

The Energy Users' Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing, building materials and food processing industries. Combined our members employ over 1 million Australians, pay billions in energy bills every year and in many cases are exposed to the fluctuations and challenges of international trade.

We welcome the opportunity to make comment on the Stage 2 Draft Recommendations for the Transmission Planning and Investment Review (the Draft). We agree with the overall objective of the review to ensure the timely and efficient delivery of the required major transmission projects to achieve our net zero target.

We seek to achieve net zero at least cost, not at any cost and argue that an efficient transition requires efficient transmission investment. We do not believe that over investment in transmission, in scale (far too big), timing (far too early) and cost (far too expensive) represents efficient transmission investment and is not in the long-term interests of consumers. If governments or other stakeholders want transmission investment to exceed efficient levels, then they should be prepared to pay the extra cost.

CONTEXT

We would like to take this opportunity to provide a consumer context to the various debates around achieving net zero and the role transmission could play in achieving this. Our focus is on ensuring consumers only pay for an efficient level of transmission investment, that consumers are not bearing an unfair level of cost and risk and that communities who will be hosting the decentralised energy system of the 21st century are not collateral damage.

These can be distilled down into two aspects of social licence that the entire energy supply chain (and governments) must manage; customer social licence and community social licence. Each are equally important to a successful energy system transition.

Customer Social Licence

We often hear that transmission costs are small in comparison to other elements (wholesale costs, environmental programs etc) and that consumers should just play their role and pay the bill. We also hear that the RIT-T is too cumbersome and should be weakened even further or even discarded. The 2022 ISP identifies that capex of \$12.7 billion is required to deliver a number of high priority transmission projects. This figure is based on an AACE class 4 cost estimate (-15% to +50%).

Recent experience with both Project Energy Connect and Humelink tells us that costs always go up, never down. For example, the costs of Humelink increased nearly 250% from \$1,350m in the PADR (January 2020) to \$3,317m in the PACR (July 2021) which was still only a Class 4 estimate. Increase the ISP estimate by just 50% and \$12.7 billion would quickly become \$19 billion.

Our Material Cost Rule Change¹ is designed to ensure more accurate costs estimates are used in the feedback loop/CPA when consumers get to know if the project is still part of the ISP Optimal Development Path and the AER decides what is a prudent and efficient level of capex.

Consumers have to rely on the TNSP to show that the individual project still has net benefits, with no independent umpire to test that conclusion. This creates unnecessary tension between energy users and the TNSP, ultimately leading to a significant reduction in trust and another round of “gold plating” claims being levelled at networks. This situation is bad for networks, consumers and governments.

Unfortunately, there are those who don’t seem to care about these negative consumer impacts. We would suggest that those who are advocating a “build it and they will come” or “just get on with it” approach would have a significantly different view of the world if they were the party facing these significant escalations in costs. We wonder why these parties expect consumers to just wear these costs increases when they wouldn’t. We would further suggest they wouldn’t be calling for a dilution of the RIT-T framework but demand it’s strengthening.

If consumers are continually seen as some form of magic pudding, where all manner of costs and risks can be justified simply by claiming it is in the customer interest (as defined by non-consumers), and this leads to an inequitable allocation of costs, bill spikes and consumers bearing market participant risks, then customer social licence for the transition will evaporate.

Another issue to consider is that even where net benefits of a new transmission project are demonstrated, consumers typically wait many years before these net benefits are realised² while paying certain costs (which networks want to increase through accelerated depreciation). For connecting generators the net benefits of the transmission asset are generally seen much sooner. Once again consumers are bearing the cost and risk of the transmission asset based on a promise that sometime in the future they will (or might) be better off.

If governments, the energy industry and regulatory bodies want to ensure customer social licence is built and not destroyed as we embark on a rapid transition of our energy market, then serious thought must be given to a far more equitable sharing of costs and risks than is currently the case.

Community Social Licence

It is encouraging that governments, the industry and regulatory bodies are beginning to understand both the risks to a least cost transition and the great inequity that could be created if communities are not central to the transition. As we have said many times, the regulatory process may slow you down but social license will stop you dead in your tracks.

We look forward to continued engagement with the Commission on the overall Transmission Planning and Investment Review through the recently established Consumer Reference Group.

¹ See <https://www.aemc.gov.au/rule-changes/material-change-network-infrastructure-project-costs>

² For example, see the FIT modelling of the timing of benefits to NSW consumers from Project Energy Connect pp 11-13 https://www.aemc.gov.au/sites/default/files/documents/new_rule_change_proposal_-_national_electricity_rules_-_transgrid_-_making_isp_projects_financeable_-_fti_report_-20200930.pdf

SUMMARY OF EUAA POSITIONS ON KEY ISSUES:

Assessment framework criteria

We agree with the proposed criteria, in particular the inclusion of ‘outcomes for customers. We believe that this should be seen in the context of the economic efficiency criteria – efficient risk allocation.

Financeability concerns

Perhaps EUAA members should not be surprised that equity investors want to push even more risk onto consumers. We keep being told about the huge amounts of capital that are ‘ready’ to invest in the transition if only we had ‘the right policy settings’ or ‘supportive Government policy’ which are just code for some form of subsidy at either electricity consumers or taxpayers’ expense. We are expected to subsidise equity returns because we are told ‘it is in our long term interests’. We are not convinced.

Were the AER to be given discretion to vary the depreciation profile we support the bespoke approach proposed in the Draft to adjust the rate of depreciation on a case by case basis. We do not support introducing a financeability or commercial viability check into the revenue setting framework.

Clarity around social licence outcomes

Our extensive experience across NEM jurisdictions suggests that in at least some cases there is a large difference between aspiration (no shortage of reports around what should be done and these have been around for some time) and on the ground delivery. That is why we recommend some targeted prescription in the rules on stakeholder engagement.

- Where a social licence contingency is granted by the AER in the CPA approval, then any costs incurred above that contingency would be borne by the TNSP
- The AER be able, if it is not already the case, to decline or reduce a cost pass through if the AER judges that the TNSP did not meet the required best practice standard for social licence engagement following the principles set out in the AER Better Resets Handbook and ISP Guidance Note
- Stakeholders be able to make submissions on the TNSP’s cost pass through application
- Establishment of a social licence benchmark cost guide to support the above - this could be part of the AEMO Transmission Cost Database

Clarity on cost recovery

The EUAA agrees with the benefits of providing greater clarity and supports the recommended option 2 – clear definition of planning activities to distinguish between activities to identify and select the preferred option and refining and delivering the preferred option.

While we support the use of pass-through provisions in the case of an unexpected increase in the cost of preparatory activities, we support the continued application of the 1% MAR threshold. As such we expect such applications to be rare given the detailed information available to TNSPs from both their internal experience and the AEMO ISP to assist in their cost estimation.

Feedback loop

We strongly support the role of the feedback loop as an important part of consumer protection. Our Material Cost Rule Change was designed to strengthen the consumer protections inherent in the feedback loop through ensuring more accurate cost forecasts are used. We agree with aligning the feedback loop to the draft or final ISP to improve its workability. We support the Draft’s Option 2 providing for a PACR exclusion window between publication of the final IASR and Draft ISP. We agree with giving effect to this window through the AER CBA Guideline.

DRAFT RECOMMENDATIONS

1. Greater flexibility to mitigate the foreseeable risk that finance ability concerns may arise in the future

The justification for the proposal to give the AER discretion to vary the depreciation profile for an actionable ISP is based on a qualitative view that Transgrid, which has an exclusive right to, but not an obligation to, build these projects might find its equity investors unwilling to fund the required capital. The Commission’s extensive review last year on this same matter decided not to implement Transgrid’s rule change to vary the depreciation profile for Project Energy Connect.

We agreed with that decision. In our submission on the original proposal³, we noted what the Draft refers to the ‘material intergenerational impact on consumer prices’ (Box 3) when we said (p. 3):

“Our members are not willing to accept the certainty of higher prices now in return for the promise of lower prices in 15-20 years’ time.

The modelling supporting the project (referred to above) showed benefits to NSW electricity consumers only *start* around 2031, or a decade after the start of construction. We do not believe it fair and equitable to ask electricity consumers to pay greater certain costs in the early years of the asset’s life before the modelled benefits are expected to appear, all in the name of furthering consumers interests.

It seems that equity investors (transmission and generation) can threaten to go on a capital strike and not fund construction for a period while the credit metrics move away from the 60/40 benchmark entity and consumers are expected to pick up the bill because we are told, it is in our long-term interests. This is at the time when ratings agencies look to the long term rating based on the regulatory framework that provides a very high level of confidence on future cash flow.

The case for giving the AER greater discretionary powers to vary a project depreciation is that, while it is not required today, it might be required in the future. We keep hearing stories about the huge levels of capital available for investment in the transition, yet so much of that seems dependent on those investors ‘getting the right regulatory settings’ or ‘supportive government policy’ which are just code for some form of subsidy at either

³ See https://www.aemc.gov.au/sites/default/files/documents/rule_change_submission_-_erc0320_-_energy_users_association_of_australia_-_20201203.pdf

electricity consumers’ or taxpayers’ expense. After all we keep being told these arrangements are in our long-term interests. Our members remain to be convinced that bearing someone else’s risk is in their interests.

If the AER were to be given that discretion (this does not indicate acceptance on our part), we support the bespoke approach proposed in the Draft through adjusting the rate of depreciation on a case-by-case basis. For the reasons outlined in the Draft, we do not support adjusting cash flows through adjusting the return on capital.

In implementing a depreciation adjustment process we do not support introducing a financeability or commercial viability check into the revenue setting framework. We agree with the Draft that this would not meet the NEO. We look forward to engaging with the AER as it develops the appropriate Guideline.

2. *Providing greater clarity around social licence outcomes in the national framework*

The EUAA agrees with the Commission that effective social licence engagement is central to not only being able to build the required level of transmission but also to build it efficiently. The experience of the Western Victorian Network Project is a stark example of the problems the lack of social licence can create. Gaining social licence is the greatest hurdle in progressing major network projects as we see in a project that completed its PACR in mid 2019 and still does not have an announced date for start of construction.

We agree that the existing methods of cost recovery for social licence activities allowed under the NER - preparatory activities approved via the revenue determination process and forecast costs through the CPA process and cost pass-throughs events that are beyond the TNSPs reasonable control - are appropriate and allow the recovery of the efficient costs of key activities to build and maintain social licence. We agree that it is not the role of the NER to set the level of compensation which is governed by jurisdictional arrangements.

Our comments focus on the relative importance of the last two – CPA and pass-through. Cost pass-throughs should not be used as a safety net for poor cost estimation at the feedback loop CPA stage. As the Draft says (p.25):

“Should TNSPs incur an unexpected or unavoidable material cost associated with carrying out social licence activities, they may seek to recover these costs as cost pass-through events.” (emphasis added)

In our Material Cost Rule Change we argued that the NEO is best served by more accurate cost estimates at both the RiT-T where project approval occurs and CPA stages. This ensures that consumers have confidence that the feedback loop provides a robust answer to the question ‘is this project still part of the optimal development path’. We need to avoid the situation where:

- poor quality (i.e. wide accuracy variation) of cost estimates for social licence are used in the RiT-T to ease the approval process
- the level of social licence in the CPA capex estimate (e.g. measured by the proportion of the route for which the TNSP has agreed land and easement acquisition costs), covers less than the complete route with a contingency to cover the part not fully agreed
- this ‘estimated social cost’ capex estimate is then used in the feedback loop and CPA
- subsequent landholder negotiations result in a significant increase in costs that are deemed ‘unexpected and unavoidable’ by the AER and allowed as a pass-through

when, had the feedback loop costs included the land and easement acquisition costs for the full route the project would not have passed the feedback loop.

Where a project has the full route land and easement acquisition costs included in the feedback loop analysis but the project does not pass the feedback loop, the EUAA is not suggesting that this project not be built. Jurisdictions and connecting generators are still able to facilitate the project proceeding by funding the ‘excess’ costs. The EUAA is wishing to ensure that only the costs necessary to pass the feedback loop are included in the TNSPs RAB. Any additional costs can be funded by the jurisdictions and generators and not be part of consumers electricity bills.

This approach addresses the issue raised in Box 5 in the Draft. Transgrid would have the actual costs of land and easement acquisition without having to include a contingency. We would argue that a better approach to determining ‘prudent’ costs is to complete the negotiations – in the form of options – prior to the feedback loop. This is not to suggest that the TNSP should ‘give in’ to all landowner demands. Jurisdictional legislation provides a framework for these negotiations.

We are proposing that were a contingency to be granted by the AER, then any costs above that contingency for particular social licence activities should not be allowed as a pass through but be a cost to the TNSP where the AER judges that the TNSP has not met best practice standard for social licence engagement following the principles set out in the AER Better Resets Handbook and the ISP Guidance Note. Given the Draft’s assessment criteria of ‘efficient risk allocation’ (p.6), consumers have no way of mitigating a risk that is created by a TNSP’s approach to social licence engagement, particularly where it fails to meet best practice.

The AER Guidance Note’s discussion of ex post reviews of ISP project capex⁴ in the context of the capex guidelines does emphasise it expects to see appropriate project governance structures and risk management plans/processes that proactively identify project risks and allocate appropriate management strategies to the risks as part of the CPA. It says (p.35):

“For completeness, in demonstrating their adherence to project and risk management frameworks and controls set out in their CPAs, we expect the TNSP to show how its actions and processes led to efficient and prudent outcomes. For example, by providing information on how their project control processes minimised a cost overrun, and justifying the efficiency of incurring the overrun in the context of finding efficiencies elsewhere.”

The key question then is – what is the best practice standard a TNSP is to be judged against for their management of social licence and hence their claim of a cost pass-through? The AER Guideline sets out a range of expectations on TNSPs to undertake extensive early engagement e.g. (p.5):

“We consider it is important that the TNSP consults with stakeholders in preparing a CPA for actionable ISP projects. Meaningful high quality early engagement, particularly with local community and consumer representatives, can:

- *Improve stakeholder and community understanding of the project's costs and risks...*

⁴ See Section 4 pp 32-37 <https://www.aer.gov.au/system/files/AER%20-%20Final%20Guidance%20note%20-%20Regulation%20of%20actionable%20ISP%20projects%20-%20March%202021%20-%20FINAL%20FOR%20PUBLICATION%2812129318.1%29.pdf>

- *Provide greater opportunity for the project solution to be designed with the benefit of local community input, particularly where local communities and/or individuals are impacted.*
- *Facilitate understanding of any community concerns, particularly of any impacted stakeholders around the route selection...*
- *Provide the TNSP with the opportunity to address or manage concerns raised and demonstrate how it has considered feedback.”*

And note (p. 33):

“... in undertaking an ex-post review, we can only take into account information and analysis that the TNSP could reasonably be expected to have considered or undertaken at the time that it undertook the relevant capex.”

We would submit that the current extensive debate and discussion on social licence engagement means the level of information and analysis the TNSP can reasonably be expected to know is very high and considerably higher than the level of information expected even a couple of years ago. And it is increasing all the time. This social licence data should be collected as part of the AEMO Transmission Cost Data Base.

The EUAA is a long-term member of the peak Transgrid Advisory Council. In our submission on the Transgrid 2023-28 revenue proposal we expressed concern that Transgrid hardly engaged at all on ISP contingent projects which would drive the revenue and pricing in 2023-28. We went on to say, regarding HumeLink⁵:

“Unfortunately, when questions were raised by consumer representatives, they were more often than not “parked” and not dealt with in any meaningful way... TAC members have been left underwhelmed by the engagement on key projects such ... HumeLink... Many TAC members felt this was a significant oversight.”

The workload taken on by Transgrid as it seeks to develop multiple, highly complex, very expensive transmission assets in a relatively short period of time is enormous. We would note that Transgrid have an option to decline to build some of these projects, allowing another party to step in. In any case, it is encouraging to see that Transgrid are responding to these concerns and have established the Energy Transition Working Group (ETWG) in response to feedback from TAC members (the EUAA is a member of this group). The ETWG met once prior to the CPA submission and has met once since. Discussion of HumeLink has not been at the detailed level expected by the AER Guideline.

Subsequent discussions with landowners in the Snowy Mountains section of the HumeLink route who made submission to the AER on Transgrid’s early works CPA indicate considerable room for improvement in community engagement around social licence. These concerns include staff turnover in the engagement process, failure to consider fire risk, the changing approach to compensation, poor quality analysis underpinning route selection and the high level of assumed compulsory acquisition.

The Draft highlights a range of submissions calling for *“...a greater level of tailored and transparent engagement”* by TNSPs. We agree with that. As earlier submissions to this process highlighted, there is considerable room for

⁵ Ibid p.4

improvement in current practices. The rules should require AER’s consideration of pass-through events be built on a high bar for best practice community engagement on social licence.

In the Victorian context, AEMO completed the PACR for the Western Victorian Network Project in July 2019 on the basis of a capex of \$370m. Following a competitive tender process, Mondo, an AusNet subsidiary was selected to

“...consult on, design, seek planning approvals for, construct, own, operate and maintain the contestable transmission augmentations proposed...”⁶.

Given the strong and continued community opposition to the project it is not unreasonable to assume that the eventual capex, assuming social licence is eventually obtained, will be significantly above \$370m and may well more than offset the PACR forecast of net market benefits of \$300m. To what extent should consumers take the risk of the poor social licence engagement undertaken initially by AEMO as part of the RiT-T and now by Mondo?

The EUAA’s extensive involvement across NEM network resets has shown considerable improvement in the quality of consumer engagement for regular reset processes in recent years. The AER’s Better Resets Handbook is driving the next stage of that improvement. The bar is getting higher all the time and the ‘best practice frontier’ keeps moving out. But ISP project engagement that has been left to the TNSPs to develop without any prescription under the rules, only the AER’s ‘expectations’ under the ISP Guidance Note. The result is that ISP project engagement has not seen that same pace of improvement and lags well behind best practice reset engagement.

It remains to be seen how the AER implements its ISP Guideline on pass through costs for an ISP project. Discussions with the AER in the context of the Transgrid Humelink CPA suggest that Transgrid’s failure to follow the Guideline’s expectations on consumer engagement (our engagement and landowner submissions) are unlikely to result in any delay of, or reduction in, the \$ approved. We don’t think this is consistent with the NEO and the Drafts’ assessment framework criteria. Why have a whole chapter on the importance of social licence in this Draft and then find it has little if any actual impact on TNSP engagement behaviour? Under an incentive based regulatory framework that has CESS/EBSS/STPIS/CSIS etc, how are networks to be properly incentivised without some form of financial penalty?

In summary, we would propose there be greater prescription around stakeholder engagement:

- Where a social licence contingency be granted by the AER in the CPA then any costs incurred above that contingency be borne by the TNSP
- The AER be able, if it is not already the case, to decline or reduce a cost pass through if the AER judges that the TNSP did not meet the required best practice standard of social licence engagement following the principles set out in the AER Better Resets Handbook and ISP Guidance Note
- Stakeholders be able to make submissions on the TNSP’s cost pass through application
- Establishment of a social licence benchmark cost guide to support the above - this could be part of the AEMO Transmission Cost Database

⁶ See <https://aemo.com.au/initiatives/major-programs/western-victorian-regulatory-investment-test-for-transmission/stakeholder-consultation>

3. *Providing greater clarity on the cost recovery of different types of planning activities*

The EUAA agrees with the benefits of greater clarity and supports the recommended option 2. We understand the risks associated with trying to forecast what preparatory expenditure might be required in a forthcoming 5 years revenue rest period. We support the use of the pass-through mechanism to account for any unexpected increase in opex resulting from preparatory activities, and support the continued use of the 1% MAR materiality threshold. As the Draft notes (p.41):

“The Commission considers that material unforeseen obligations are unlikely to arise given the ISP joint planning process where TNSPs work closely with AEMO to develop the ISP. Therefore, TNSPs are reasonably aware of potential preparatory obligations for specific projects prior to the ISP being published.”

The recently published 2022 ISP clearly sets out the actionable projects to 2030 and future ISP projects beyond then. TNSPs should also have significant internal information on which to provide a reasonably accurate estimate of preparatory activities for their next 5 years reset period. Given this, plus the proposed definition of preparatory events, we expect the likelihood of any opex pass-through events as rare.

We support the recommendation to allow the staged CPA process to mature and be drawn on by TNSPs where appropriate. The purpose of our Material Cost Rule change was to strengthen the RiT-T and CPA processes so that the costs applied for are no more than the level that still ensures the project has net benefits and the project remains the preferred project with the highest net benefits.

4. *Improving the workability of the feedback loop*

The EUAA strongly supports the feedback loop. Those who propose its removal are obviously those who do not bear any costs of building ISP projects, only enjoy the benefits of the investment return or free connection for their generating assets.

We agree with aligning the feedback loop with the draft or final ISP will improve its workability. This will ensure the particular project is assessed using the latest IASR and ISP ODP. We support the Draft’s Option 2 providing for a PACR exclusion window between publication of the final IASR and Draft ISP. We agree with giving effect to this window through the AER CBA Guideline.

As always we would be happy to discuss any part of this submission.

Kind regards,



Andrew Richards
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