

5 September 2022

Ms Anna Collyer
Chair
Australian Energy Market Commission
Sydney South NSW 1235

By online submission

Dear Ms Collyer,

Material change in network infrastructure project costs (ERC0325)

The Australian Energy Market Operator (AEMO) welcomes the opportunity to comment on the Australian Energy Market Commission's (AEMC) draft determination in relation to 'material change in circumstances' (MCC) provisions for the Regulatory Investment Test (RIT). These provisions are of importance to AEMO in its roles as National Transmission Planner (hereafter referred to as 'AEMO NP') responsible for preparing the Integrated System Plan (ISP) and triggering the RIT-T for actionable ISP projects and also as Victorian Transmission Planner (hereafter referred to as 'AVP') responsible for applying the Regulatory Investment Test for Transmission (RIT-T) to augmentations of the Victorian Declared Shared Network.

AEMO acknowledges the broad scope of the draft determination which considers all RITs. Given the roles of AVP and AEMO NP in planning major transmission projects, this submission focuses on material changes relevant to RIT-Ts subject to the actionable ISP framework.

AEMO disagrees that the revised MCC provisions promote efficient outcomes for consumers by appropriately balancing the timely and economic delivery of network projects. Revising the MCC provisions as proposed would add further regulatory obligations and complexity and reduce the likelihood that actionable projects are delivered within the optimal timing identified in the ISP. These revisions reduce investment certainty and are an unnecessary administrative burden that will not improve current outcomes under the existing MCC provisions.

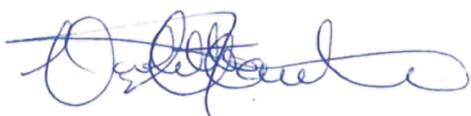
AEMO supports the AEMC's draft position to exempt AVP from developing reopening triggers for Victorian RIT-T applications and agrees AVP is not subject to the same incentives as other Transmission Network Service Providers (TNSPs). The special arrangements for major transmission investments in Victoria should be taken into account when considering the application of MCC provisions to AVP.

There remains a lack of clarity as to how RIT-T requirements are assessed and which body is responsible for their assessment. AEMO does not have a role in RIT-T compliance and disagrees with the AEMC's draft position that the AER currently does not have a role in assessing RIT-Ts. The actionable ISP framework already provides an opportunity to address a MCC before a contingent project application (CPA) is considered.

Cost estimation accuracy and consistency at various stages in the ISP framework is more important than revising the MCC provisions. AEMO agrees that this is most appropriately addressed within AER guidelines. However, AEMO supports less reliance on binding obligations within AER guidelines and more meaningful engagement on the consistent application of an appropriate cost estimate classification system, appropriate cost estimate classes for ISP, RIT-T and CPA processes, the consistent capture of risk and contingencies and the provision of transparent cost breakdowns. Five preliminary recommendations to improve the accuracy and consistency of transmission cost estimates for ISP, RIT-T and CPA processes within the actionable ISP framework are included in Attachment 1 below.

Should you wish to discuss any of the matters raised in this submission, please contact Paul Rositano, Specialist Network Regulation (paul.rositano@aemo.com.au).

Yours sincerely,



Violette Mouchaileh

Executive General Manager – Reform Delivery

ATTACHMENT 1:

This section provides more detail on AEMO’s view on:

- the application of the revised MCC provisions in the National Electricity Market (NEM) for actionable ISP projects where AEMO NP has a role in triggering RIT-Ts via the ISP and assessing the RIT-T preferred option via the feedback loop, and
- improving transmission cost estimate accuracy and consistency, including specific recommendations to achieve improvements for ISP, RIT-T and CPA processes within the actionable ISP framework.

APPLICATION IN THE NEM

Revised MCC provisions do not promote timely delivery of network projects

AEMO disagrees that the revised MCC provisions promote efficient outcomes for consumers by appropriately balancing the timely and economic delivery of network projects. Revising the MCC provisions as proposed would add further regulatory obligations and complexity and reduce the likelihood that actionable projects are delivered within the optimal timing identified in the ISP.

AEMO submissions on the Transmission Planning and Investment Review urged the AEMC to consider streamlining regulatory processes for transmission projects identified as actionable in the ISP and the removal of duplicative processes and complex and excessive regulatory obligations.¹ AEMO considers that the streamlining benefits sought when the ISP framework commenced in July 2020 have not been realised.

The AEMC’s draft determination describes the revised MCC provisions as allowing RIT proponents to propose more appropriate, more timely and less costly courses of action than full reapplication of the RIT.² In practice, however, AEMO expects that situations requiring RIT reapplication to be exceptional (as recognised by the AER’s RIT-T and RIT-D Application Guidelines), and further, situations requiring reapplication of the RIT in its entirety to be more limited again.³

AEMO agrees the RIT-T proponent is best placed to determine whether a MCC has occurred and the RIT-T should be reapplied. References to “a MCC” throughout this submission refer to a change, which in the reasonable opinion of the RIT-T proponent, means that the preferred option identified in the Project Assessment Conclusions Report (PACR) is no longer the preferred option, or an ISP or ISP update shows a change to the relevant identified need, consistent with the MCC provision for actionable ISP projects.⁴

¹ Submissions available at: <https://www.aemc.gov.au/market-reviews-advice/transmission-planning-and-investment-review>.

² AEMC, *Draft Rule Determination: National Electricity Amendment (Material change in network infrastructure project costs) Rule* (‘Draft determination’), 7 July 2022, p.11.

³ See section 4.5 in both the RIT-T and RIT-D Application Guidelines.

⁴ See NER clause 5.16A.4(n)(2).

A RIT-T proponent should assess a MCC on a case-by-case basis taking into account the magnitude and driver of the change and, for market benefits-driven RIT-Ts, the net market benefits buffer the preferred option has above zero and relative to other credible options. The same change that results in a different preferred option for one RIT-T may result in no change in the preferred option for another, or a change in the cost of skilled labour or steel may similarly affect all the top-ranking credible options. AEMO strongly agrees the regulatory framework should avoid ‘analysis paralysis’ and unnecessarily delaying the development of efficient transmission investments.

The draft rule seeks to address these concerns by using reopening triggers that RIT-T proponents can tailor to a specific RIT-T application which, if triggered, may require further information or analysis to be provided to the AER, and by exempting RIT-T proponents from considering whether a MCC occurred within six months of completing a RIT-T or subsequently rerunning analysis. However, AEMO considers existing arrangements allow the AER to request further information from RIT-T proponents to demonstrate compliance with the MCC provision and, where a MCC has occurred, the AER has discretion within a determination to waive the requirement to reapply the RIT-T, either in part or in full.⁵

Revised MCC provisions are unnecessary

Introducing additional MCC obligations reduces investment certainty, risks additional cost for and timely delivery of transmission projects and imposes an unnecessary administrative burden that will not improve current outcomes under the existing MCC provisions. Currently, when a potential MCC occurs after RIT completion, RIT proponents often test the impact of that change and publish those results to demonstrate that the RIT preferred option remains unchanged.⁶ The existing MCC provisions do not require this, however, RIT proponents recognise the benefits of transparency and confirming the economic viability of a project with stakeholders and the AER. If a RIT proponent fails to do this and the RIT outcome is in doubt, the AER can challenge compliance with the MCC provisions via its compliance and enforcement role, or a stakeholder can approach the AER to raise compliance concerns which the AER may pursue if it considers there is merit.

AEMO disagrees with the AEMC’s draft position that the AER currently does not have a role in assessing RIT-Ts. The removal of the AER’s preferred option assessment as to whether the preferred option satisfies the RIT-T and addition of the AEMO feedback loop when the actionable ISP framework was introduced was used to support this position.⁷

While removal of the preferred option assessment may reduce AER visibility over relevant RIT-T costs and benefits, AEMO considers that the AER still has an important role in ensuring RIT-T proponents comply with the National Electricity Rules (NER). Indeed, the AER’s final decision on

⁵ RIT-T proponents must reapply the RIT to address a MCC unless otherwise determined by the AER (as per NER clause 5.16A.4(n)).

⁶ For example, see ElectraNet, ‘*Project EnergyConnect: Updated Cost Benefit Analysis*’, 30 September 2020, available at <https://www.electranet.com.au/projects/south-australian-energy-transformation>.

⁷ Draft determination, p.22. In accordance with former NER clause 5.16.6, the preferred option assessment included an AER determination as to “whether the preferred option satisfies the regulatory investment test for transmission”. The ESB’s ‘*National Electricity Amendment (Integrated System Planning) Rule 2020*’ commenced 1 July 2020 to include the actionable ISP framework and remove clause 5.16.6 from the NER.

guidelines to make the ISP actionable makes its role clear, including a proactive approach to monitoring compliance using various tools as supported by its compliance and enforcement policy.⁸

AEMO also notes that AER guidelines have introduced compliance reporting obligations on RIT-T proponents following PACR publication regarding binding elements of those guidelines.⁹ The AEMC's draft rule extends reporting requirements to the meeting of reopening triggers and the provision of any further information requested by the AER. Rather than mandating self-reporting, AEMO considers it is more appropriate and efficient for the AER to obtain additional information from RIT-T proponents on a case-by-case basis as part of its overarching compliance and enforcement role.

The actionable ISP framework is already weighed down by self-assessment and mandatory reporting. AEMO's preference is for fewer reporting obligations and a greater focus on meaningful engagement with stakeholders, including the AER. Despite these reporting requirements, there appears to be a lack of clarity as to how RIT-T requirements are assessed and which body is responsible for their assessment. AEMO does not have a role in RIT-T compliance, as discussed further below.

Feedback loop and the actionable ISP project trigger event

The AEMC's draft determination considers that the CPA process should be leveraged by requiring TNSPs to confirm that no reopening triggers have been triggered when submitting a CPA and provide supporting analysis, thereby creating a MCC checkpoint before a CPA is considered by the AER.¹⁰ However, the actionable ISP framework already provides an opportunity to address a MCC before a CPA is considered.

AEMO agrees that the feedback loop does not confirm that the RIT-T preferred option remains preferred. The feedback loop instead focuses on alignment of the RIT-T preferred option with the ISP optimal development path and confirming that the status of the project as "actionable" remains unchanged.

However, confirmation via the feedback loop is only one of the criteria that must be satisfied within the actionable ISP project trigger event (NER clause 5.16A.5). The first criterion (clause 5.16A.5(a)) is that the RIT-T proponent issues a PACR "that meets the requirements of clause 5.16A.4 and which identifies a project as the preferred option".¹¹ As clause 5.16A.4 includes the existing MCC provision for actionable ISP projects, a RIT-T proponent is ineligible to submit a CPA using the actionable ISP project trigger event if, at the time, the MCC provisions applied and in the reasonable opinion of the RIT-T proponent, the preferred option identified in the PACR was no longer the preferred option.

AEMO considers the requirement within clause 5.16A.5(a) reinforces the AER's compliance and enforcement role regarding the existing MCC provisions prior to consideration of a CPA. When

⁸ AER, *'Final decision: Guidelines to make the Integrated System Plan actionable'*, August 2020, pp.15-18, available at <https://www.aer.gov.au/networks-pipelines/guidelines-schemes-models-reviews/guidelines-to-make-the-integrated-system-plan-actionable>.

⁹ AER, *'Cost benefit analysis guidelines: Guidelines to make the Integrated System Plan actionable'*, August 2020, p.5.

¹⁰ Draft determination, p. 23.

¹¹ The 'preferred option' is defined within NER clause 5.15A.1(c) as "the credible option that maximises the present value of net economic benefit to all those who produce, consume and transport electricity in the market".

developing the actionable ISP framework, the ESB also recognised the link between clause 5.16A.5(a) and the MCC provision.¹² AEMO does not have a role in RIT-T compliance and is not required to consider whether a PACR meets the requirements of clause 5.16A.4 before assessing the preferred option in the feedback loop.

AEMO does not suggest that the requirement for a PACR to meet the requirements of clause 5.16A.4 prior to CPA lodgement necessitates an AER assessment akin to a preferred option assessment. Former NER clause 5.16.6 required the AER to make a determination within 120 business days (with provisions for extension) whereby the AER would review both the RIT-T process and outcome, including the reasonableness of inputs, assumptions and methodologies.¹³ Neither does AEMO suggest that a thorough MCC check is needed before accepting every CPA. As discussed above, the need to confirm compliance with the MCC provision should be based on the individual circumstances of the RIT-T and the nature of any changes since PACR publication. At a minimum, however, clause 5.16A.5(a) should allow the AER to make enquiries, if appropriate in the circumstances, as to whether MCC provisions apply prior to accepting a CPA.

The AER can do this simply by requesting that the RIT-T proponent provide information or analysis to demonstrate that no MCC occurred in compliance with clause 5.16A.4(n). Such requests can be made on a case-by-case basis where the RIT-T proponent has not already published an update that addresses any changes since PACR publication.

TRANSMISSION COST ESTIMATES

Transmission cost estimate accuracy and consistency are more important than revising MCC provisions

AEMO reiterates that cost estimation accuracy and consistency at various stages in the ISP framework is more important than revising the MCC provisions.¹⁴ The ISP framework does not require a specific class or accuracy level of cost estimates for ISP, RIT-T and CPA processes. Feedback received during IASR consultations revealed that there was a range of conflicting expectations on the appropriate level of cost estimate accuracy within these processes.

When developing an ISP, differences in the accuracy of cost estimates requested from TNSPs require AEMO to undertake a validation process to ensure consistency. Improved cost estimate accuracy and consistency will help address issues associated with changes in cost estimates at various regulatory stages by increasing certainty as to how estimates are calculated and the treatment of risk.

¹² The ESB's response to submissions on its Draft ISP Rules states: "NER 5.16A.4(n) together with 5.16A.5(a) and the revised transitional provisions together require existing actionable ISP projects to reapply the RIT-T using either the old or new framework in the event of a material change in circumstances." ESB, *Converting the Integrated System Plan Into Action: Response to submissions on Consultation Draft ISP Rules*, March 2020, p.19, available at: <https://www.energy.gov.au/government-priorities/energy-ministers/energy-ministers-publications/actionable-isp-final-rule-recommendation>.

¹³ For example, see AER Decision, *South Australian Energy Transformation: Determination that the preferred option satisfies the regulatory investment test for transmission*, January 2020 at: <https://www.aer.gov.au/system/files/AER%20-%20Determination%20-%20SAET%20RIT-T%20-%2024%20January%202020.pdf>.

¹⁴ As submitted in response to the AEMC's TPIR consultation paper.

The AEMC's draft rule makes clarifying amendments to allow relevant AER guidelines to provide guidance in relation to acceptable cost estimate classification systems that should be used for the RIT and the role for contingency allowances. AEMO agrees that cost estimate accuracy and consistency is most appropriately addressed within AER guidelines. However, AEMO disagrees that binding guideline obligations and associated mandatory compliance reporting are required to promote the development of estimates consistent with any new guidance.

Prior to the commencement of the actionable ISP framework and the introduction of binding elements within AER guidance, RIT-T proponents were always very conscious of applying the RIT-T consistent with the RIT-T Application Guidelines. Rather than identifying formal compliance obligations, it was commonly understood that relevant guidance within the RIT-T Application Guidelines represented the AER's view and its likely approach to assessing compliance with the NER and RIT-T instrument when considering a RIT-T dispute, preferred option assessment or general compliance enquiry.

AEMO supports less reliance on binding obligations within AER guidelines and more meaningful engagement on the consistent application of an appropriate cost estimate classification system, appropriate cost estimate classes for ISP, RIT-T and CPA processes, the consistent capture of risk and contingencies and the provision of transparent cost breakdowns. The outcomes of this engagement should inform AER guideline amendments. AER and stakeholder expectations shared during ISP, RIT-T and CPA consultations would help drive outcomes consistent with this new guidance without the need for binding elements. In the interest of enhancing this discussion and in anticipation of future engagement, AEMO has provided some preliminary recommendations below.

AEMO recommendations for improving transmission cost estimate accuracy and consistency

AEMO makes the following five preliminary recommendations to improve the accuracy and consistency of transmission cost estimates for ISP, RIT-T and CPA processes within the actionable ISP framework:

Recommendation 1: The AACE international cost estimate classification system should be used as a standard.

Recommendation 2: The application of AACE cost estimates should be standardised given AACE does not provide guidance on how to apply cost estimates within a cost-benefit analysis.¹⁵ For example, sensitivity testing on the upper end of a cost estimate within a given class could be a standard. A checklist or guidance should be developed to promote consistent application of AACE cost estimates.¹⁶

Recommendation 3: Cost estimates should include reasonable approximations for any cost that ultimately impacts on consumer bills, including highly uncertain costs such as contingency allowances and environmental offsets.

¹⁵ AACE currently provides guidance on estimating a cost and uncertainty range but not on how to apply that distribution of potential costs to an economic assessment.

¹⁶ Similar to the checklist shown in Appendix A1 to AEMO's 2021 Transmission Cost Report, available at <https://aemo.com.au/en/consultations/current-and-closed-consultations/transmission-costs-for-the-2022-integrated-system-plan>.

Recommendation 4: AEMO or TNSPs (as relevant) should publish:

- breakdowns for all transmission cost estimates used in the ISP (including preparatory activities), RIT-T and CPA, and
- project estimates for RIT-Ts and CPAs using AEMO's Transmission Cost Database to enable stakeholders to understand differences between TNSP estimates and NEM-wide average values.

If this cannot be provided, TNSPs should provide this information to AEMO to enable a public transmission cost database to be developed, published and maintained. Project data for individual projects would be averaged and anonymised for each ISP cycle.

Recommendation 5: Preparatory activities and REZ design reports should be published by AEMO on behalf of TNSPs, including information regarding scope, all component costs, uncertainty ranges and classifications. Costs and scope should not be made confidential.

ATTACHMENT 2:

This section provides AEMO's view on the proposed application of the revised MCC provisions in Victoria where AVP is RIT-T proponent.

APPLICATION IN VICTORIA

AEMO supports the AEMC's draft position to exempt AVP from developing reopening triggers for Victorian RIT-T applications. As acknowledged in the AEMC's draft determination, AVP is not subject to the same incentives as other TNSPs.¹⁷ When exercising declared network functions in Victoria, the sole adoptive jurisdiction in the NEM, AVP must promote efficient investment in network infrastructure in accordance with the National Electricity Objective.

The special arrangements for major transmission investments in Victoria should be taken into account when considering the application of MCC provisions to AVP. Transmission investment in Victoria is subject to contestability that allows flexibility, encourages innovation and permits multiple proponents to competitively bid for the right to construct, own, operate and maintain major transmission projects. This contestable approach relies on competitive pressure from a broader collection of interested parties to produce prudent and efficient outcomes.

¹⁷ Draft determination, p.28-9.