instrument.

(d) In undertaking the review referred to in clause (c), the AER may consider:

   (1) The appropriateness and accuracy of the DNSP's data collection, reporting and recording processes and systems

   (2) Whether the performance data reported is consistent with the parameter definitions contained in appendix A and the distribution determination

   (3) Whether the revenue increment or decrement proposed by the DNSP has been calculated in accordance with this scheme.

(e) A DNSP must notify the AER in writing as soon as it becomes aware of, or plans any material changes to data collection or recording methods used by the DNSP to record and report on the DNSP's performance against the DNSP's parameters.

(f) Any notice provided to the AER under clause 7.3(a) must include an assessment of whether the changes to the data collection or recording methods no longer allow the DNSP to accurately record and report on the DNSP's performance against one of the parameters applicable to the DNSP.

(g) The AER may amend or suspend this scheme as a result of the DNSP's new data collection methods.

8 Appendix C: Adjustments to allowed revenue

A DNSP's annual revenue (through average tariffs for all customers) is increased (or decreased) based on changes in customer satisfaction from regulatory year to regulatory year. The H-factor applies only to standard control services.

Clause 6.2.6 of the NER requires that the control mechanism for standard control services must be of the prospective CPI minus X form, or some incentive-based variant of the prospective CPI minus X form. The H-factor amount, expressed as a nominal dollar change in revenue for each regulatory year, is incorporated into the control mechanism in accordance with the NER and the DNSP's distribution determination.

The value of the H-factor for each regulatory year of a regulatory control period is calculated in accordance with this appendix.

Below is the formula to apply to standard control services revenues.

Figure C.1 Calculation of revenue adjustment for the Customer Service Incentive Scheme

1. $TAR_t \geq \sum_{i=1}^{n} \sum_{j=1}^{m} p_t^{ij} q_t^{ij}$ $i = 1, \ldots, n \; and \; j = 1, \ldots, m \; and \; t = 1, 2 \ldots, 5$

2. $TAR_t = AAR_t + I_t + S_t + B_t + C_t$ $t = 1, 2 \ldots, 5$

3. $AAR_t = AR_t$ $t = 1$

4. $AAR_t = AAR_t - 1 \times (1 + \Delta) \times (1 - X_t)$ $t = 2, \ldots, 5$

where:

$TARt$ is the total allowable revenue in year t.

$p_t ij$ is the price of component 'j' of tariff 'i' in year t.

$q_t ij$ is the forecast quantity of component 'j' of tariff 'i' in year t.

t   is the regulatory year.

AR_t is the annual smoothed revenue requirement in the Post Tax Revenue Model (PTRM) for year t.

AAR_t is the adjusted annual smoothed revenue requirement for year t.

I_t is the sum of incentive scheme adjustments in year t. Likely to incorporate but not limited to revenue adjustments for f-factor and the Customer Satisfaction Incentive Scheme (H-factor). To be decided in the distribution determination.

S_t is the s-factor amount for regulatory year t.1 As it currently stands, the s-factor will incorporate any adjustments required due to the application of the AER's STPIS.

B_t is the sum of annual adjustment factors in year t. Likely to incorporate but not limited to adjustments for the unders and overs account. To be decided in the distribution determination.

C_t is the sum of approved cost pass through amounts (positive or negative) with respect to regulatory year t, as determined by the AER. It will also include any end-of-period adjustments in year t. To be decided in the distribution determination.

ΔCPI_t is the CPI for year t, as determined in the relevant distribution determination.

For example, for 2020–21, year t–2 is the December quarter 2018 and year t–1 is the December quarter 2019.

X_t is the X-factor in year t, incorporating annual adjustments to the PTRM for the trailing cost of debt where necessary. To be decided in the distribution determination.

Figure C.2 H-factor calculation formula

$$\mathrm{H}_t = AR_{t-2}\mathrm{H}_{t-2}{}^{\%} \times (CPI_{t-1}/CPI_{t-3}) \qquad\qquad t = 1,\ldots,5$$

H_t is the H-factor for regulatory year t.

AR_{t-2} For t=1 and 2, AR_{t-2} represents the annual smoothed revenue requirement in the Post Tax Revenue Model (PTRM) for year 4 and 5 of the previous regulatory control period, respectively.

$\mathrm{H}_{t-2}{}^{\%}$ is the sum of the raw H-factors for all parameters for regulatory year t - 2, before banking, expressed as a percentage of revenue (or prices) calculated annually through the compliance assessment. For t = 1 and 2, $St-2\%$ represents the sum of the raw H-factors for year 4 and 5 of the previous regulatory control period, respectively.

9 The Customer Satisfaction H-factor

The H-factor for each parameter is calculated by comparing a DNSP's performance against its parameters and the performance targets and incentive rates included in the DNSP's distribution determination for a regulatory year during the regulatory control period.

The raw H-factor is the sum of the H-factors for each parameter. Equation (X) ensures that the raw H-factor result cannot exceed the percentage of revenue at risk specified in clause 2.5 or the relevant distribution determination.

$H_t = \min(\max(H'_t, H-), H+)$

where:

H-   is the lower limit of the revenue at risk

H+   is the lower limit of the revenue at risk

The sum of the raw H-factors for all reliability of supply parameters calculated as follows:

$H'_t = \sum_p ir_p * [Tar_p - Act_p]$

where:

H_t is the sum of the raw H-factors for all parameters

p   is a performance parameter

ir_p is the incentive rate for parameter p

Act_p is the actual performance for parameter p

Tar_p is the target performance for parameter p

t   is the regulatory year t, and t–1 is the regulatory year in which the performance parameter is measured.