Submission to the Transmission Planning and Investment - Stage 2 Draft Report

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Contact:
Kate Healey
Policy Manager RE-Alliance
kate@re-alliance.org.au
0456 674 551

About RE-Alliance
RE-Alliance works to deliver a renewable energy transformation in Australia filled with sustainable, long-term benefits for regional communities. We do this by listening to the needs of communities most impacted by the transition, facilitating collaboration across the renewables industry to deliver social outcomes and advocating for meaningful benefits for regions at a policy level.

We thank the Australian Energy Market Commission (AEMC) for the opportunity to comment on the *Transmission Planning and Investment - Stage 2 Draft Report* (the Draft Report).

We note that the AEMC has focussed its thoughts on four reform aspects in the Draft Report:

1. Financeability concerns;
2. Social licence concerns;
3. Cost recovery arrangements for planning activities; and
4. Improving the workability of the feedback loop.

We comment on each reform area below.

Financeability concerns

The AEMC is concerned to ensure that the revenue framework appropriately supports the financing of major transmission investments. The AEMC explains that

> *"When a network business invests in a project, it starts receiving a return on the investment based on forecast capital expenditure. However, the business does not start receiving a return of the investment (depreciation) until the investment is commissioned. As depreciation typically occurs on a straight-line basis, this cash flow meets the project's requirements over its lifetime. However, this profile may not match the profile of financing requirements. Specifically, it*

does not match the requirements to meet the higher levels of debt in early years, but is greater than the debt attributed in later years. In the absence of changes to the business' capital structure, this may in the short term negatively impact some of the financial metrics that form part of the range of factors that are used to assess the creditworthiness of a business".[1]

Thus, under the current regulatory arrangements there is a mismatch between when the transmission company starts spending on the project and when it receives funding for it. Cash flow challenges may occur when a large amount of new investment relative to the existing regulated asset base (RAB) occurs in a short period of time, if businesses are unable to raise funds and adjust capital structures within the required timeframe.

We also note that the AEMC concludes that

> *"Multiple large projects conducted concurrently or in sequence would make new investments a much larger proportion of the RAB. This would likely impact short-term cash flow relative to the RAB more significantly than single large investments or a more gradual accretion of investments. While shareholders can assist by supporting a business with additional equity, reducing the gearing of the business, this does dilute returns to investors in the short term and has the potential in some circumstances to contribute to the delay or avoidance of future investment".*[2]

We agree with the AEMC's finding that financeability challenges could arise in the future under realistic future Integrated System Plan (ISP) development plans and that it is appropriate for the Australian Energy Regulator (AER) to have sufficient flexibility to address this issue. Indeed, we tend to think that financeability issues have already arisen with regard to Project EnergyConnect (PEC). We quote from our previous submission to the *Transmission Planning and Investment Review Consultation Paper*.

> *"We note the AEMC's rejection of TransGrid and Electranet's Financeability Rule change requests. The Commission found that the current regulatory framework does not create a barrier to financing TransGrid's or Electranet's share of current ISP projects including PEC.*
>
> *However, we note that following the AEMC's rejection of the rule change, the company's Boards expressed significant concern that the projects might not be able to be funded and may not therefore be built.*

[1] AEMC, Transmission planning and investment - Stage 2, Draft report, 02 June 2022 p 11 available at: https://www.aemc.gov.au/sites/default/files/2022-06/stage_2_draft_report_-_transmission_planning_and_investment_review.pdf
[2] *Ibid* p.11.

The situation was solved when the Clean Energy Finance Commission stepped in with up to $295 million in capital.

> *"The CEFC investment, on behalf of the Australian Government, was made via an innovative subordinated note instrument which contributed to the crowding in of further private sector debt to this critical project. The CEFC investment in PEC will see TransGrid build the NSW portion of the new 330 kV interconnector connecting the energy grids of NSW and SA, with an additional link to North West Victoria".* [3]

Electranet also received funding from the Australian and South Australian Governments for their section of PEC. The Commonwealth and State Governments committed on a 50/50 basis, to fund up to $100 million for PEC through joint underwriting of key early works.

Following the funding announcements from the Australian and South Australian Governments and the CEFC the Boards of both TransGrid and Electranet committed to progressing with the build of PEC.

We note subsequent discussion about the rate of return and the return of capital through depreciation and the AER's view that it is unclear as to whether its discretion extends to resolving financeability concerns by adjusting depreciation timing, even when this would best achieve the national electricity objective. If this is the AER's view then RE-Alliance would support the finding that the regulatory framework does not currently have sufficient flexibility for the AER to address potential financeability concerns, should these arise. RE-Alliance would support the ability of the AER to use this flexibility to deliver a lower cost of capital that ultimately flows through to consumers as reduced costs.

Further to this, we note discussion on pages 15-17 of the Draft Report on whether it is appropriate to adjust the return on capital (through the rate of return instrument), or adjust the return of capital (through depreciation). RE-Alliance supports the AEMC's view that providing more flexibility to adjust the rate of depreciation is an appropriate and proportionate approach to addressing the issue.

Finally, there is discussion on whether a financeability or commercial viability test should be introduced or whether a more targeted approach to considering financeability only where this is raised by a business with respect to a specific

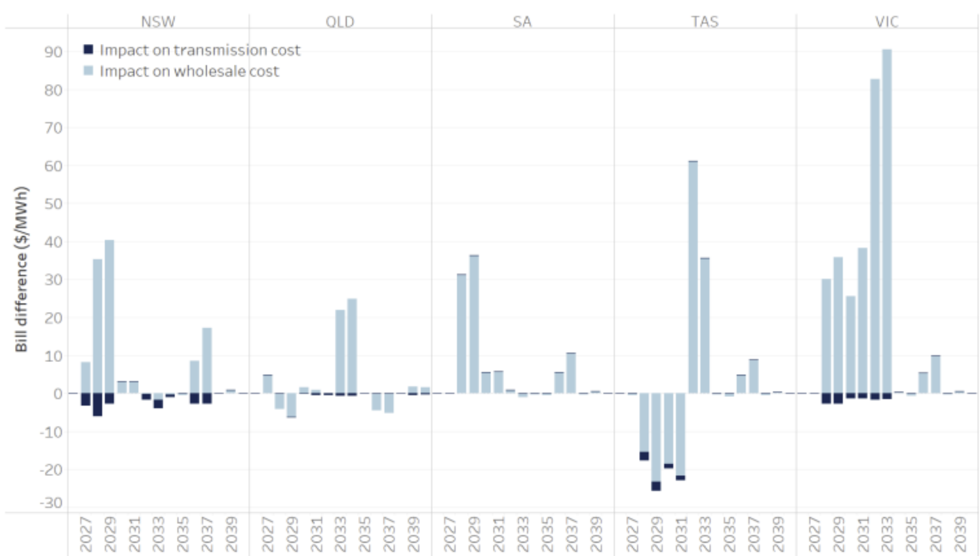
[3] Historic CEFC investment to kickstart nation building Project EnergyConnect: available at: https://www.cefc.com.au/media/media-release/historic-cefc-investment-to-kickstart-nation-building-project-energyconnect/

actionable ISP project would be more appropriate. We agree with the AEMC that the more targeted approach may be more flexible and simple to implement and would be in the long term interests of consumers.

However, we note that this would require the making of a new rule and for the AER to develop and consult on a guideline, which is expected to take six to nine months from the date a rule is made.

This brings into focus the issue of timeliness. RE-Alliance notes recent modelling completed by Endgame Economics for NEXA Advisory. The Figure below shows the very significant increases in wholesale costs if critical transmission infrastructure is delayed by two years[4]. Reduced transmission costs are dwarfed by increased wholesale costs. It is of paramount importance that the transmission projects proceed in the timelines outlined in the ISP, especially noting the degree to which consumers are already suffering due to a lack of timely progression of transmission projects in recent years.

Figure 5 – Change in wholesale and transmission cost ($/MWh, real 2022 AUD) caused by a two-year delay in transmission



Alternative finance options

There is of course another possible way of dealing with short term private sector financeability issues - a contribution of funding and/or debt by the Federal or State

[4] Endgame Economics, Modelling Electricity Bill Impact of Transmission Project Delays - A Report for NEXA Advisory 7 June 2022 p. 9 available at: https://nexaadvisory.com.au/site/wp-content/uploads/2022/06/Report-Modelling-Electricity-bill-impact-due-to-transmission-delay_2022-06-07.pdf

Government. This was demonstrated by the CEFC in its $295 million capital injection into PEC via a subordinated note instrument which contributed to the crowding in of further private sector debt.

The Federal Government's *Rewiring the Nation Policy* will invest $20 billion to rebuild and modernise the grid, in line with the projects outlined in the ISP. The Government plans to establish the Rewiring the Nation Corporation (RNC) which will partner with industry and provide low cost finance to build these ISP projects.

RE-Alliance finds it surprising that this option is not even canvassed in the report. RE-Alliance raised it as a potential funding mechanism in our last submission to the *Transmission Planning and Investment Review Consultation Paper*.

Admittedly, the current Government was the then Opposition during most of the time this report was being written, but a major alternative funding source should surely be considered when deliberating on policy options to address an issue such as financeability. In the event that Labor was not elected, the CEFC has shown its previous willingness to invest in transmission projects and the Victorian Government has a $540 million Renewable Energy Zone (REZ) Fund to invest in needed REZ network infrastructure.

RE-Alliance recommends that further iterations of this report should draw on consultation with the Government and AEMO and the CEFC, who will be administering the Rewiring the Nation Fund.

Social licence concerns

RE-Alliance is encouraged that the AEMC has recognised social licence as a key issue for consideration in the Review. We are pleased to note the AEMC's findings that compensation payments can be recovered through:

- preparatory activities, for which forecast operating expenditure (opex) is approved via the revenue determination process
- forecast costs assessed in the RIT-T and recovered under the CPA process
- cost pass-throughs, where TNSPs can seek to amend their revenue determination for specific pass-through events that are beyond the TNSPs reasonable control.

Whilst AEMC staff had told us verbally that this was the case, this is the first time we have seen this expressed in written form.

The AEMC states that "existing cost recovery mechanisms are appropriate and allow TNSPs to recover efficient costs associated with key activities to build and maintain social licence".[5] We propose that defining what efficient costs are is at the heart of the issue. The AEMC suggests that "decisions on the quantum of compensation received by impacted parties are the remit of jurisdictional instruments, not the national electricity rules (NER). The role of the NER is to allow for recovery of the efficient costs of meeting jurisdictional legislative requirements".

We note that the NSW Government has been undertaking a review of payment arrangements to landholders who host new transmission infrastructure. We understand that an announcement will be made in the near future on new measures to share the benefits associated with the transmission build more broadly within the affected community. It will be important that these measures apply both within REZs and to projects outside REZs (e.g. HumeLink). Ideally, payments would also be consistent across jurisdictions. So for example, in a project like PEC which crosses three states landholders would not receive different payments in different jurisdictions.

We have had discussions with the AER on this matter over the last year. As we understand it there are two possible options for determining what efficient costs might be.

1. As described by the AEMC, a jurisdictional instrument prescribes a certain amount of compensation or benefit sharing costs. In NSW, for instance, compensation costs are determined with reference to the *NSW Land Acquisition (Just Terms Compensation) Act 1991* or

2. The AER could provide advice to transmission companies on what efficient costs might look like. This might be in the form of Guideline and might for instance draw on the new NSW arrangements (once announced).

There is fairly broad consensus that current compensation arrangements under the *NSW Land Acquisition (Just Terms Compensation) Act 1991* and equivalent legislation in other jurisdictions is not commensurate with what landholders receive for hosting similar infrastructure such as wind turbines. Based on a wind turbine capacity of around 6 megawatts, landholders can receive up to $30,000 per turbine a year for hosting wind turbines, with payments usually being made annually over a 25 year period. By contrast, payments for transmission easements are one off and of a much smaller quantum of payment. Landholders would appreciate the flexibility of annual payments and payments being increased to a level which compensated them for any inconvenience or need to change farming practices, any potential loss in land value and which share the benefits that the transmission company and the broader community reap through placing new transmission infrastructure on their land.

[5] AEMC, Transmission planning and investment - Stage 2, Draft report, 02 June 2022 p 21 available at: https://www.aemc.gov.au/sites/default/files/2022-06/stage_2_draft_report_-_transmission_planning_and_investment_review.pdf

We further note that consideration is being given to the question of how TNSPs could share these benefits beyond transmission hosts to highly impacted neighbouring properties and local communities. This is an area the AER should consider in its deliberations on these questions.

We await the NSW Government's announcement of new arrangements with interest. It may be beneficial for the AER to provide guidance on what constitutes efficient costs to all transmission companies operating across the NEM.

We also understand that there is a multi-jurisdictional working group considering landholder transmission payment issues. Depending on the details of the NSW Government announcement and its community reception, other jurisdictions may be interested in mirroring the new NSW Government arrangements.

RE-Alliance recommends that the AEMC and AER consider the concept of a Guideline and consult with jurisdictions and assess whether it would be more useful than each individual jurisdiction implementing separate arrangements.

The AEMC also considers whether existing consultation arrangements are appropriate and finds that "the obligations within the NER for TNSPs to build and maintain social licence are largely appropriate".[6]

In our report *Building Trust for Transmission: Earning the Social Licence Needed to Plug in Australia's Renewable Energy Zones* RE-Alliance recommended:

1. That engagement start early during the RIT-T process and includes:
   - landholders and asset owners along potential transmission line routes;
   - local community members and groups;
   - local Councils and State Planning Departments; and
   - First Nations, environment and other special interest groups.
2. The RIT-T cost benefit analysis is expanded to include consideration of social and environmental costs and benefits on local communities.

The lived experience of communities facing the acquisition of new easements and the building of new transmission lines through their properties is that they often do not hear about it until well after the RIT-T has been completed, during the jurisdictional planning process, when they may be approached my a transmission company representative informing them that an easement is sought over their property.

Despite what the AEMC considers as appropriate requirements in the NER, communities are uninformed and subsequently angry, hence our first recommendation above.

[6] *Ibid.* p27.

Since the publication of our report we have found transmission companies very receptive to this suggestion. For example, Powerlink has published a Community Engagement Strategy[7] which has a series of commitments including “Be an active community member: engage early and often”.

Our second recommendation that “the RIT-T cost benefit analysis is expanded to include consideration of social and environmental costs and benefits on local communities” was taken up by the Hon Chris Bowen, during the election campaign when he foreshadowed a review of the RIT-T.

During his address to this year’s Energy Networks Australia Conference he stated that a Labor Government “would work with the states, market bodies, networks, and most importantly communities, to improve the RIT-T process…. He announced the following three directions for reform:

- First, affected communities should be heard much more clearly in the RIT-T process, and indeed throughout transmission planning. That should include genuine engagement from the start, not the end, of the process.
- Second, the RIT-T process should better capture social and economic benefits.
- Third, the RIT-T process should be no longer or more onerous than is necessary”.[8]

RE-Alliance is concerned that the report does not mention this Government commitment and more concerned that the AEMC does not seem to understand the depth of feeling in the community running against some proposed transmission projects, particularly the Western Victorian Transmission Network Project, recently renamed the Western Renewables Link.

RE-Alliance understands that including the social and environmental costs and benefits on local communities within the RIT-T cost benefit analysis is a somewhat radical suggestion within energy market circles, as there is an existing preference for only counting direct market costs and benefits.

As with climate action, another area which has been limited by this exclusive market cost and benefits approach, the costs of inaction may be much larger than taking early action.

We note AusNet’s submission to the Transmission Planning and Investment Review Consultation Paper where they say:

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[7] Powerlink Community Engagement Strategy available at: https://www.powerlink.com.au/sites/default/files/2021-08/Community%20Engagement%20Strategy.pdf

[8] Chris Bowen MP, Shadow Minister for Climate Change and Energy Address to Energy Networks Australia Conference 18 March 2022.

"There is no acknowledgement or requirement for early consideration of potential social and environment impacts that may be of concern to communities.

NER clause 5.15.2(a) defines a credible option is an option (or group of options) that addresses the identified need, is commercially and technically feasible, and can be implemented in sufficient time to meet the identified need. Feasibility as defined here does not consider social or environmental impacts.

As a result, the existing regulatory framework (notably the RIT-T) does not provide for early consideration of potential social and environmental impacts that may be of concern to communities. Instead, these impacts and stakeholders' associated view of them, are addressed much later via statutory approvals and are subject to variations between jurisdictions (e.g. environmental impact assessments, cultural heritage approvals, land use planning approvals, environmentally protected species approvals)".[9]

We note that in Western Victoria AusNet is facing fierce opposition from some members of the local community who are opposed to the preferred route of the Western Renewables Link and wish to see the line undergrounded. This would be massively more expensive, and a cost borne by all consumers. If the initial RIT-T had included consideration of social and environmental costs and benefits a different route may have been chosen. Instead, the need to develop new route alternatives in response to community concern has significantly delayed this project[10].

This process may well have been complicated and difficult to undertake and involved the development of new methodologies, but the reality is that without social licence such projects will continue to be severely delayed, face increased costs and may not go ahead at all.

That is the cost of inaction and this is what the Government's RIT-T review seeks to address.

RE-Alliance hopes that the Final Report is guided by the Government's announced priorities and any further development in this area between now and then.

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[9] AusNet submission to the Transmission Planning and Investment Review Consultation Paper p. 10. available at: https://www.aemc.gov.au/sites/default/files/documents/ausnet_services_5.pdf
[10] Simlilar delays have been encountered with the proposed transmission link to NSW's Central West Orana, where local opposition saw the original route abandoned after over a year of consulation https://www.dailyliberal.com.au/story/7650727/alliance-celebrates-central-west-orana-renewable-energy-zone-being-relocated/

Cost recovery of planning activities

RE-Alliance notes the AEMC's intention to "make changes to distinguish between planning activities for actionable ISP projects based on whether they relate to the selection or delivery of a preferred option to meet an identified need. This will be given effect through:

- amending the definition of 'preparatory activities' in the NER to further clarify that their purpose is to inform the selection of a preferred option.
- removing the term 'early works' from AER and AEMO documentation and replacing it with consistent language that characterises activities as either preparatory or not, based on their purpose. That is, whether an activity relates to the selection of a preferred option (in which case it is a preparatory activity) or delivery of a preferred option (in which case it is not a preparatory activity)".[11]

RE-Alliance would support this proposed change and agrees with the AEMC that the current arrangements could cause some confusion and uncertainty in cost recovery arrangements for both transmission companies and the AER. We agree that having the NER referencing 'preparatory activities' while AER and AEMO documents refer to 'early works' is confusing.

We note that the definition of preparatory activities in the NER is:

> *"preparatory activities means activities to design and investigate the costs and benefits of actionable ISP projects, future ISP projects and REZ stages (as applicable), including:*
> *a) detailed engineering design;*
> *b) route selection and easement assessment work;*
> *c) cost estimation based on engineering design and route selection;*
> *d) preliminary assessment of environmental and planning approvals; and*
> *e) council and stakeholder engagement".*[12]

We find Figure 4.1 helpful in that it clarifies that preparatory activities include planning activities required by the ISP and the RIT-T process and that these costs are recovered via a TNSP's opex allowance. Other planning activity related costs can be recovered via the staged CPA process.

We note the AEMC's comments that there is still some confusion with regards to cost recovery arrangements when there is a "combination of activities required to identify

[11] AEMC, Transmission planning and investment - Stage 2, Draft report, 02 June 2022 p 35 available at: https://www.aemc.gov.au/sites/default/files/2022-06/stage_2_draft_report_-_transmission_planning_and_investment_review.pdf

[12] Clause 5.10.2 of the NER.

the preferred option (preparatory activities) and activities to deliver the preferred option (such as easement acquisition)".[13]

We agree that this is a complex area, as community and landholder engagement clearly need to occur during the preparatory activities stage, and arranging easement purchase arrangements are a time consuming process which needs to be commenced as early in the process as possible. Nonetheless, this does seem to be more a delivery related item and we welcome the AEMC's further consideration of this matter in Stage 3 of the report.

Something that RE-Alliance has previously suggested is that there might be a role for Government in funding what we referred to as the pre-planning stage of all the proposed transmission lines in the ISP (by which we meant preparatory activities). By undertaking the preparatory activities immediately it would provide more time for community engagement and to get route selections right, while also reducing the timelines for transmission projects potentially by several years. With the preparatory activity works done, transmission investment decisions could then be accelerated when they are needed rather than the later dates given in the 2022 ISP.

This option was partially accepted by AEMO when they stated in the 2022 ISP that immediate action to progress actionable projects is needed. They continue:

> *"Government support through finance, underwriting or other measures, fast-tracked licencing and environmental assessments, and streamlining of the regulatory framework governing critical transmission projects identified in the ISP, would assist in accelerating their delivery to realise these potential benefits".*[14]

RE-Alliance considers that there could be a role for the Rewiring the Nation Fund to potentially fund preparatory activities for actionable projects, with the build itself being paid for as normal through the contingent project application (CPA) process.

As we have noted previously, "recovering funding for transmission projects from electricity consumers is a regressive form of taxation. The provision of State and/or Federal government funding to support the roll out of this essential transmission infrastructure is progressive and would reduce the burden shouldered by energy consumers".[15]

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[13] AEMC, Transmission planning and investment - Stage 2, Draft report, 02 June 2022 p 45 available at: https://www.aemc.gov.au/sites/default/files/2022-06/stage_2_draft_report_-_transmission_planning_and_investment_review.pdf

[14] AEMO, 2022 Integrated System Plan, June 2022. p 16 available at: https://aemo.com.au/-/media/files/major-publications/isp/2022/2022-documents/2022-integrated-system-plan-isp.pdf?la=en

[15] RE-Alliance submission to the AEMC Transmission Planning and Investment Review p.9 available at: https://d3n8a8pro7vhmx.cloudfront.net/vicwind/pages/2672/attachments/original/1637561961/REA_Submis

RE-Alliance recommends that AEMO and the CEFC, who will be administering the Rewiring the Nation Fund, give consideration to funding preparatory activities for actionable ISP projects.

Improving the workability of the feedback loop

RE-Alliance agrees with the AEMC that aligning the feedback loops with the publication of a draft or final ISP will improve workability. Further, we agree with the AEMC that Option 2 which involves aligning the feedback loop and project assessment conclusions report (PACR) exclusion window between the final inputs, assumptions and scenarios report (IASR) and draft ISP, with feedback loop requests permitted any other time in the ISP cycle is the preferred option. Aligning the feedback loop with the draft ISP would give more time for the feedback loop to operate. Further delays to the RIT-T process should be avoided if at all possible.

We agree that there is potential for delay due to the bunching of feedback loop assessments and we agree with the AEMC's proposed solution - allowing the contingent project application (CPA) and feedback loop to run concurrently. Finally, we agree with the AEMC that Option 2: amending the AER's Cost Benefit Analysis (CBA) Guidelines is an appropriate way of giving practical effect to the Commission's recommendation.

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