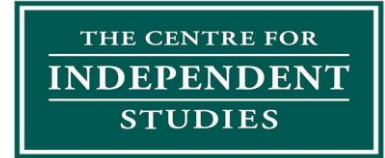


4 July 2024

Ms Anna Collyer
Chair
Australian Energy Market Commission
Submitted via www.aemc.gov.au



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RE: Submission to AEMC's Draft Rule Determination for ERC0380 *Bringing early works forward to improve transmission planning*

Dear Ms Collyer,

The Centre for Independent Studies (CIS) welcomes the opportunity to respond to the AEMC's Draft Rule Determination for the *Bringing early works forward to improve transmission planning* rule change.

The CIS is a leading independent public policy think tank in Australia. It has been a strong advocate for free markets and limited government for more than 40 years. The CIS is independent and non-partisan in both its funding and research, does no commissioned research nor takes any government money to support its public policy work.

Our view is that the draft rule does not give sufficient protection to consumers against the risk of significant costs being incurred as part of early works that are not ultimately needed, because the preferred option or entire project ends up not being in consumers' best interests. There is an asymmetry in the weight given to the risk of project delays, which presumes the project should proceed, and should not ideally be delayed. The risk of over-investment and premature investment must be balanced with delayed investment to protect the long-term interests of consumers. The draft rule fails to protect consumers from unnecessary expenditure.

We also object to the AEMC review being delayed by two years. Unlike the AEMC's review, the Commonwealth's review has no statutory obligation to protect the long-term interest of consumers, and recent actions by the Commonwealth make clear that other policy priorities such as emissions reductions have taken precedence over considering costs. The Commonwealth review recommendations do not address the current issues with the ISP around the unaffordability of the ODP for consumers and the lack of transparency around costs of government policies included as binding constraints in the ISP model. The AEMC review should proceed as scheduled in the NER to ensure

consumer interests are adequately protected, particularly concerning the costs imposed by government policy constraints in the ISP model.

These two issues must be addressed to ensure the rule change sufficiently protects consumers from overinvestment in transmission projects.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'A Morrison'.

Aidan Morrison
Director of Energy Program
Centre for Independent Studies
Email: amorrison@cis.org.au

Outcomes for consumers

One of the key criteria the AEMC has used in assessing this rule change is outcomes for consumers. However, the scope of possible outcomes for consumers considered by the AEMC is too narrow and thus fails to adequately protect consumers through the draft rule. This is because the risk of overinvestment in projects that do not end up being needed — or are not needed until many years later — is not given sufficient weight in bringing forward early works.

On page 5 of the draft determination, the AEMC defines this criterion around the question, “Does the draft rule improve planning for actionable ISP projects to ensure the best outcomes for consumers — in terms of mitigating the risk for project delays and later cost increases for consumers?” This criterion only deals with risks associated with project delays and not risks arising from overinvestment in early works for projects that subsequently fail the Regulatory Investment Test for Transmission (RIT-T) and do not go ahead.

The AEMC further states:

“The Commission’s draft rule would improve cost recovery certainty for efficient and earlier planning activities. Undertaking more planning activities, earlier in the process would enable TNSPs to develop options for transmission investment that more accurately reflect social, cultural, heritage and environmental impacts. This would mitigate the risk of later project cost increases and delays because of later consideration of these factors. Bringing these activities forward could also mitigate the risk of additional costs to consumers due to supply chain delays and labour supply issues by enabling TNSPs to secure long lead time items earlier in the planning process.”

The AEMC’s ultimate role is serving the long-term interests of consumers. Improving cost recovery certainty for Transmission Network Service Providers (TNSPs) should not be weighed more greatly than protecting consumers from overinvestment or projects being delivered sooner than needed. This is especially important for significant costs such as those arising from procuring long lead time equipment. Consumers are not only at risk of future project cost increases, but also at risk of paying for early works of projects that do not end up proceeding. The AEMC must also consider that delaying projects could ease supply constraints and reduce the cost of projects in the future. As stated on page 1, the draft rule aims to “protect consumers against inefficient expenditure.” But the draft rule fails to protect consumers from *unnecessary* expenditure.

On page 8, the AEMC states:

“Bringing these activities forward could also mitigate the risk of additional costs to consumers due to supply chain delays and labour supply issues by enabling TNSPs to secure long lead time items earlier in the planning process. We consider that, on balance, incurring greater costs of planning earlier in the process will significantly benefit consumers by avoiding greater costs to consumers in the future.”

The claim that bringing forward the purchasing of long lead time equipment will avoid greater costs to consumers in future rests on the assumption this equipment will be required; if not for the preferred option, then for a different option or project.

The draft rule states:

(d1) In assessing whether to approve the costs of early works for an actionable ISP project where that project has not been the subject of a completed regulatory investment test for transmission, the AER must have regard to whether the:

(1) early works are common to all ISP candidate options and any other options that would be identified in a regulatory investment test for transmission for the actionable ISP project; and

(2) outcome of the early works can be sold or utilised to support other projects.

This wording does not protect consumers against an outcome in which none of the options pass the RIT-T, and the equipment does not end up being able to be used for another project or sold due to a broad-scale suspension of ISP projects. This is now a plausible scenario, as an alternative future government could pursue an energy policy which would mean none or very few of the actionable ISP projects that are designed to support renewables end up being built. The AEMC needs to take into account the major risk this presents to consumers that TNSPs will use early works cost recovery for items that do not end up being needed and (following a change of government) cannot be used for another project or sold, placing large unnecessary costs on consumers.

This risk of overinvestment is acknowledged in the Energy Minister’s rule change request on page 8:

“There is the risk of a TNSP recovering costs for early work, which are passed on to consumers, but the project does not go ahead. However, the Commonwealth considers the risk of this eventuating is low.”

There is no obvious reason why the Commonwealth should consider this risk low. This assumption seems to favour the interest of TNSPs over those of consumers. The rules must appreciate that there is an inherent tension between the natural interest of TNSPs, who

benefit from any project proceeding at the earliest schedule, and consumers who will necessarily bear the costs, with offsetting benefits entirely dependent on a suitable economic cost-benefit analysis showing the project is necessary and preferred.

Previous decisions made by the AEMC do not show adequate appreciation of this tension, and the importance of scrutiny and consultation necessary for protecting consumer interests. For example, when writing “projects seeking feedback loops are unlikely to see their status as part of the ODP change due to consultation on a draft ISP”, as stated by the AEMC on page 15 of the final determination for *Improving the workability of the feedback loop*, it appears that the AEMC has also adopted a position that assumes a low risk of unmerited projects being advanced, but needing to be cancelled following closer scrutiny.

If AEMO were to use consultation with consumers on the draft ISP in a non-trivial way (i.e., allowing consumer feedback to have a material impact on the final ODP), then this risk of overinvesting in early works for projects that do not proceed would not be “low”. Given that this rule change removes the requirement for some of the earlier merit-tests and consultation processes to occur before expenditure on a project is incurred, the assumption that the risk of projects being cancelled remains low does not adequately protect consumers from the risk of overinvestment or premature investment.

Further, in the Final 2024 ISP, five new transmission projects have been listed as actionable. These were not included in the Draft ISP, or subject to the consultation processes in the preparation of the Transmission Expansion Options Report. Thus, the ODP is indeed capable of being changed, including through stakeholder consultation (e.g. with TNSPs) between the publication of a Draft ISP and Final ISP.

There is asymmetry in the way that consultation on a Draft ISP is considered to be capable of varying the ODP. The AEMC considers removal of projects previously assessed as actionable sufficiently unlikely as to obviate the need for consultation, whereas it is apparently acceptable for projects never previously assessed to be added without consultation. This draft rule appears to extend this pattern of preference for increasing and accelerating investment in transmission.

Early works have already demonstrated consumer risk. For example, page 9 of TransGrid’s HumeLink Stage 2 Contingent Project Application states:

“Our contractual arrangements with our D&C contractors require us to execute the contract by July 2024. We will incur significant penalties under the contract for every day the agreement is delayed beyond this date. Receiving the AER’s Decision by 29 March 2024 is the latest possible date to enable us to finalise matters, including our funding arrangements, to meet the July 2024 contract execution timeframe. This contractual arrangement reflects the timing we have imposed on our D&C

contractors to construct the Project to meet the July 2026 delivery date and lock in contract terms early to avoid cost escalation.”

TransGrid uses the cost of delaying execution of design and construction contracts previously locked in during early works to argue for expedited AER approval of HumeLink. This exemplifies the risk to consumers that TNSPs will lock in significant contracts as part of ‘early works’ to later argue for the project being expedited to avoid cost escalations, even if the project may not end up being needed as soon as originally indicated, or even at all.

With five new actionable projects being listed in the Final 2024 ISP, outside any consultation as part of the Draft ISP, this draft rule will allow substantial funding for early works to be granted without any of the previous tests of economic benefit being applied, such as the PADR or PACR as part of the RIT-T.

On page 8 of the final determination for the *Improving the workability of the feedback loop*, the AEMC argued that the existence of economic testing and consultation through the PACR, which “responds to matters raised in submissions”, provides an additional important safeguard to consumers. The AEMC used this reasoning to justify the removal of consultation required between a Draft and Final ISP for issuance of the feedback loop. However, these pre-requisite steps intended as safeguards are now also being averted. This is a substantial erosion of transparency, and a dramatic acceleration of investment, that cannot be presumed to be in the best interest of consumers.

AEMC Review of ISP

The AEMC’s review of the ISP should not be delayed for two years. This is because the Commonwealth review is insufficient to ensure consumers’ long-term interests are being protected, and the ISP in its current form does not serve the long-term interests of consumers.

The terms of reference for the Commonwealth review state “the Energy and Climate Ministerial Council will approve the interim and final report and recommendations.” It is unclear to what extent the recommendations were shaped by political objectives, as energy ministers are not bound to consider the long-term interests of consumers in the same way the AEMC is. The AEMC should therefore conduct its own review without delay.

This is especially important, considering the ISP in its current form is not primarily serving the long-term interests of consumers. As Merryn York, Executive General Manager System Design at AEMO, stated in the 2024 ISP post-publication webinar on the topic of government policies included in all scenarios of the ISP:

“...we do have a limit on the range of things that we can model and the scenarios are very much focused on what is needed to happen to deliver on those policies.”

The ISP currently includes policies such as the ‘82% renewables by 2030’ target in all scenarios with no assessment of the impact on consumers. The reasons for excluding scenarios free of these policy constraints, and excluding an assessment of the costs to consumers arising from these policy constraints relies on a misinterpretation of the NER.

Specifically, AEMO has misinterpreted NER 5.22.3 (b). It states AEMO “must consider emissions reduction targets stated in the targets statement”. AEMO believes “must consider” means excluding alternative outcomes to government policies in ISP scenarios.

This misinterpretation fails to protect consumers, as any government policy — no matter how costly or ineffective — becomes a binding constraint on all scenarios of the model, directly impacting the ODP. The result is an ODP that includes projects that do not deliver cost savings for consumers and are merely recommended because they help a government meet its target (regardless of how costly or unachievable the target may be).

The Consumer Panel shares our concerns over the way the ISP currently includes government policies. As stated on page 7 of their report for the Draft 2024 ISP:

“We would suggest that the more governments (National and Jurisdictions) realise the difficulties of achieving their 2030 objectives, the greater the policy intervention and the less consumers are able to transparently see that the ISP is indeed an optimal development path from a consumer perspective with particular respect to the NEO.”

This issue was not addressed by the Commonwealth review. The recommendations on government policies were concerned only with promoting transparency around the consultation process with jurisdictions and clarifying how policies are included. There were no recommendations dealing with the issues of *cost* transparency for policies. An AEMC review needs to be implemented under the NER’s current 2025 timeline to ensure this issue is resolved for the 2026 ISP.

The Consumer Panel further expressed concern on page 6 that “many consumers will not be able to ‘afford’ the costs described in the Draft ISP...” The Final 2024 ISP makes five additional projects actionable under the ODP compared to the Draft, making the question of affordability even more important.

The proponents of these additional projects can benefit from recovering costs sooner for early works under the draft rule, without consumers being consulted on their inclusion in the ODP. As Samantha Christie, Manager Strategic Planning at AEMO, stated in the 2024 ISP

post-publication webinar, AEMO has “undertaken close joint planning with transmission network service providers” for these changes to the ODP. This same level of consultation was not afforded to consumers prior to projects being deemed actionable in the Final ISP.

Consumers need to have confidence AEMO is taking into account their long-term interests, and not solely the interests and views of TNSPs, in the selection of projects for the final ODP. An AEMC review is therefore greatly needed to promote trust and transparency in the ISP consultation process and the resulting ODP.

It is crucial that the AEMC protects the long-term interests of consumers by conducting a review by 1 July 2025, as stated in the current NER, with a particular focus on the costs to consumers of projects in the ODP and government policies.