Powerlink Queensland
2023-27 Revenue Proposal

Insurance Deep Dive

13 November 2020

Agenda

1. Context for the 2023-27 regulatory period
2. Purpose of session
3. The challenges:
   - Insurance market
   - Operating environment
4. Our approach:
   - Risk management
   - Insurance program
   - Pass through
5. Trade-off cost and risk
   - Cyclone scenario
6. Key considerations and customer views

2023-27 Revenue Proposal context

- In our draft Revenue Proposal in September 2020, we proposed no real growth in total operating expenditure over the 2023-27 regulatory period, and no step changes.
- We developed this target with particular regard to customer feedback on productivity, affordability, the current economic climate and COVID-19 impacts.
- This strategy includes our insurance costs, which are currently increasing and are forecast to continue to rise over the coming years.
- A no real growth in total operating expenditure target will be a challenging target for us to meet, and we need to explore ways to drive innovative business practices, seek efficiencies and aim to live within our proposed total operating expenditure for 2023-27.
- This includes in our insurance program, which is the focus of today's discussion.

What we've heard from customers

- Customers are concerned about rising insurance premiums and risks for customers.
- How does customer risk change under the different insurance elements?
- How long will the current hardening phase of the insurance market last for?
- How do global factors impact Powerlink's insurance costs?
- What are the exposures we are trying to balance and what are the trade-offs if a disaster occurs?

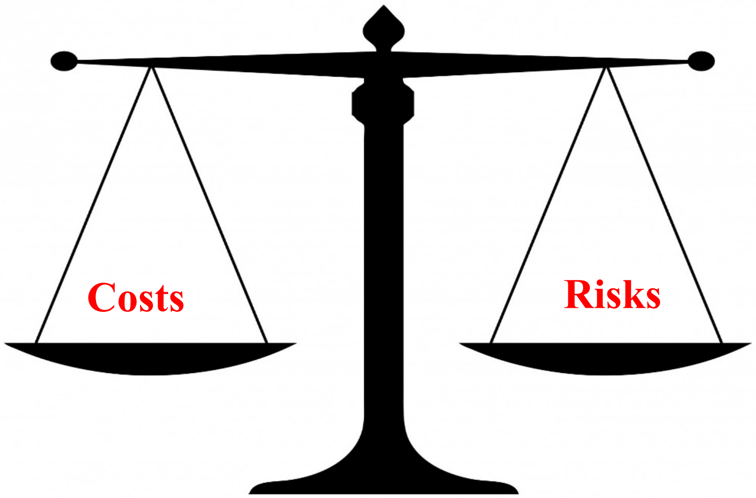
What we have done to date:

- In March 2020 our Chair, Kathy Hirschfield, discussed Powerlink's risk profile and risk management policies.
- In June 2020 we heard from our brokers, Marsh, about the key global factors and the drivers influencing the insurance market.
- We have adopted a no real growth strategy which includes our insurance costs.

Purpose of session

- If insurance costs continue to rise at predicted levels we will need to make trade-offs between costs and risks, to seek a reasonable balance for customers and Powerlink.

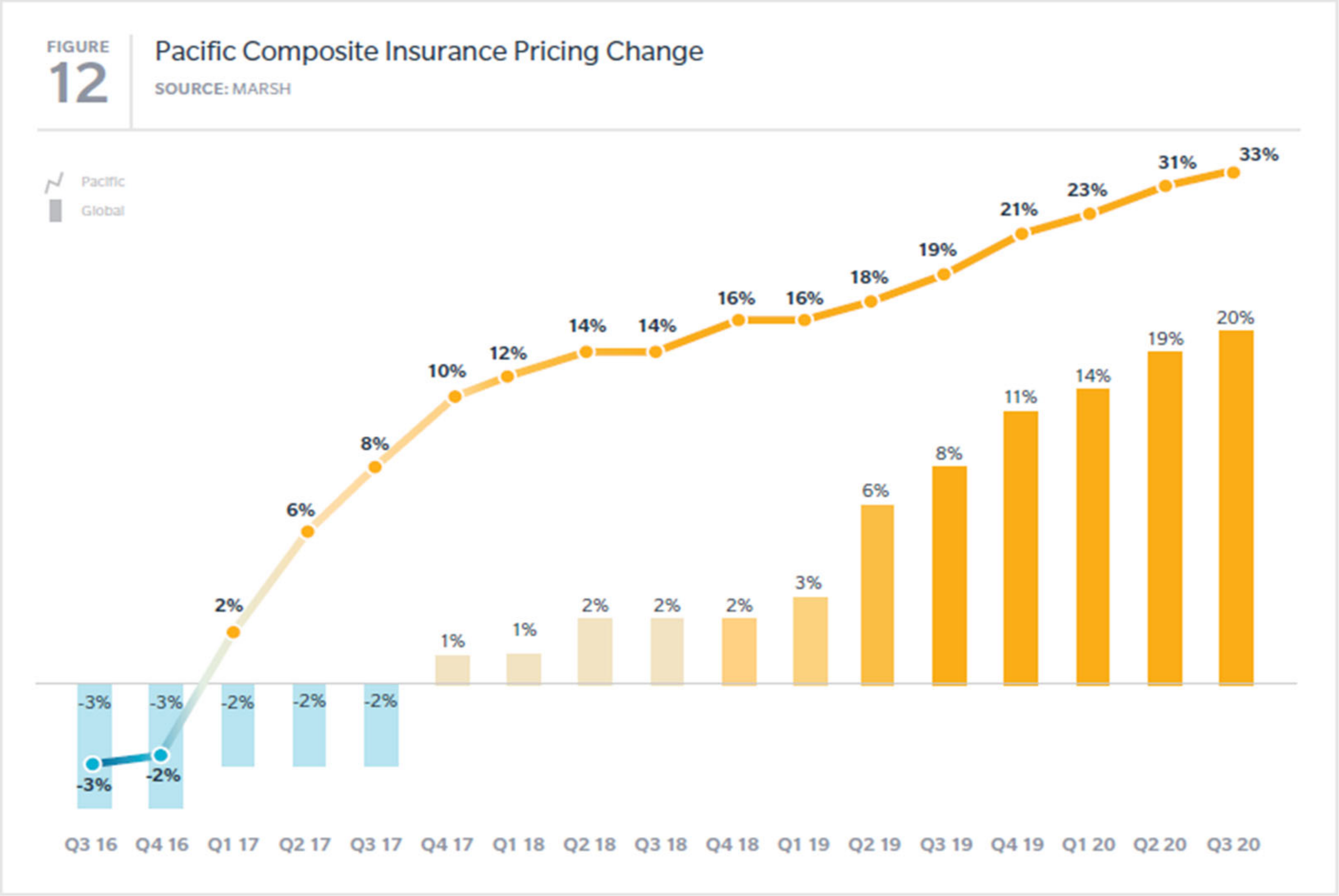
- The purpose of this session is **to help inform our considerations and decision-making on insurance over the 2023-27 regulatory period and beyond**.



Insurance Market

- There are currently significant challenges in the insurance industry and global market factors are having implications on insurance costs across the board.

- Rising insurance premiums and withdrawn capacity or risk of availability are being driven by factors such as:
  - a hardening insurance market
  - the impact of recent bushfire events
  - pandemic and cyber risks.

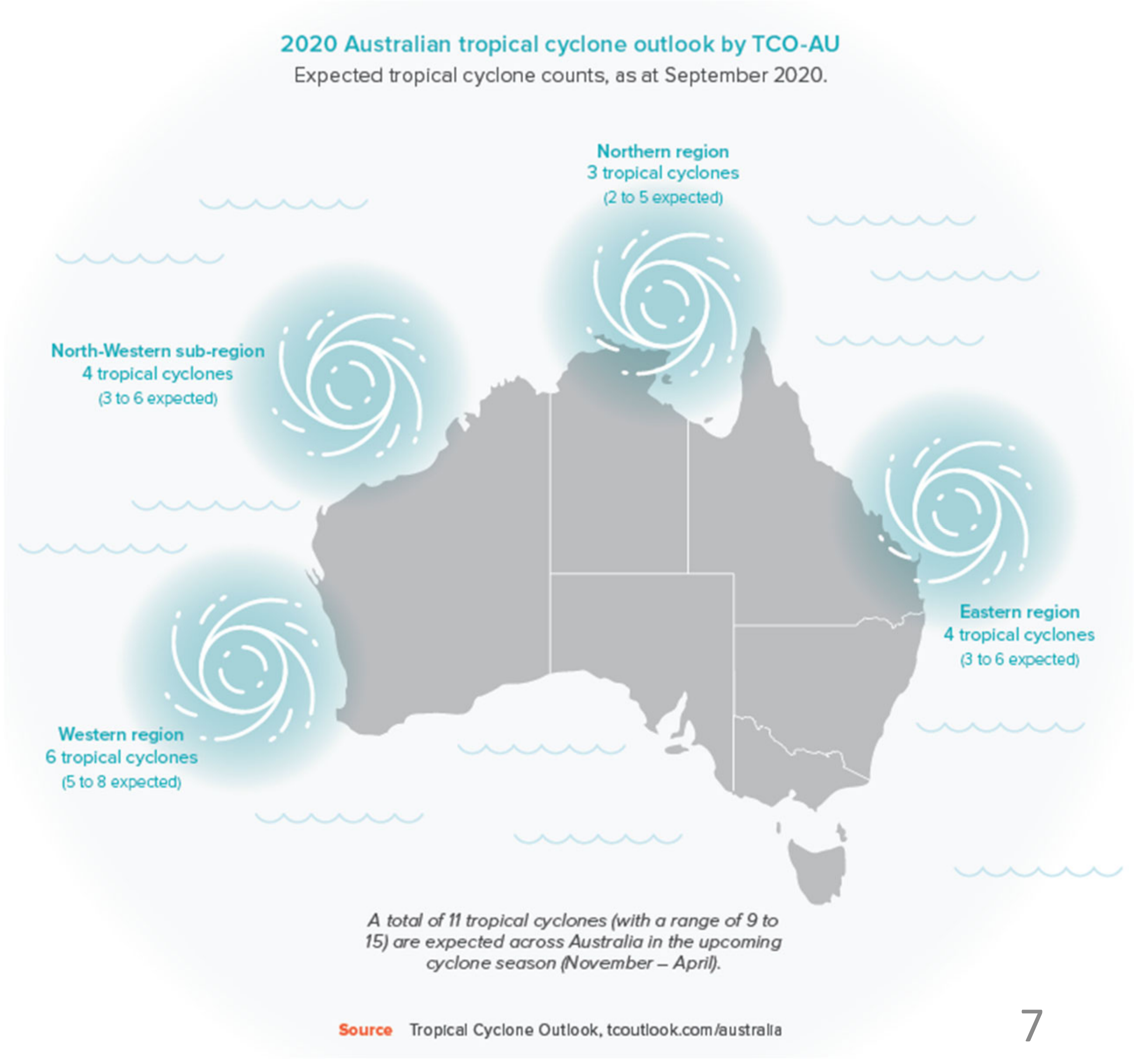


Operating Environment

- Extreme weather events creates challenges for the operation of the transmission network.

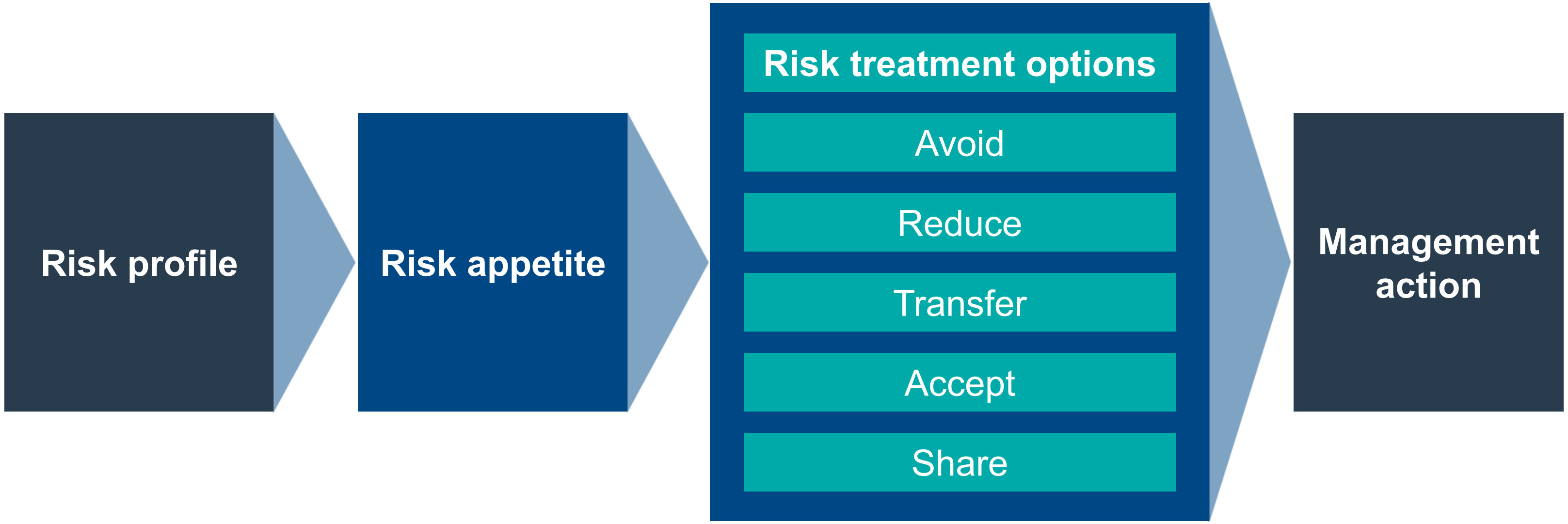
- The Bureau of Meteorology (BOM) declared the Australia in heading into a La Nina conditions which have implications for upcoming weather events.

- Weather events such as bushfires place upward pressure on insurance premiums. The insurance market generally responds to events as a whole and the impacts are seen globally across the market.



Risk management

- Risk management is recognised as an integral component of good corporate governance and **is fundamental in achieving strategic and business objectives.** Risk management improves decision-making, identifies opportunities and mitigates the impact on the business of material events.



- Insurance is typically required where we cannot prudently avoid or mitigate a risk.

Insurance Program

- Powerlink's insurance program includes a combination of insurance policies, self-insurance and pass through arrangements.

- It is important to consider the trade-off of costs and risks to both customers and the business and the interaction between these elements.

Insurance Element	Description
Insurance Policies	• The cost of obtaining commercial insurance coverage. This may include: ○ **Property** e.g. Industrial Special Risk (ISR) - Property and Machinery / Electrical Breakdown / Towers and Lines. ○ **Liability** e.g. General & Products Liability (including Professional Indemnity) ○ **Financial Lines & Ancillary** e.g. Directors & Officers (D&O) Liability, Motor Vehicle, etc
Self Insurance (SI)	• Covering small claims and complements insurable and non-insurable events.
Pass Throughs	• To potentially recover costs of defined, unpredictable, high costs events that are not economic to insure.

Insurance Program

- We undertake an extensive annual insurance program review.
- We proactively pursue and build long-term relationships with insurers.
- Our insurance requirements are informed by a range of processes including:
  - Annual and ongoing operational risk assessments
  - Worst foreseeable loss studies
  - Underwriter engineering reports
  - Industry / activity benchmarking
  - Broker advice
  - Powerlink claims history
- Our history and risk management practices make Powerlink a ‘good risk’ from an Insurer perspective.

Pass throughs

- A cost pass through allows a Network Service Provider to seek approval from the AER to recover costs in providing prescribed transmission services. The change in cost must be greater than 1% of MAR.

- The Rules specify the requirements for considering a cost pass through, including whether the network service provider could have insured against the event on reasonable commercial terms.

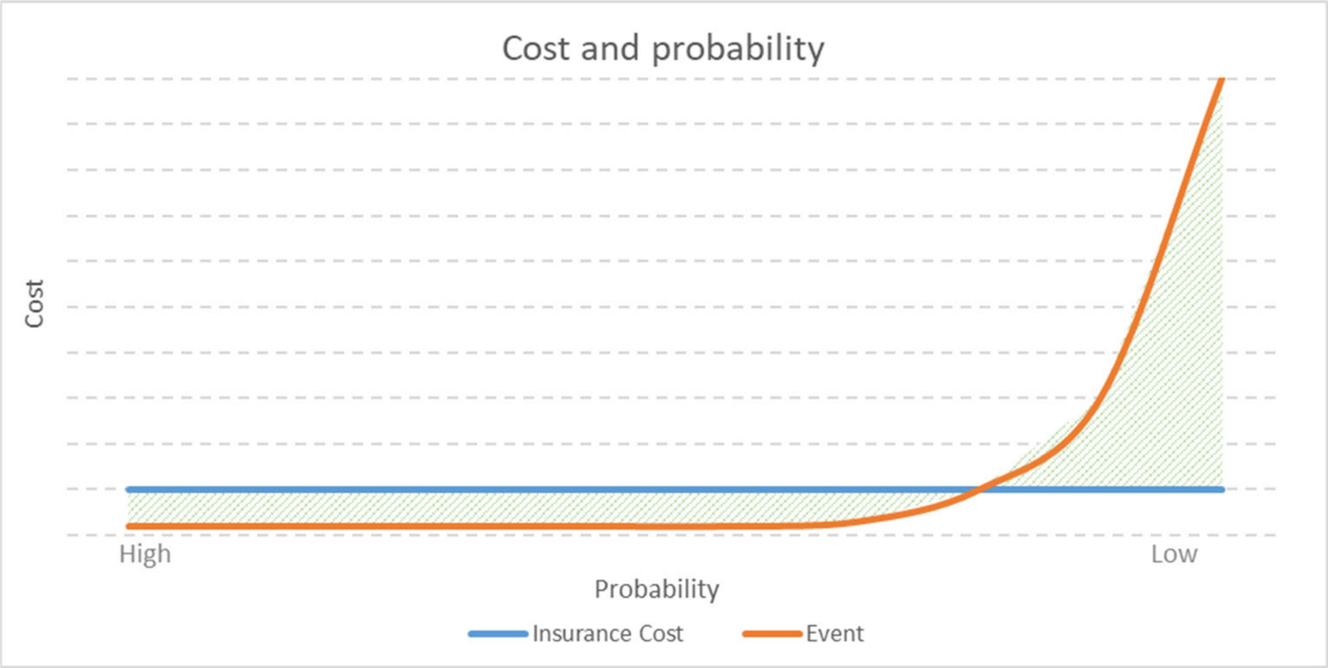
- Below is an illustration of the elements:

  1. *with commercial insurance*:

  2. *with no insurance:*

Trade-off of cost and risk

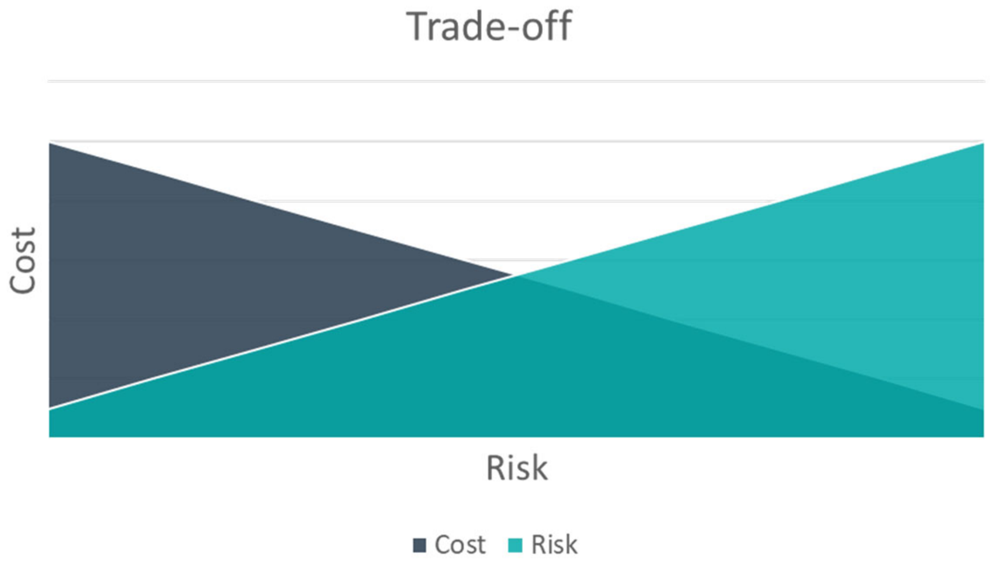
- High cost events with a low probability creates significant risk and uncertainty for business and customers.



Certainty vs uncertainty

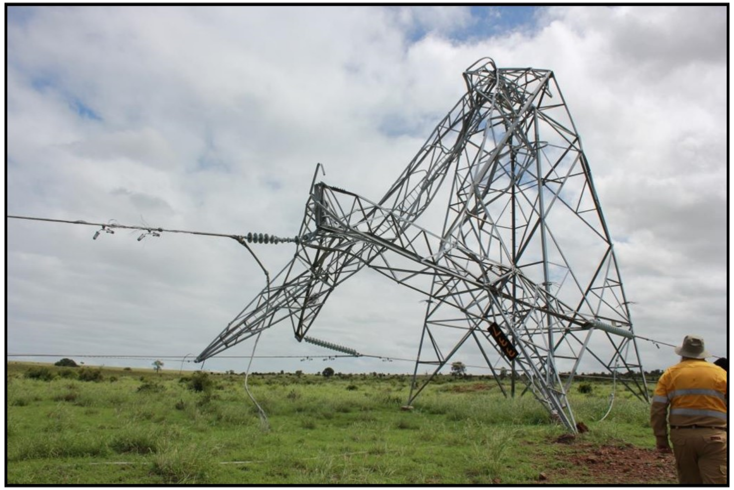
- Trading certainty of costs with uncertainty of pass through risk

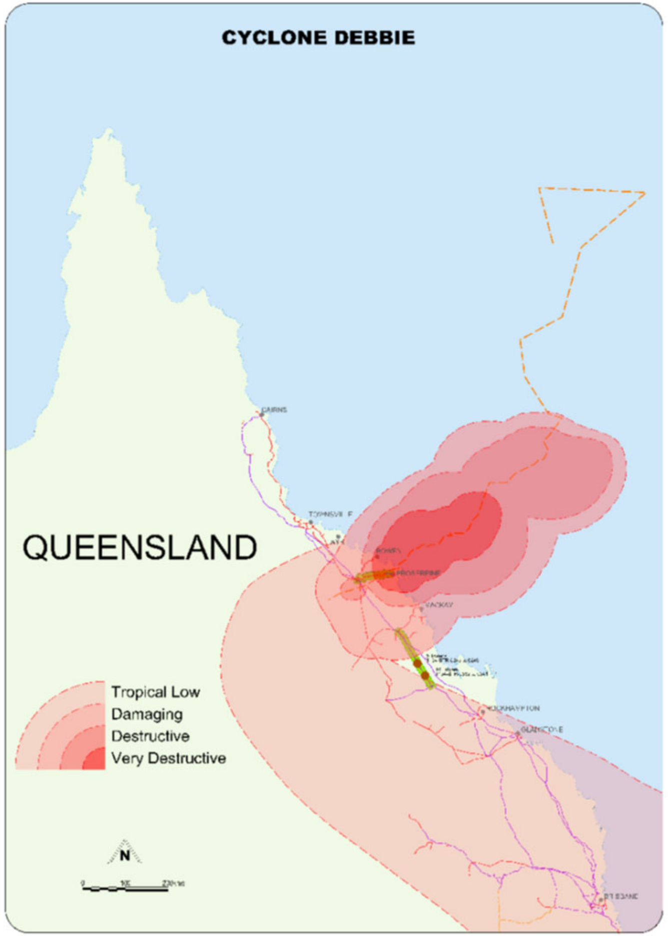
Approach	Description	Risks	Cost
Remove Policies	Not taking out insurance policies.	↑ risk of pass through and less certainty of costs	↓ in no event; ↑if significant event
Reduce Coverage / Limits etc	Selecting areas / assets that is insured eg. electrical breakdown cover, by age etc.	↑ risk of pass through and less certainty of costs	↓ in no event; ↑if significant event



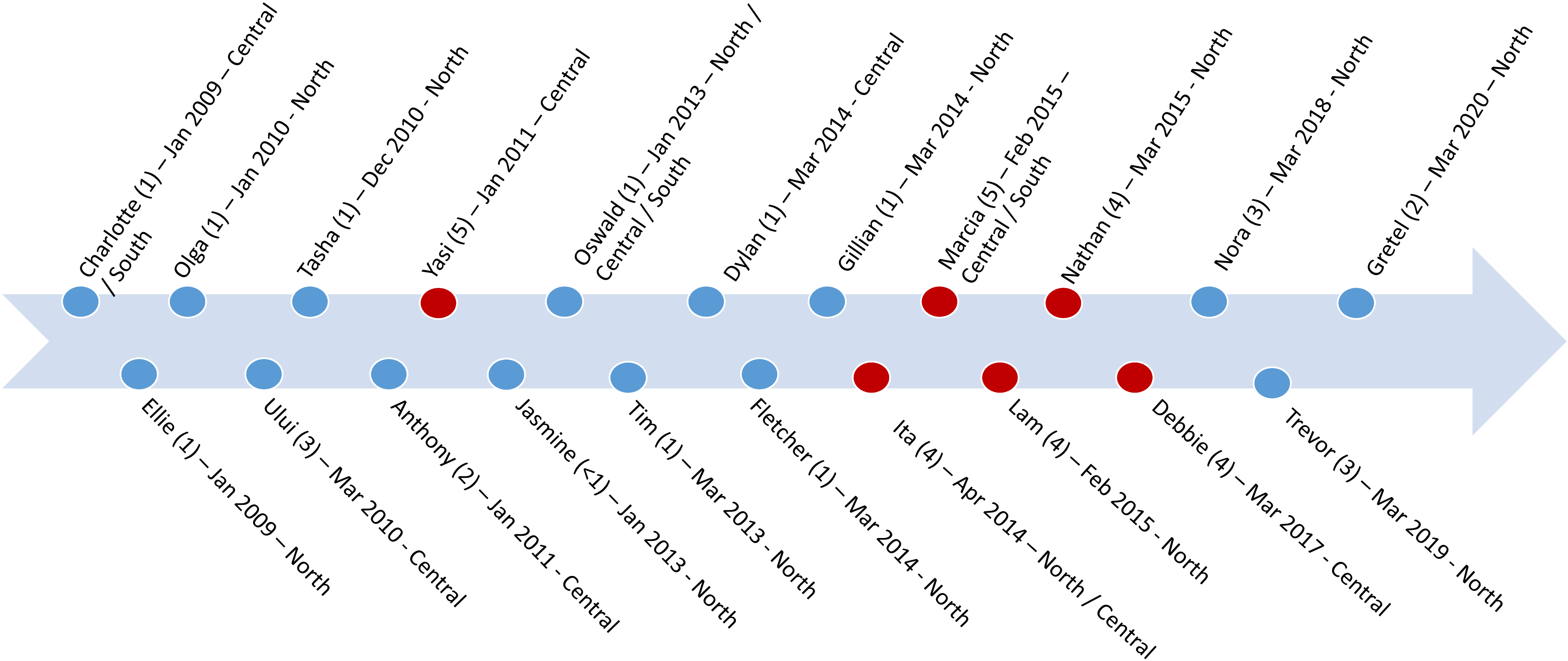
Cyclone / Ex-cyclone Debbie

- In 2017 we spent $9 million to replace 19 transmission towers in the Lotus Creek and Clarke Creek areas that were damaged by severe floodwaters from Tropical Cyclone Debbie.
- Network exposure - 19% cyclone, 65% tropical low (84% in total) of network was exposed to the collective Debbie / Ex-Debbie event





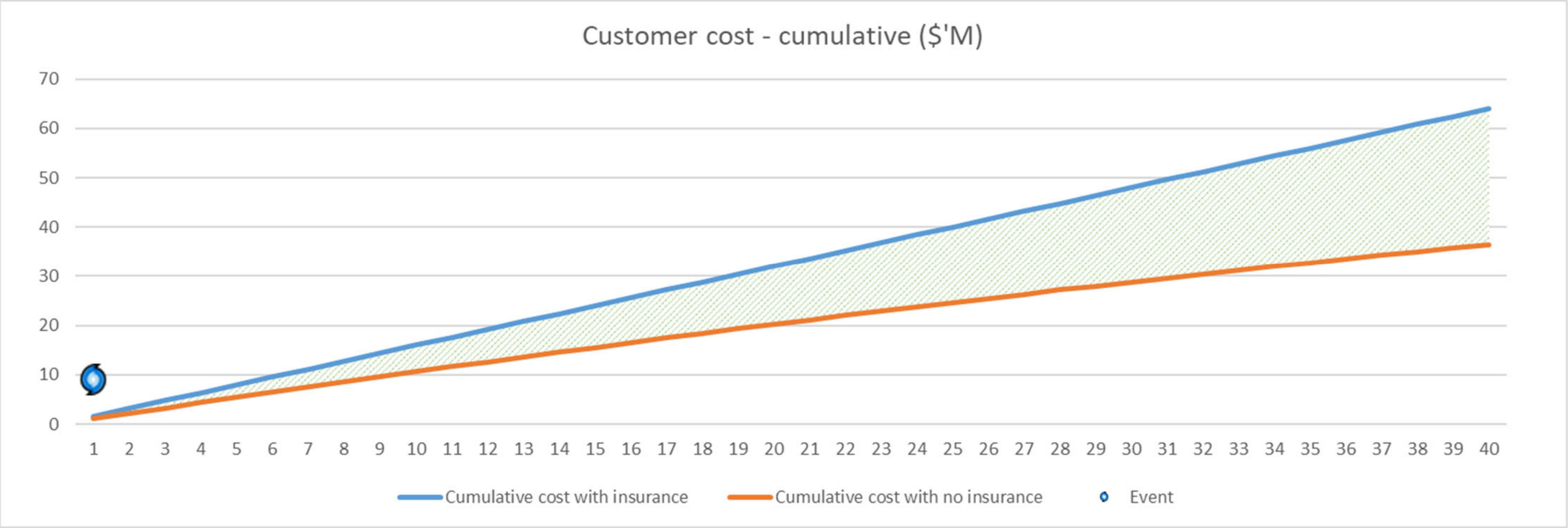
Queensland cyclone history



Category 4 or 5 cyclone

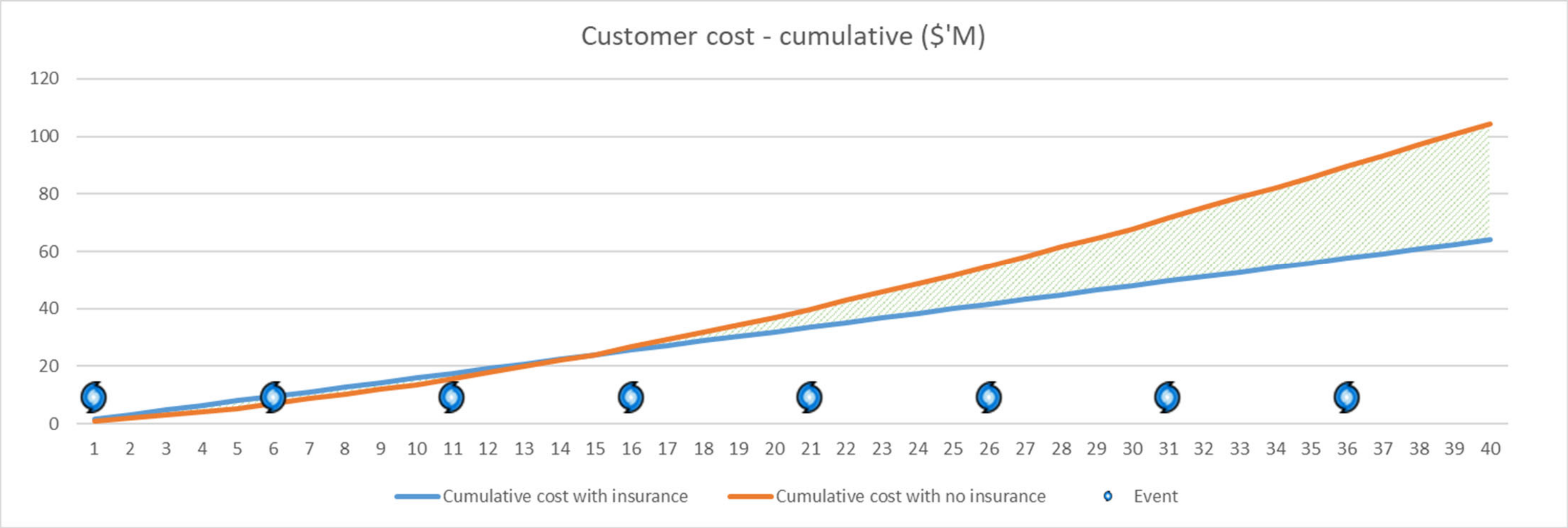
Scenario 1 – One cyclone event

- One cyclone resulting in $9M damage



Scenario 2 – Multiple cyclone events

- One cyclone every 5 years resulting in $9M damage per event.



Key Factors

- Factors for determining a prudent and efficient allocation of risk and costs include:
  - Minimising total cost to customers.
  - Prevailing Insurance market.
  - Availability / Capacity of Insurance coverage.
  - Operating environment, business profile and activities, asset base, etc.
  - Claims history.
  - AER's assessment of a prudent and efficient level of insurance.

Discussion

- **Are there any other factors should we consider in our decision making for insurance for the 2023-27 regulatory period?**

- **What are the key customer considerations we should take into account when making decisions about our insurance costs and coverage?**

- **How do we balance certainty of cost vs uncertainty of pass throughs for customers?**