



Mr Rupert Doney
Australian Energy Market Commission
Level 6, 201 Elizabeth Street
Sydney NSW 2000

Lodged through online portal

17 August 2022

Dear Mr Doney,

Transmission Planning and Investment Review (EPR0087) – Contestability Options Paper

ENGIE Australia & New Zealand (ENGIE) appreciates the opportunity to respond to the Australian Energy Market Commission (“the Commission”) in response to the Transmission Planning and Investment Review Contestability Options Paper (“the Paper”).

The ENGIE Group is a global energy operator in the businesses of electricity, natural gas and energy services. In Australia, ENGIE has interests in generation, renewable energy development, and energy services. ENGIE also owns Simply Energy which provides electricity and gas to more than 740,000 retail customer accounts across Victoria, South Australia, New South Wales, Queensland, and Western Australia.

International evidence shows contestability is a viable approach

ENGIE commends the AEMC for commissioning the analysis from KPMG reviewing international regulatory frameworks that allow and encourage contestability in the provision of transmission services. This has provided robust evidence that contestability can be a viable approach to delivering transmission services. There are notable successes as well as opportunities to learn from other jurisdictions.

Inevitably it is always difficult to fully quantify the net gains to consumers from introducing competition to transmission services, as the assessment is dependent on constructing a plausible counterfactual. Nonetheless it is reasonable to suppose that where the new transmission (or non-network option) has been delivered that it has been as cheap or cheaper than a regulated monopoly approach, given the pressures of competition. Claims to the contrary appear to have come mostly from incumbent transmission network service providers (TNSPs¹) and should be assessed prudently.

One potential benefit not fully canvassed in the KPMG report is the opportunity to take information from competitive transmission processes and use it to improve monopoly network revenue determination processes. In these processes, the efficient cost of capital must be estimated for a notional network entity, but in a model such as the UK’s OFTO tenders, bidders are competing on lower costs, including the cost of

¹ This is the Australian term, and other jurisdictions may use different terms for broadly the same type of business. For simplicity “TNSP” is used throughout this submission to refer to domestic and international transmission service providers. Page 1

financing. While an offshore transmission connection asset may not be completely analogous to a full transmission network, it is close enough to provide at least an indirect benchmark on efficient financing costs and structures.

The KPMG case study report identifies that the British regulator Ofgem is considering an onshore wind model where the incumbent TNSP builds the new asset, but it sets allowed revenue based on OFTO benchmarks for efficient financing costs². But Ofgem has stated that it is already using this information as evidence to help it set an efficient rate of return for all regulated energy networks³. The combined regulatory asset base (RAB) of energy networks regulated by the AER is over \$100bn, so any new information that helped them set a more efficient rate of return would have a material benefit for consumers.

Contestability models should focus on the scope for greatest gains

ENGIE considers there are two areas of the transmission process where contestability would have the most benefit, and this should be taken into account when designing a contestability model for the NEM.

1. Innovative solutions to meet needs

Possibly the greatest possible benefit is to encourage the widest possible range of solutions to meet the identified transmission need. This would include non-network solutions, noting that these are not applicable to all transmission requirements. However, where they could be a viable solution, they are more likely to be proposed by parties other than the incumbent TNSP, whose expertise is primarily in building and operating traditional transmission assets.

Analysis of DNSP expenditure by Energeia⁴ found that regulatory investment tests appeared significantly biased towards traditional “poles and wires” solutions built by the incumbent DNSP carrying out the test with very few non-network options being chosen instead. A similar bias is likely for TNSPs. Analysis by CEPA⁵ for the Commission considered capital expenditure bias more broadly and found a range of reasons why capex may be preferred that went beyond the structure of the financial incentives built into the regulatory framework.

Accordingly, to maximise this type of benefit, an early-stage contestability approach would be required, which could potentially be met through the Commission’s straw person 4. The party running the tender process would need to be a disinterested party, i.e., they could not also be a bidder, and they would need to have no financial incentive to favour one type of solution over another. Given these criteria, it is unlikely that the TNSPs would be well placed to carry out this role, as they are likely to want to participate in the tender too. AEMO would be the obvious alternative for a NEM-wide process.

² International and domestic examples of transmission contestability case studies report, KPMG, July 2022, p31

³ See for example: [RIO-2 Final Determinations – Finance Annex](#), Ofgem, February 2021, p53

⁴ [DER Optimisation final report](#), Energeia, 2022

⁵ [Expenditure incentives faced by network service providers](#), CEPA, July 2018

ENGIE recognises that this is the straw person that would require the greatest changes to the existing framework, and the details of the approach would need to be carefully considered to ensure no unanticipated consequences. The successful bidder would need to co-ordinate with the incumbent regional TNSP and AEMO to ensure integration of their solution into the existing system. ENGIE notes that while the tripartite approach in Victoria is often subject to criticism, a comparable issue arises when a new interconnector is built, and the incumbent TNSPs have to co-ordinate to ensure their shares of the overall project integrate with each other. This arrangement has not been the subject of complaints by incumbents.

A further consideration is that the Commission has identified that this model requires a NEM-wide approach to be fully effective. ENGIE agrees that in general, NEM-wide processes are more efficient and effective than separate jurisdictional approaches. However, NEM reform is currently proceeding along a twin track of developing NEM-wide solutions in the Rules and jurisdictions using their powers to implement alternative approaches when they choose to do so. So, concerns that some jurisdictions are working on their own models of contestability should not inhibit development of a NEM-wide approach.

Accordingly, ENGIE considers this model could deliver significant long run benefits to consumers and should be developed further.

2. Lower costs to deliver an agreed solution

Late-stage models of contestability can also deliver savings to consumers by lowering the costs to deliver an agreed solution. TNSPs will rightly point out that they typically run a competitive tender for the construction works. This is true, but for example, for Project EnergyConnect, these subcontracted works only accounted for 78 per cent of the total sought by TransGrid and ElectraNet through their contingent project applications (CPA). The other 22 per cent of costs were not subject to this type of competitive comparison and consumers relied on the AER to find whatever scope for savings they could.

As noted above, another potential significant source of savings is through lower finance costs. Accordingly, any late-stage model of contestability should include finance costs as part of the tender structure, as Ofgem does in its OFTO model, rather than simply award the successful bidder a regulated rate of return. While setting up a tender process may take some time, it has the scope to replace two current regulatory processes with one, i.e., the RIT-T application and the CPA. So, the overall elapsed time may be shorter than under current arrangements.

Other considerations

ENGIE considers the Commission's proposed assessment criteria to be reasonable. As the Commission has identified there are trade-offs to consider in assessing different options and so it is likely that the weight given to different factors will play an important role in the Commission's decision.

To that end, ENGIE considers that given straw persons 1-3 are all analogous to existing NEM or jurisdictional processes, the implementation costs and challenges, timeliness concerns and accountabilities should all be relatively low and manageable. This is not to suggest that the existing processes are necessarily optimal, and the Commission may identify improvements that can be made, but it would be counterintuitive that these straw persons should be considered to have significant barriers and costs to their implementation.

Conversely, straw person 4 may incur some complexity and additional implementation cost, and the accountabilities and efficient timeframes will need to be worked through, but the expected benefits should also be more material.

ENGIE considers that the potential benefits of contestability are such that the Commission should seek to maximise the scope of projects to which contestability will apply. Network extensions such as renewable energy zones (REZs) and new interconnectors are obvious candidates, and there may be scope to extend coverage further.

If the Commission wishes to be cautious, it could iterate application by starting with these categories and then extending coverage one a few tenders have been carried out and the net benefits are clearer. The more projects are contestable, the more potential bidders are likely to be attracted. The Commission should take comfort from the fact that the first NSW REZ tender attracted three credible bidders who were not the incumbent TNSP. This illustrates that if a tender process is designed appropriately to attract bidders, there are sufficient potential candidates to ensure some competitive pressures.

It is also worth considering a twin-track process. Given late-stage models similar to straw persons 1-3 already exist in the NEM, including the existing Victorian arrangements and the new NSW REZ arrangements, then these do not represent radical new reforms. If the Commission is able to determine that one of its straw persons 1-3 (with tweaks as necessary) is viable it may be able to implement this approach sooner rather than later, and then take some time to fully develop an early-stage process. The UK is an example where late-stage models have been implemented initially to prove up contestability before developing early-stage models which are more complex to design.

Should you have any queries in relation to this submission please do not hesitate to contact me via jamie.lowe@engie.com.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Jamie Lowe', written in a cursive style.

Jamie Lowe

Head of Regulation,
Compliance and Sustainability