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Australian Energy Market Commission
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National Electricity Amendment (Replacement Expenditure Planning Arrangements) Rule 2016, Draft Rule Determination, 11 April 2017

Jemena Electricity Networks Vic Ltd (**JEN**) welcomes the opportunity to respond to the draft rule change – Replacement expenditure planning arrangements (**draft rule**).

The Energy Networks Association (**ENA**) has consulted JEN on the issues presented in the draft rule determination and we support ENA's submission to this draft rule.

The Australian Energy Market Commission (**AEMC**) has made a draft rule to increase the transparency of electricity network service provider (**NSP**) decisions on investment in network assets. The draft rule makes a number of amendments to the existing planning and investment framework in the National Electricity Rules (**NER**).

The draft rule:

- extends the regulatory investment test (**RIT**) to include replacement capital expenditure
- stipulates that the existing regulatory investment test —currently applied to augmentation projects—will apply to replacement capital expenditure
- retains the threshold investment test amount at the current levels of $5 million for distribution investments
- requires that annual planning reports must include information on:
    - retirement information for all network assets
    - de-rating information for those network asset de-ratings that cause a network constraint
    - investments in information technology and communications systems related to the management of network assets.

JEN supports the draft rule as it promotes greater transparency on network asset retirement, de-rating and replacement decisions. However we have concerns with the proposed transitional arrangements and the $100,000 threshold for grouping of replacement assets for the purposes of annual planning reports.

Threshold for grouping of replacement assets in the Annual Planning Reports

In setting reporting requirement there is a trade-off between the administrative costs of developing the annual planning reports and the benefits of greater transparency on network asset retirement, de-rating and replacement decisions . The AEMC has recognised this in its draft rule and considered practical cost thresholds to minimise the administrative costs of reporting.

To reduce the reporting burden, the draft rule allows a NSP to report assets together where:

- assets of the same type are to be replaced across more than one location in the same calendar year; and
- the replacement cost of each individual asset is expected to have a capital cost of $100,000 or less.

Whilst the $100,000 threshold appears to provide a practical balance between the benefit of reporting and compliance costs—at a teleconference of ENA members—a majority of members assessed the threshold to be still onerous on them.

JEN suggests the threshold should be increased to $200,000. A higher threshold would strike the right balance. It would still inform non-network solution providers of the type of assets forecast for replacement by area in a practical and meaningful way, without the annual planning reports becoming unwieldy by having too much information on individual replacement assets. Non-network solution providers who require detailed information of asset replacements in a particular area will be able to get the information by contacting the relevant NSP.

Annual Planning Reports

The draft rule requires that annual planning reports will need to include additional information on retirement of all network assets; network asset de-ratings that cause a network constraint in network; and investments in information technology and communications systems related to the management of network assets.

JEN generally develops the distribution annual planning reports (**DAPR**) by October of each year. Management approval of the DAPR takes place in November and the report finalised and published in December. The final rule is expected to be published in July 2017, this gives JEN less than four months to comply with the new reporting requirements in the first year. This timeframe does not give JEN sufficient time to develop the changes to systems and processes necessary to comply with the rule change, particularly in the first year of reporting. JEN suggests the new reporting requirements on network assets and asset de-ratings be included in the 2018 DAPR.

Transitional arrangements

The draft rule determination acknowledges that NSPs will require some time to prepare for the introduction of the draft rule requirements and the Australian Energy Regulator (**AER**) will also be required to review and update its RIT guidelines. Accordingly, the draft rule determination proposes transitional arrangements requiring:

- the new annual planning report requirements are to apply for the next scheduled annual planning reports—for DNSPs the commencement date is 31 December 2017
- the new RIT requirements are to apply from 1 July 2018

- replacement projects committed by 1 July 2018 will not be required to be assessed under the RIT
- replacement projects that become committed projects after 1 July 2018 will be required to be assessed under the RIT
- the annual planning reports will be used to identify whether a project is committed prior to 1 July 2018.

However, in recent correspondence to the ENA,[1] the AEMC is seeking feedback on bringing forward the commencement date of the provision requiring application of the RIT to replacement expenditures from 1 July 2018 to 13 September 2017 and requiring NSPs to publish by 18 August 2017 a list of "excluded projects" as at 18 July 2017. Any projects that are not "excluded" on 18 July will be subject to the RIT process.

JEN has significant concerns if the application of the RIT to replacement expenditures is brought forward

The AEMC proposes to define an "excluded project" in the NER using the *committed project* definition clauses (b) and (d) in the AER's RIT guidelines:

- Clause (b) – construction has either commenced or a commencement date has been set (and/or)

- Clause (d) – contracts for supply and construction of the major components of the necessary plant and equipment have been finalised and executed, including any provisions for cancellation payments.

The AEMC cites the reason for bringing forward the commencement date of the new RIT rule is because some stakeholders have raised concerns about the delay in the new rules applying and the potential for NSPs to commit to projects after the rule is published to avoid having to undertake a RIT for replacement expenditures.

Impacts on JEN

JEN notes that it is not practical to execute contracts for supply and construction and set construction dates by 18 July 2017 for our major network replacement projects in order to meet the AEMC's proposed "excluded projects" deadline.

When applying this new framework in JEN's case, bringing forward the rule commencement date will cause delay to the completion of four major network asset replacement projects. All four projects are identified in JEN's 2016 DAPR. The project will be delayed by the time taken to undertake the RIT, which is estimated to be approximately 6 to 12 months. If these projects are delayed due to the RIT, JEN will not be able to maintain acceptable levels of network safety and supply reliability, as this will increase the risk and exposure to equipment failure resulting in loss of supply to large number of our customers.

The business cases for these four projects are scheduled to be approved in the second half of 2017 and become *committed project*. JEN's business cases for capital expenditures greater than $5 million undergoes an extensive governance process.

[1] Email from AEMC to Energy Networks Australia, 31 May 2017.

JEN proposes an alternative and preferable method for transitioning to the new rules

To address the concern that NSPs may seek to avoid having to undertake a RIT under the transition arrangement in the draft rule determination, the arrangement could be strengthened by including an additional requirement that the “excluded projects” must be those replacement projects that are *committed projects* by 1 July 2018 and are already published in the NSP’s 2016 annual planning report. This additional provision would prevent the potential for NSPs to commit to projects after the rule is published to avoid having to undertake a RIT.

Our suggestion avoids the need to change the transitional arrangement in the draft rule determination for the application of the RIT to replacement expenditures and does not increase the risk and exposure to equipment failures. Additionally, under our preferred method for transitioning to the new rules, the AER’s consultation process to update the RIT guidelines does not have to be rushed through by 12 September 2017.

If you have questions in relation to the submission, please contact Siva Moorthy on (03) 9173 8774 or at siva.moorthy@jemena.com.au.

Yours sincerely

[signed]

Matthew Serpell
Manager Asset Regulation and Strategy