



Australian Energy Market Commission

Draft Rule Determination

**National Electricity Amendment (Regulatory
Test Thresholds and Information Disclosure
on Network Replacements) Rule 2008**

Rule Proponent
Grid Australia

31 July 2008

Signed:

John Tamblyn
Chairman

For and on behalf of
Australian Energy Market Commission

Commissioners
Tamblyn
Woodward

Inquiries

The Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

E: aemc@aemc.gov.au

T: (02) 8296 7800

F: (02) 8296 7899

Citation

AEMC 2008, *Regulatory Test Thresholds and Information Disclosure on Network Replacements*, Draft Rule Determination, 3 July 2008, Sydney

About the AEMC

The Council of Australian Governments, through its Ministerial Council on Energy, established the Australian Energy Market Commission (AEMC) in July 2005 to be the Rule maker for national energy markets. The AEMC is currently responsible for Rules and policy advice covering the National Electricity Market. It is a statutory authority. Our key responsibilities are to consider Rule change proposals, conduct energy market reviews and provide policy advice to the Ministerial Council as requested, or on AEMC initiative.

This work is copyright. The Copyright Act 1968 permits fair dealing for study, research, news reporting, criticism and review. Selected passages, tables or diagrams may be reproduced for such purposes provided acknowledgement of the source is included.

Contents

Abbreviations	v
Summary	vi
Summary of the Rule change proposal	vi
First Round Consultation	vi
The Commission's Decision	vii
The Commission's reasoning for its decisions	vii
Consultation on the draft Rule determination and draft Rule	viii
1 Grid Australia's Rule proposal	1
1.1 Summary of the Rule change proposal	1
1.2 Context and background	2
1.3 Links with other Projects	3
1.4 Consultation on the Rule proposal	4
1.5 Extension of time to publish draft Rule determination	5
1.6 Further Extension of time to publish draft Rule determination	5
2 Commission's Assessment of the Rule Change Proposal	7
2.1 Methodology for developing the draft Rule determination	7
2.2 The Commission's power to make a Rule	7
2.3 Assessment of the Draft Rule: the Rule making test, the national electricity objective and MCE statements of policy principles	8
2.4 Grid Australia's assessment of how its Rule change proposal satisfies the National Electricity Objective	8
2.5 The Commissions Assessment of the National Electricity Objective	9
2.6 Commission's Determination	15
2.7 Differences between proposed Rule and draft Rule	16
A Commission's analysis of the Proposed Rule	17
A.1 Regulatory Test asset thresholds	17
A.2 Information disclosure for network replacements	26
A.3 Information disclosure for network replacements - Special arrangements for Victoria	28
A.4 Indexation of the threshold values	29
B Current Regulatory Test Processes for Thresholds	33

C	Indexation Percentage Increases from Inception of Threshold Values to Present.....	35
D	Information Provided in Annual Planning Reports (APRs) — Clause 5.6.2A(b)(4) and 5.6.2.A(b)(5)	37

Abbreviations

ACCC	Australian Competition and Consumer Commission
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
APR	Annual Planning Report
Commission	see AEMC
CPI	Consumer Price Index
DRP	Draft Statement of Principles for the Regulation of Transmission Revenue (May 1999)
Draft SRP	Draft Statement of Principles for the Regulation of Electricity Transmission Revenues (August 2004)
ERAA	Electricity Retailers Association of Australia
ETNOF	Electricity Network Owners Forum (now referred to as Grid Australia)
kV	Kilovolt
MCE	Ministerial Council on Energy
MNSP	Market Network Service Provider
NEL	National Electricity Law
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company
NEO	National Electricity Objective
PPI	Producer Price Index
RIT-T	Regulatory Investment Test for Transmission
Rules	National Electricity Rules
TNSP	Transmission Network Service Provider

Summary

Summary of the Rule change proposal

On 21 November 2007 the Commission received a Rule change proposal from the members of the Electricity Transmission Network Owners Forum (ETNOF). ETNOF are now referred to as Grid Australia. The Rule change proposal was in relation to augmentation asset thresholds under the regulatory test, and information disclosure requirements for network replacements. While the regulatory test currently applies to transmission and distribution augmentations, this Rule change proposal only applies to transmission augmentation thresholds and replacements. The appropriate thresholds for distribution have not been considered. The main elements of the Rule change proposal are:

- To increase the current regulatory test thresholds applying to new small transmission network assets from \$1 million to \$5 million and new large transmission network assets from \$10 million to \$35 million;
- Index the regulatory test's monetary thresholds to movements in the Producer Price Index (PPI); and
- Require Transmission Network Service Providers (TNSPs) to disclose certain information on all proposed replacement network assets in excess of \$5 million in their Annual Planning Reports (APRs).

Grid Australia states that the Rule proposal will:

- Reduce the allocation of funds towards unnecessary regulatory test assessment, consultation, and information disclosure thus providing for a more efficient planning process; and
- Increase the responsiveness of TNSPs in relation to consumers needs for network augmentation projects.

First Round Consultation

The Commission published the Rule change proposal in accordance with section 95 of the National Electricity Law (NEL) and consultation closed on 20 December 2007. Seven first round submission were received including a supplementary submission from Grid Australia. The submissions from Hydro Tasmania, the NGF and Energex displayed various degrees of support for the Rule change proposal. The submissions from VENCORP, the Energy Retailers Association of Australia (ERAA) and TRUenergy were not supportive of the Rule change proposal. Grid Australia made a supplementary submission that clarified and provided further information to support its Rule change proposal.

The Commission's Decision

The Commission is satisfied that the draft Rule is likely to promote the National Electricity Objective (NEO)^a, and that it satisfies the Rule making test. For this reason, the Commission has determined to make this draft Rule determination and accompanying draft Rule with some key modifications and enhancements under section 99 of the NEL.

The Commission's reasoning for its decisions

The Commission considers that in assessing the Rule change proposal that it needs to find the appropriate balance between the level of regulatory scrutiny applied to augmentation projects to promote efficient market outcomes and providing the appropriate regulatory burden on TNSPs in respect of those projects. In this regard the Commission seeks to provide for the best regulatory practice result.

In this draft Rule determination, the Commission has generally accepted Grid Australia's proposed Rule change. As a result of submissions received, the Commission's analysis, and a review of the wording of the proposed Rule, however, the Commission has made a number of drafting amendments and made modifications on some specific matters of the proposed Rule that have operational implications.

The Commission proposes to:

- Increase the new small transmission network asset threshold from \$1 million to \$ 5 million;
- Provide for information disclosure on network replacements over \$5 million; and
- Provided a mechanism to maintain the threshold values over time.

The key modifications proposed by the Commission are:

- Raising the new large transmission network asset threshold from \$10 million to \$20 million (and not \$ 35 million as proposed in the Rule change proposal);
- Providing for a three yearly review of threshold values to be conducted by the AER (and not automatic annual indexation as proposed in the Rule change proposal);

^a When this Rule change proposal was submitted the National Electricity Objective was known as the National Electricity Market objective (NEM objective). The NEM objective became the National Electricity Objective on 1 January 2008. There are no substantive differences besides the change in name from the NEM objective to the National Electricity Objective

- Removing the ability of the AER to change the amount of the asset thresholds that is provided for in the definitions of new small transmission network asset and new large transmission network asset;
- Additional information to be provided in regards to replacement transmission assets including: the purpose of the proposed new replacement transmission asset; a list of alternative projects to the proposed new replacement transmission asset; and the TNSPs estimated total capitalised expenditure on the proposed new replacement transmission asset;
- Provision for VENCORP to publish the replacement transmission asset information in the Victorian APR and for SP AusNet to provide the relevant information by 28 February each year; and
- Clarifying the meaning of the term “replacement network asset”.

This draft Rule determination sets out the reasons of the Commission in accordance with the requirements of the NEL and sets out the Commission’s assessment in relation to the above proposed changes. The draft Rule, which has been made in accordance with this assessment is attached.

Consultation on the draft Rule determination and draft Rule

The Commission invites submissions on this draft Rule determination by 15 September 2008. The Commission has elected to consult on this Rule change proposal for 6 weeks in accordance with statutory timeframes.

In accordance with section 101 of the NEL, any interested person or body may request that the Commission hold a hearing in relation to the draft Rule and draft Rule determination. Any request must be received no later than 7 August 2008

Send submissions electronically to submissions@aemc.gov.au

Or mail to:

Australian Energy Market Commission

PO Box H166

AUSTRALIA SQUARE NSW 1215

1 Grid Australia's Rule proposal

1.1 Summary of the Rule change proposal

On 21 November 2007 the Commission received a Rule change proposal from the members of ETNOF who are now known as Grid Australia¹.

1.1.1 Increasing asset thresholds

Firstly Grid Australia proposes that the current thresholds applying to new transmission network augmentations under the Rules be amended as follows:

- The new small transmission network asset threshold be increased from \$1 million to \$5 million; and
- The new large transmission network asset threshold be increased from \$10 million to \$35 million.

The effects of the Rule change proposal are that projects that no longer fall into the small asset threshold will not be required to be assessed under the regulatory test. Also the regulatory test information will no longer be required to be disclosed to the market. There are still however information disclosure requirements specified in clause 5.6.2A for all augmentation assets. For projects that drop out of the new large asset threshold and into the new small asset threshold the effect is that there will be no separate individual public consultation in respect to those projects and no mechanism for dispute resolution. However the extent of the information is the same in the APRs an application notices.

Currently the regulatory test applies to transmission and distribution augmentations and currently the new small and large distribution network asset thresholds are identical. This Rule change proposal however proposes to only raise the new and small transmission network assets and make no change to the distribution asset thresholds. The Commission has not considered an increase to the asset thresholds for distribution in analysing this Rule change proposal.

1.1.2 Indexation of asset thresholds

Grid Australia proposes that the Regulatory Test thresholds be indexed over time by an appropriate escalator so that the monetary thresholds are maintained over time. Grid Australia proposes the PPI released by the Australian Bureau of Statistics be the escalator, as it considers this to better reflect the general movement in the prices facing the construction sector than the Consumer Price index (CPI).

¹ The members of Grid Australia are: Electranet Pty Ltd, Powerlink Queensland, SP AusNet, Transend Networks Pty Ltd and Transgrid.

1.1.3 Information disclosure on network replacements

Grid Australia proposes TNSPs be required to disclose certain information on replacement projects in excess of \$5 million in their respective APR's. Grid Australia proposes that the information to be disclosed in the APR's be:

- A brief description of the project; and
- The planned commissioning date.

Currently there are information disclosure requirements for all network augmentations only. There are no information disclosure requirements applicable to network replacements.

Grid Australia also proposes that the replacement asset threshold be indexed.

1.1.4 Problems to be addressed by Rule change

Grid Australia states:

- that the current monetary thresholds in the Regulatory Test were established in 2001 as part of the Network and Distributed Resources Code changes. At that time, some TNSPs expressed concern that the thresholds for small and large transmission network assets were set too low, and that those TNSPs considered that more appropriate thresholds would be of the order of \$7-25 million for new small network assets and above \$25 million for new large network assets. The rule-maker at the time however decided to take a conservative stance in setting the threshold values to the present figures as the arrangements were still new; and
- that since 2001, there have been substantial increases in the input cost of materials used in transmission assets (eg steel, aluminium, copper) and labour costs.

Grid Australia therefore believes that the asset thresholds need to be increased to more realistic levels. This would provide for more efficient allocation of resources as less resources would be required to produce assessment and consultation documentation. Furthermore the time taken to approve simple transmission augmentations would be improved providing a benefit for consumers.

1.2 Context and background

The Australian Competition and Consumer Commission made a determination on 13 February 2002 to incorporate the threshold levels in its Networks and Distributed Resources Determination². The threshold levels were set at \$1 million for the new small transmission network asset and \$10 million for the new large transmission

² ACCC, Applications for Authorisation - Amendments to the National Electricity Code Network and Distributed Resources, 13 February 2002.

network asset³. Grid Australia's main proposal is for these threshold levels to be changed to \$5 million dollars (for the small asset threshold) and \$35 million for the large asset threshold).

The Commission commented on the issue of the large asset threshold in its Transmission Network Replacement and Reconfiguration Rule change proposal. In its draft Rule determination the Commission considered a threshold of \$ 35 million (being the midway point of a range between \$20 million and \$50 million)⁴. These comments however were made in the context of broadening the application of the regulatory test to large network replacements and that in its final determination the Commission decided that, on the basis of submissions received, it was not clear that such a proposal would promote the NEO⁵.

Grid Australia notes the Commission's comments in its Rule change proposal and considers those deliberations of the Commission to be a realistic reflection of today's construction costs for significant augmentations.

1.3 Links with other Projects

1.3.1 National Transmission Planner Review

As part of the National Transmission Planner Review, the Commission was requested by the Ministerial Council on Energy (MCE) to make recommendations for a new project assessment and consultation process for transmission to replace the current regulatory test with respect to transmission projects. The Commission's recommendations were provided to the MCE on 30 June 2008 and were published on 22 July 2008.⁶

For the new transmission assessment process (called the Regulatory Investment Test for Transmission (RIT-T), the Commission has recommended having one single threshold of \$5m. Proposed transmission projects which have an economic and technically feasible option costing more than \$5m, will be required to undertake a RIT-T assessment. The proposed RIT-T also contains an objective framework which enables the extent of assessment and consultation to be tailored to the specific impact and materiality of the proposed project.

The proposed RIT-T has been developed to implement the objectives set out by Council of Australian Governments (COAG) in its response to the Energy Reform Implementation Group. Therefore given the amalgamation of the reliability and market benefits limbs, and the increased focus on assessing national benefits, the proposed RIT-T will be a significantly different test to the current regulatory test.

³ ACCC, Applications for Authorisation – Amendments to the National Electricity Code Network and Distributed Resources, 13 February 2002.

⁴ AEMC, Draft National Electricity Amendment (Transmission Network Replacement and Reconfiguration) Rule 2006, 26 October 2006, p18.

⁵ AEMC, Transmission Network Replacement and Reconfiguration Rule determination, 1 March 2007.

⁶ AEMC, National Transmission Planning Arrangements, Final Report to MCE, 30 June 2008

The Commission's determination on the appropriate threshold for the RIT-T has been developed in this context.

The Commission views the consideration of the appropriate thresholds for this Rule determination to be separate and distinct given that the differences in the assessment methodology and consultation process between the current test and proposed RIT-T.

The MCE is currently considering the proposed RIT-T. The Commission has recommended that the proposed RIT-T be implemented through the fast tracked Rule change process and that the AER is allowed 12 months from the commencement of the new rules, to develop the new RIT-T. The determination for this proposed Rule will be take effect until the introduction of the RIT-T.

1.3.2 Review of Demand Side Participation in the NEM

The Commission has initiated a review to investigate if the Rules are limiting the efficient involvement of the demand-side in the NEM. On 16 May 2008 the Commission published an issues paper seeking stakeholder comment on a range of identified issues⁷. One of the identified issues was whether the Regulatory Test thresholds may be limiting the ability for alternatives to smaller network augmentations to be considered. Submissions to the issues paper closed on 20 June 2008. A draft report is due to be published in September 2008 followed by a final report to be published in December 2008.

1.4 Consultation on the Rule proposal

On 20 December 2007 the Commission commenced consultation under section 95 of the NEL on the proposal. Consultation closed on 15 February 2008. The Commission received seven submissions to the proposal including a supplementary submission from Grid Australia. Submissions were received from the following parties:

- Grid Australia;
- VENCORP;
- Energy Retailers Association of Australia (ERAA);
- TRUenergy;
- Hydro Tasmania;
- National Generators Forum (NGF); and
- Energex.

⁷ AEMC, Review of Demand-Side Participation in the National Electricity Market Stage 2: Issues Paper, 16 May 2008.

The submissions from Hydro Tasmania, the NGF and Energex displayed various degrees of support for the Rule change proposal. The submissions from VENCORP, the ERAA and TRUenergy were not supportive of the Rule change proposal. Grid Australia made a supplementary submission that clarified and provided further information to support its Rule change proposal.

1.5 Extension of time to publish draft Rule determination

On 3 April 2008 the Commission published a notice under section 107 of the NEL to extend the publication of the draft Rule determination for 10 weeks to 3 July 2008. The Commission considered it necessary to extend the publication of the draft Rule determination in order to sufficiently analyse and address complex issues necessary to finalise it. The complex issues included the establishment of appropriate threshold values and further analysis into automatic indexation.

1.6 Further Extension of time to publish draft Rule determination

On 26 June 2008 the Commission published a further notice under section 107 of the NEL to extend the publication of the draft Rule determination in order to sufficiently analyse and address complex issues necessary to finalise the draft Rule determination. The Commission made this decision to analyse information it recently received⁸ to assist it in formulating views in relation to whether or not to increase the Regulatory Test thresholds.

⁸ This information was requested from Grid Australia and VENCORP by the Commission and was provided on a confidential basis. The information has been treated in accordance with the Commissions guidelines on submissions.

This page has been intentionally left blank

2 Commission's Assessment of the Rule Change Proposal

This section of the draft Rule determination provides the assessment framework by which the Commission has assessed the Rule change proposal, the Commission's assessment of the Rule change proposal against the NEO⁹ and reasons for its decision in section 2.5 below. Further analysis of its reasoning is provided in Appendix A to this draft Rule determination.

2.1 Methodology for developing the draft Rule determination

The Commission has determined in accordance with section 99 of the NEL to make with amendments and modifications, a draft Rule. A list of the key modifications and amendments to the draft Rule from the proposed Rule is included in section 2.6 below. A draft of the Rule to be made which is different to the proposed Rule put forward by the proponent, is attached to this determination.

This draft Rule determination sets out the Commission's reasons for making the draft Rule. The Commission has taken into account:

1. The Commission's powers under the NEL to make the Rule;
2. The proponent's Rule change proposal and proposed Rule;
3. Submissions received;
4. Relevant MCE statements of policy principles; and
5. The Commission's analysis as to the way(s) in which the draft Rule will or is likely to contribute to the achievement of the NEO¹⁰ so that it satisfies the statutory Rule making test.

2.2 The Commission's power to make a Rule

The Commission is satisfied that the Draft Rule falls within the subject matters for which the Commission may make Rules, as set out in section 34 of the NEL and in Schedule 1 to the NEL.

The draft Rule relates specifically to section 34(1) of the NEL, which states that:

"...the AEMC, in accordance with this Law and the Regulations, may make Rules, to be known, collectively, as the "National Electricity Rules", for or with respect to-

(a) regulating -

...

⁹ Formerly known as the National Electricity Market objective.

¹⁰ Ibid

- (iii) the activities of persons (including Registered Participants) participating in the national electricity market or involved in the operation of the national electricity system;”

The Draft Rule also falls under the following subject matter items under Schedule 1 to the NEL, namely:

item 12. the augmentation or expansion in the capacity of transmission systems and distribution systems; and

item 23. incentives for regulated transmission system operators to make efficient operating and investment decisions.

2.3 Assessment of the Draft Rule: the Rule making test, the national electricity objective and MCE statements of policy principles

The Rule making test requires the Commission to be satisfied that a Rule that it proposes to make will contribute to the NEO¹¹.

The test requires the Commission to consider the implications of the proposed new Rule, for efficient investment in, and efficient operation and use of, electricity services, in respect of:

- (a) price, quality, reliability and security of supply of electricity; and
- (b) the reliability, safety and security of the NEM;

which impact on the long term interests of end users of electricity.

The NEL requires the Commission to have regard to any MCE statements of policy principles in applying the Rule making test. The Commission notes that currently there are no MCE statements of policy principles that currently relate to Regulatory Test thresholds or information disclosure on network replacements.

2.4 Grid Australia’s assessment of how its Rule change proposal satisfies the National Electricity Objective

Grid Australia states that raising the asset thresholds under the Regulatory Test contributes to the NEO¹² by promoting efficient investment in electricity transmission networks.

Grid Australia states:

- that Market Participants and other stakeholders have shown negligible response to consultations on small network assets identified in the APR, with TNSPs having received only a single submission over the last six years. On

¹¹ Formerly known as the National Electricity Market objective.

¹² Ibid

the balance, it considers that the cost of continuing to provide such information for investments within the current new small network asset range outweighs the benefit to the market and is therefore inefficient.

- That TNSPs incur relatively significant resource and administrative costs in complying with the Regulatory Test and the formal consultation processes described in the Rules for new large network assets. The inefficient allocation of a TNSP's resources to produce relevant documents and undertake requisite consultations with stakeholders detracts from achievement of the NEO¹³ by adding undue cost to transmission investments. These costs are ultimately passed on to electricity consumers.

Grid Australia states that raising the large network asset threshold to \$35 million:

- will allow TNSPs and potential non-network solution proponents in particular, to focus their efforts on regulatory test assessments that are likely to generate genuine non-network options;
- the consequential reduction in regulatory burden upon TNSPs as a result of not being required to apply the extended regulatory test consultation process to future new large network assets below \$35 million will improve the efficiency of the consultation and approval process. Grid Australia states that it will also promote timely decision-making on network investments to enhance the reliability, safety and security of electricity supply. Grid Australia states that such an outcome is considered to be in the long term interests of consumers.

Grid Australia states that raising the asset thresholds provides both an efficient and practical approach to meeting the NEO¹⁴ as TNSP resources could be better utilised if diverted away from the production of information and analysis which provides little or no value to the market, toward those which do.

2.5 The Commissions Assessment of the National Electricity Objective

In assessing this Rule change proposal against the NEO¹⁵ the Commission considers that the key question is balancing the amount of regulatory scrutiny applied to augmentation projects to promote efficient market outcomes and providing the appropriate regulatory burden on TNSPs in relation to those projects.

In assessing the costs and benefits of the proposal the Commission needs to consider whether the requirement for the tools of regulatory scrutiny (including information disclosure, public consultation, a test for economic efficiency of projects and dispute resolution) need to be balanced by the regulatory burden, (including costs to TNSPs, necessity of the information and the efficient allocation of resources). Promoting

¹³ Formerly the National Electricity Market objective

¹⁴ Ibid

¹⁵ Ibid

timely investment and preventing unnecessary delays are also factors that the Commission considers are important in assessing this proposal.

The Commission must seek to achieve the best regulatory practice in considering these factors for the different threshold levels of augmentation projects.

Grid Australia's Rule change proposal has four main elements:

- Increasing the new small transmission network asset threshold;
- Increasing the new large transmission network asset threshold;
- Providing for information disclosure on network replacements; and
- Providing for threshold values to be maintained over time.

The Commission has assessed these elements of the Rule change proposal in respect of transmission only. While some of the issues of this Rule change proposal are applicable to distribution as well as transmission the Commission considers the assessment and applicability of these issues in relation to distribution to be a separate matter requiring separate analysis. The Commission therefore considers the applicability of the elements of this Rule change proposal to distribution to be out of scope of this Rule change proposal.

2.5.1 Commission's consideration of thresholds generally

In assessing the regulatory test asset thresholds for transmission the Commission has examined the following information (see Appendix A for further detail):

- Input cost information (see Appendix C Part 3.1.5);
- Information on the cost of undertaking the regulatory test compared to the capital costs of projects¹⁶ ;
- Examination of APRs and application notices to ascertain the number of projects that fall within relevant cost bands and to assist in understanding the level of information; and
- Historical information including the relevant ACCC decision that incorporated the thresholds in the National Electricity Code (now the Rules)¹⁷.

¹⁶ This information was requested by the Commission and provided to the Commission on a confidential basis and has therefore been treated in accordance with the Commission's "Guidelines for making Written Submissions on Rule Change proposals". The guidelines state that the Commission considers that where submissions (or parts of submissions) are treated as confidential, they cannot be tested and subjected to the full scrutiny that the public consultation process allows. The Commission takes this lack of public scrutiny into account in the appropriate weight to be attributed to confidential information contained in a submission.

The Commission notes that input costs have increased since the inception of the thresholds. Appendix C shows that the input cost increases from the various indices from 2002 to the present are: 36% for the general construction PPI; 64% for the power transformer PPI; 102% for the distribution transformer PPI; 20% for the electricity supply PPI and 16% for the CPI. This means that projects that were originally not intended to be captured by the threshold are now being captured by the thresholds as the threshold values have remained constant over time. This consequently would increase the regulatory burden on TNSPs and result in an increase in costs, the time taken to approve investments and the requirement for the extra allocation of resources to address the regulatory burden. The results are inefficiencies in the regulatory process.

Submissions to the Rule change proposal however have commented that regulatory scrutiny on regulated businesses increases their transparency in terms of their expenditure and in the network planning process¹⁸. The Commission considers however that this should be balanced against the cost of that regulatory scrutiny to achieve regulatory best practice. The Commission also notes that some submissions have also commented that the thresholds should be increased¹⁹.

The Commission considers that arrangements should reflect good regulatory practice. This means that it is important that the process does not result in unjustified cost and use of resources. The regulatory process imposes a cost and that should be proportionate to the size and effect of the project. The inflation in input costs has caused an unintended shift in the relationship between the regulatory process and the impact of the project which was established by the ACCC in 2002²⁰.

The Commission therefore considers that based on the evidence presented in its analysis that it would promote the NEO²¹ to increase the regulatory test threshold values with respect to transmission network augmentations. The Commission considers that there is no exact science to determining the appropriate thresholds. Instead it is a matter of judgement and ensuring that the appropriate balance is achieved between regulatory scrutiny and transparency for the different levels of projects. This assessment will be undertaken for the two threshold levels below.

2.5.2 Increasing New Small Transmission Network Asset Threshold

The Commission has determined that the asset thresholds are to be increased. This section shows the Commission's reasoning for the amount that the new small transmission network asset threshold should be increased to.

¹⁷ ACCC, Applications for Authorisation – Amendments to the National Electricity Code Network and Distributed Resources, 13 February 2002.

¹⁸ VENCorp submission, pp 1-2, ERAA submission pp1-2, TRUenergy Submission pp1-2.

¹⁹ HydroTasmania submission, p1, NGF submission, p1, Energex submission pp1.

²⁰ ACCC, Applications for Authorisation – Amendments to the National Electricity Code Network and Distributed Resources, 13 February 2002.

²¹ Formerly the National Electricity Market objective.

In considering the quantum of the threshold the Commission has to consider the best regulatory practice threshold amount. The Commission also has regard to the effects of increasing the small asset threshold. These are:

- Projects between \$1 million and \$5 million would now not be required to undertake the regulatory test assessment; and
- The information from undertaking the regulatory test would not be disclosed to the market because such projects are now not required to undertake the regulatory test assessment. Information on these projects is still required to be published under clause 5.6.2A of the Rules (See Appendix D).

The Commission has also ascertained that:

- The information not supplied to the market by raising the threshold was only the regulatory test assessment information , and that clause 5.6.2A of the Rules requires information to be disclosed regardless of the asset threshold (see appendix D);
- That in place of the regulatory test assessment, the Chapter 6A framework provides scrutiny on the economic efficiency of projects when TNSPs seek to obtain approval from the AER for their five year revenue determinations. This effectively provides regulatory scrutiny on TNSPs to minimise the cost of projects and therefore provides safeguards for projects of between \$1 million to under \$5 million;
- Information on the costs of undertaking the regulatory test against the capital cost of projects²² showed that the proportion of costs of undertaking the regulatory test was high in comparison to other project cost bands for the project cost band of \$1 million - \$5 million; and
- Input costs have increased. Appendix C shows that the input cost increases for the various indices from 2002 to the present are: 36% for the general construction PPI; 64% for the power transformer PPI; 102% for the distribution transformer PPI; 20% for the electricity supply PPI and 16% for the CPI

In light of this analysis the Commission has determined that the new small transmission network asset threshold should be increased to \$5 million. In setting this value the Commission has accepted Grid Australia's Rule change proposal. The Commission considers that this amount provides the appropriate balance between the level of regulatory scrutiny applied to augmentation assets and providing the appropriate regulatory burden on TNSPs in relation to projects. The Commission further notes that increasing the threshold value to \$5 million would ensure that simple minor projects are not unnecessarily delayed.

²² Information provided on a confidential basis

2.5.3 Increasing Large New Transmission Network Asset thresholds

The Commission considers that the question of how much to increase the large asset threshold is a separate question to the small asset threshold due to the different effects of increasing the large and small thresholds. The effects of increasing the large asset threshold are:

- That information disclosure will be through the APRs and not through application notices and requests for information which include public consultation; and
- There is no mechanism to dispute certain matters.

In determining an increased threshold value for the large asset threshold the Commission is required to balance on the one hand the fact that input costs have increased which has meant that assets that were not intended to be captured by this threshold are now captured, thus increasing the regulatory burden on and the administrative costs of TNSPs. On the other hand however the Commission considers that the regulatory scrutiny in terms of public consultation and the availability of dispute resolution is important for projects of a particular scale.

The Commission has therefore decided not to accept Grid Australia's proposal of raising the new large transmission network asset threshold to \$35 million but instead to raise the new large transmission network asset threshold to \$20 million.

The Commission considers that this figure reflects the increase in input costs and also provides the appropriate balance between the regulatory burden on TNSPs and ensuring the appropriate level of regulatory scrutiny to promote efficient market outcomes, and the timely delivery of transmission services to consumers. In providing for this increase the Commission notes that participants will still be able to provide comments to the TNSP on the proposed projects through responding to the information contained in the APRs. The increase will also provide for transmission investment to proceed in a timely manner and not be unnecessarily delayed.

2.5.4 Information Disclosure on Network Replacements

The Commission agrees with submissions²³ and the Rule proposal that additional information disclosure by TNSPs on network replacements over \$5 million increases the transparency of the planning process and the operation of regulated businesses. In this way information disclosure promotes the NEO²⁴.

The Commission has accepted Grid Australia's Rule change proposal but has made key modifications and enhancements to it. These include:

²³ ERAA submission p4, Energex submission pp 1-2, NGF submission p1.

²⁴ Formerly the National Electricity Market objective.

- Providing for additional information in regards to network replacements over \$5 million that are in accordance with the information currently required for all augmentations (whether they fit into an augmentation threshold or not);
- Clarifying the definition of network replacements in accordance with the policy intent of the proposal; and
- Providing that VENCORP publish the APRs for the Victorian jurisdiction and that SP AusNet provide the relevant information to VENCORP by 28 February each year. In amending the Victorian derogation the Commission has had regard to the matters set out in section 89 of the NEL and considers that this consequential amendment to the Victorian derogation is required.

The Commission considers that these modifications provide useful information to the market without imposing too onerous a burden on the TNSPs and therefore better promote the NEO than the proposed Rule.

2.5.5 Threshold values to be maintained over time

The Commission has accepted Grid Australia's proposal that the threshold values should be maintained over time in real terms for:

- New small transmission network assets;
- New large transmission network assets; and
- Network replacement information (as proposed in this Rule change proposal);

The Commission considers that this promotes the NEO²⁵ as it provides that the required projects are captured by the relevant thresholds over time to maintain the appropriate balance between regulatory scrutiny and transparency and the regulatory burden on TNSPs.

The Commission however has made extensive modifications and enhancements to this part of the Rule change proposal (see section 2.7 below and Appendix A part 4). While the Commission accepts the principle of Grid Australia's proposal it notes comments made in submissions questioning the validity of the PPI as proposed by Grid Australia²⁶.

The Commission considers that a review of the threshold values is a more preferable method of maintaining the threshold values over time in real terms than automatic indexation.

The Commission considers that a review would allow for a number of indices to be used and for market consultation to guide the determination of an appropriate value.

²⁵ Formerly the National Electricity Market objective.

²⁶ ERAA submission, p3, Hydro Tasmania submission, p1-2.

A review would provide for a more thorough analysis into the input costs of the threshold values. This would also include a consultation period where it is expected that the relevant factors from the various aspects of industry could be obtained.

The review has been limited to being a review of a change to the input costs only and not a review of the material value of the asset thresholds. In accordance with this principle the Commission has removed the provision currently contained in the definitions of new small transmission network asset and new large transmission network asset that allows the AER to change the value of the asset thresholds.

Having analysed the effects of indexation from 2002 to the present the Commission considers that the review should take place every three years as the analysis found that input costs did not vary considerably on an annual basis.

The Commission considers that the timeframes to conduct the review should allow adequate time for industry consultation, and for a thorough examination of the input costs but should not unduly delay the introduction of changes that would seek to maintain the value of the thresholds where there is a change in input costs. The Commission has therefore provided for a 16 week process, with 6 weeks allocated to the publication of a draft decision, 5 weeks allocated to consultation and 5 weeks allocated to the publication of a final decision.

The Commission considers that the AER be responsible for conducting the review as this function is in accordance with the AER's current roles of monitoring, enforcing and promulgating the Regulatory Test.

The Commission considers that this mechanism allows for the proper consultative consideration of appropriate threshold values over time, and therefore better promotes the NEO over automatic indexation.

2.6 Commission's Determination

The Commission has assessed the main elements of this Rule change proposal against the NEO²⁷, and in accordance with its assessment framework as described above. The Commission has also had regard to the information that has been presented to it and that it has obtained through its own analysis and research. The Commission's decision in respect to this Rule change proposal therefore is to:

- Increase the new small transmission network asset threshold from \$1 million to \$ 5 million;
- Increase the new large transmission network asset threshold from \$10 million to \$20 million;
- Provide for information disclosure on network replacements over \$5 million;
and

²⁷ Formerly the National Electricity market objective.

- Provide for a review process so that the threshold values are maintained over time in real terms.

2.7 Differences between proposed Rule and draft Rule

The Commission has largely adopted Grid Australia's proposed Rule but has made some modifications arising out of its own analysis and in examining issues raised in submissions. The modifications have been made as the Commission considers that they better promote the NEO²⁸. The Commission's reasoning for the modifications are outlined in Appendix A to this determination. The modifications to the proposed Rule contained in the draft Rule are:

- Raising the new large transmission network asset threshold from \$10 million to \$20 million (and not an increase to \$35 million as proposed in the Rule change proposal);
- Providing for a three yearly review of threshold values to be conducted by the AER (instead of annually updated based on PPI);
- Removing the ability of the AER to change the amount of the asset thresholds that is provided for in the definitions of new small transmission network asset and new large transmission network asset;
- Additional information to be provided in regards to replacement transmission assets including: the purpose of the proposed new replacement transmission asset; a list of alternative projects to the proposed new replacement transmission asset; and the TNSP's estimated total capitalised expenditure on the proposed new replacement transmission asset;
- Provision for VENCorp to publish the replacement transmission asset information in the Victorian APR and for SP AusNet to provide the relevant information by 28 February each year; and
- Clarifying the meaning of the meaning of the term "replacement network asset".

²⁸ Formerly the National Electricity Market objective.

A Commission's analysis of the Proposed Rule

In this Appendix, the Commission addresses a number of issues that have been raised in submissions or that have emerged during its analysis.

In assessing this Rule change proposal against the NEO the Commission considers that the key question is balancing the amount of regulatory scrutiny applied to augmentation projects to promote efficient market outcomes and providing the appropriate regulatory burden on TNSPs in relation to those projects.

In assessing the costs and benefits of the proposal the Commission needs to consider whether the requirement for the tools of regulatory scrutiny (including information disclosure, public consultation, a test for economic efficiency of projects, and dispute resolution) need to be balanced by the regulatory burden, (including costs to TNSPs, necessity of the information and the efficient allocation of resources). Promoting timely investment and preventing unnecessary delays are also factors that the Commission considers are important in assessing this proposal.

The Commission must seek to achieve the best regulatory practice in considering these factors for the different threshold levels of augmentation projects.

In summary, there are four areas covered in this draft determination:

1. Regulatory test asset thresholds. This includes discussion of the asset thresholds generally and discussion of the particulars of the new small transmission network asset threshold and new large transmission network asset threshold;
2. Information disclosure for network replacements;
3. Special arrangements under the Victorian Derogation; and
4. Indexation of relevant values.

The Commission has assessed these elements of the Rule change proposal in respect of transmission only. While some of the issues of this Rule change proposal are applicable to distribution as well as transmission the Commission considers the assessment and applicability of these issues in relation to distribution to be a separate matter requiring separate analysis. The Commission therefore considers the applicability of the elements of this Rule change proposal to distribution to be out of scope of this Rule change proposal.

A.1 Regulatory Test asset thresholds

A.1.1 Proponent – Asset thresholds Generally

In its Rule change proposal Grid Australia states that:

- The asset thresholds in the Regulatory Test were part of the Network and Distributed Resources Code changes²⁹. At the time they were introduced some TNSPs considered that the threshold levels were too low. The ACCC however erred on the side of conservatism as the threshold arrangements were new and set the levels to \$1 million and \$10 million.
- Since 2001, there have been substantial increases in the input cost of materials used in transmission assets (eg steel, aluminium, copper) and in construction labour costs. Grid Australia provided information in their supplementary submission on upward movements in relevant input costs; and the actual costs of construction of certain types of projects³⁰.
- In relation to the issue of demand management solutions Grid Australia acknowledges that such solutions are able to defer transmission network investment for relatively short periods of time. Grid Australia however states that such solutions are generally implemented at the distribution level. Grid Australia states that that TNSPs account for demand side initiatives in their APRs and regulatory test information through the demand and energy forecasts provided by DNSPs.

A.1.2 Proponent - New Small Transmission Network Assets

In relation to the new small network asset threshold specifically, Grid Australia states that the threshold is too low because:

- “a very limited number of transmission network augmentations can be constructed for a capitalised value of less than \$10 million. Such augmentations might include capacitor banks, the installation of small transformers where minimal substation works are required and minor upratings of existing transmission lines”;
- “Market participants and interested parties have demonstrated negligible interest in these types of assets, apart from being informed at a high level that such network developments are being proposed. In light of some six years experience in conducting the regulatory test and undertaking the necessary public consultation under the Rules, only one submission has ever been lodged with a TNSP in response to consultations on small network assets (and this submission did not propose a non-network solution); and
- “In the majority of these cases, there are few, if any, feasible network alternatives and no non-network alternatives... Experience indicates that market participants are unlikely to develop alternatives to defer these low

²⁹ ACCC, Applications for Authorisation – Amendments to the National Electricity Code Network and Distributed resources, 13 February 2002.

³⁰ Grid Australia supplementary submission, pp5-7.

cost long life assets [such as capacitor banks]... the provision of information regarding the ranking of options and Regulatory Test analysis for assets under \$10 million is therefore considered to be of very limited value.”³¹

In its Rule change proposal Grid Australia stated that a benefit from raising the small asset threshold would be to increase the responsiveness of market participants to identified and emerging network developments. Grid Australia states that small augmentations are generally required to meet localised load increases which can arise at relatively short notice. Grid Australia states that increasing the threshold would also reduce the unnecessary and inefficient use of resources to develop and provide information that is of minimal interest to market participants.

Grid Australia states that a new threshold of \$5 million should ensure that the development of routine and non-controversial assets such as capacitor banks are not unproductively captured by the relevant consultation requirements under the Rules and thereby improve the efficiency of consultation and approval processes within the businesses.

A.1.3 Proponent - New Large Transmission Network Assets

In relation to new large transmission network assets specifically, Grid Australia states that the primary driver for the increase in the threshold level is to improve the efficiency of the consultation and approval processes associated with such developments. Grid Australia states that its experience of applying the Regulatory Test indicates that the majority of opportunities for efficient non-network alternatives arise at thresholds much greater than the current \$10 million threshold established in the Rules.

Grid Australia states that its data indicates that:

- “A total of 111 submissions were received in response to formal Regulatory Test consultations undertaken under the Rules in relation to 144 identified emerging needs”;
- “64% of the submissions received through the Application Notice/Final Report process related to routine and uncontroversial matters, with the remaining 36% offering potential non-network options;
- “Of the 110 submissions received in response to consultations on identified emerging limitations in the new large network augmentation category since 2001, only seven proposals across the entire NEM were demonstrably commercially and technically feasible. These non-network options were made in response to transmission line augmentations estimated to cost over \$33 million (\$2001/02), rather than transformer or capacitor bank installations. Specifically, the regulatory test analysis and consultation resulted in recommendations to construct new large network assets estimated to cost \$33

³¹ Grid Australia Rule change proposal, pp3-4.

million, \$48.9 million, \$73 million, \$320 million and \$340 million respectively. As the cost of these projects would be much higher in 2007 dollars, they would all still be captured under the proposed new threshold of \$35 million; and

- “Significant augmentation projects of broad interest to market participants and non-network solution proponents were unlikely to be constructed for less than \$25 million historically, or \$35 million more recently. For example, of the 44 consultations undertaken by TNSPs on large augmentation projects in the last six years, 54% of these were estimated to cost well in excess of \$35 million. A further 23% of such consultations fell within the \$25 million - \$35 million category. This information indicates that, on the basis of history alone, \$10 million falls well short of the baseline for network augmentations the consultation process is designed to address. Indeed, projects which were regarded as small network assets at that time can now find themselves (inappropriately) cast as large projects, due solely to the significant escalation in input costs since 2001”³².

Grid Australia further explains that non-network solutions appear only to be viable as alternatives to large network augmentations because the size of the capital investment and the likely dollars available for non-network solutions. It states that transmission network investments are long-lived so the annual transmission revenue requirement to support the investment is comparatively low. It states that if the non-network solution is only required for a few years, a much lower capital investment will result in the annual cost of the non-network solution exceeding the alternative transmission revenue requirement, and so be uneconomic.

Grid Australia further states that while non-network solution proponents may be willing to put forward potential solutions to address network limitations, they are less willing to accept appropriate responsibility for performance to meet a TNSPs mandated reliability obligations (e.g. penalties for non-performance).

Grid Australia therefore states that:

- The \$10 million threshold is, at today’s construction costs, clearly out of step with what constitutes an appropriate hurdle value upon which to initiate investigations;
- The \$10 million threshold is also significantly lower than the historical project value at which technically and commercially feasible non-network options have been proposed;
- increasing the thresholds for the Regulatory Test will not diminish the opportunities for non-network alternatives to transmission investment. Instead, it may serve to focus the attention of providers of non-network alternatives on those investment opportunities that are most likely to be

³² Grid Australia Rule change proposal, p5

economically viable and serve to increase the overall efficiency of the NEM;
and

- that in the Commission's draft Rule determination for the Transmission Network Replacement and Reconfiguration Rule change that the Commission postulated a threshold of \$35 million – being the midpoint of the \$20 million to \$50 million range it perceived as appropriate³³. Grid Australia considers this to be reflective of where the threshold level should be³⁴.

A.1.4 Submissions

VENCorp did not support the Rule change proposal and questions whether increasing the threshold values would reduce the amount of necessary information available to market participants. VENCorp also does not agree that a lack of feedback or submissions to APRs, applications notices or requests for information are an indication that is not used or relied on by the market. VENCorp is of the view that the information is valuable.

The ERAA did not support the Rule change proposal as it considered that the regulatory regime should have a bias towards transparency at the cost of a little administration expense.

The ERAA states:

- Existing TNSP revenues were set on the basis of the current levels of consultation continuing. Conversely Grid Australia have not proposed any reduction in cost to consumers as a result of the reduced administrative overheads provided by its proposed threshold levels. The ERAA therefore consider that the proposal provides a reduced level of service and transparency by TNSPs with no additional benefit to consumers;
- The administration costs of the current threshold levels are minimal compared to the capital costs of the projects being assessed and consulted on. The ERAA therefore considers that the risks of inappropriate investment proceeding at the proposed threshold levels exceed the costs to customers of maintaining the existing thresholds;
- A lack of response does not indicate the information is of no use. The ERAA considers that the information can be used by competitive market participants to better inform their investment decisions in a particular area; and
- A lack of submissions may indicate that most projects are non-controversial. The ERAA considers that it is better for the market to determine what is

³³ AEMC, Draft National Electricity Amendment (Transmission Network Replacement and Reconfiguration) Rule 2006, 26 October 2006.

³⁴ AEMC, Transmission Network Replacement and Reconfiguration, 1 March 2007.

controversial through a consultation process rather than for a TNSP to make such a decision.

TRUenergy does not support the Rule change proposal and is of the view that increases of 500% and 350% are not justifiable whilst the overhead of completing the test remains small in comparison with the cost of the augmentation. TRUenergy further states:

- An increase in the threshold will mean that a range of investments that are currently assessed under the regulatory test would be bypassed. TRUenergy is of the view that the costs of running a fully transparent test are small compared to the capital cost of the proposed augmentations therefore the current thresholds do not seem overly burdensome;
- The chapter 6A framework is based on the current thresholds. TRUenergy is of the view that given the regulatory test's role in assisting the AER to determine whether forecast capital expenditure is reasonable and efficient that the Commission should not permit a dramatic increase in the thresholds;
- Increasing the thresholds will substantially reduce the amount of information available to the market. TRUenergy state that generator investments can be impacted by wealth transfers resulting from decisions whether or not to progress transmission investments. It states that these wealth transfers can be larger than the augmentation itself. TRUenergy states that the planning and assessment processes for augmentations need to be conducted transparently or market based investors will lose confidence in the process of transmission development. It states that this will increase the risk burden on participants and the market;
- The lack of formal submissions on augmentations below \$35 million does not mean a lack of interest but rather is a statement of confidence in the regulatory test; and
- The lower levels of transparency and information available to the market as a result of increasing the regulatory test thresholds is contrary to the recommendations of a recently released NERA report on the role of demand side participation in the NEM.

Hydro Tasmania supports the principles outlined by Grid Australia and the aim of reducing overheads associated with economically efficient changes to the transmission network. Hydro Tasmania proposes a threshold that varies with the total regulated asset base of each jurisdiction. Hydro Tasmania is of the view that this would provide the appropriate balance between regulatory scrutiny and the impact on customers.

The NGF supports Grid Australia's Rule change proposal. It states however that in relation to the higher threshold, that an increase from \$10 million to \$35 million appears large relative to the capital budgets of smaller TNSPs. The NGF states that a value closer to \$25 million may provide greater assurance that all large projects of significance to NEM participants would continue to receive full scrutiny.

Energex supports the Rule change proposal and states that since 2001 there have been substantial increases in the input costs of materials used in transmission and distribution assets and in construction labour costs.

A.1.5 Commissions analysis of information

In reaching its decision the Commission has examined the following information as part of its analysis:

- Input cost information from the inception of the threshold values to the present (see appendix C);
- Information on the cost of undertaking the regulatory test compared to the capital costs of projects. This information was requested by the Commission and provided to the Commission on a confidential basis and has therefore been treated in accordance with the Commission's "Guidelines for Making Written Submissions on Rule Change Proposals". The guidelines state that the Commission considers that where submissions (or parts of submissions) are treated as confidential, they cannot be tested and subjected to the full scrutiny that the public consultation process allows. The Commission takes this lack of public scrutiny into account in the appropriate weight to be attributed to confidential information contained in a submission;
- Examination of APRs and application notices to ascertain the number of projects that fall within relevant cost bands and to assist in understanding the level of information disclosure and consultation;
- Historical data including the relevant ACCC decision that incorporated the thresholds in the National Electricity Code (now the Rules)³⁵.

A.1.6 Commission's consideration of thresholds generally

In assessing the regulatory test asset thresholds for transmission the Commission has examined the following information (see Appendix A for further detail):

- Input cost information (see Appendix C);
- Information on the cost of undertaking the regulatory test compared to the capital costs of projects³⁶ ;

³⁵ ACCC, Applications for Authorisation – Amendments to the National Electricity Code Network and Distributed Resources, 13 February 2002.

³⁶ This information was requested by the Commission and provided to the Commission on a confidential basis and has therefore been treated in accordance with the Commission's "Guidelines for making Written Submissions on Rule Change proposals". The guidelines state that the Commission considers that where submissions (or parts of submissions) are treated as confidential, they cannot be tested and subjected to the full scrutiny that the public consultation process allows.

- Examination of APRs and application notices to ascertain the number of projects that fall within relevant cost bands and to assist in understanding the level of information; and
- Historical information including the relevant ACCC decision that incorporated the thresholds in the National Electricity Code (now the Rules)³⁷.

The Commission notes that input costs have increased since the inception of the thresholds. Appendix C shows that the input cost increases from the various indices from 2002 to the present are: 36% for the general construction PPI; 64% for the power transformer PPI; 102% for the distribution transformer PPI; 20% for the electricity supply PPI and 16% for the CPI. This means that projects that were originally not intended to be captured by the threshold are now being captured by the thresholds as the threshold values have remained constant over time. This consequently would increase the regulatory burden on TNSPs and result in an increase in costs, the time taken to approve investments and the requirement for the extra allocation of resources to address the regulatory burden. The results are inefficiencies in the regulatory process.

Submissions to the Rule change proposal however have commented that regulatory scrutiny on regulated businesses increases their transparency in terms of their expenditure and in the network planning process³⁸. The Commission considers however that this should be balanced against the cost of that regulatory scrutiny to achieve regulatory best practice. The Commission also notes that some submissions have also commented that the thresholds should be increased³⁹.

The Commission considers that arrangements should reflect good regulatory practice. This means that it is important that the process does not result in unjustified cost and use of resources. The regulatory process imposes a cost and that should be proportionate to the size and effect of the project. The inflation in input costs has caused an unintended shift in the relationship between the regulatory process and the impact of the project which was established by the ACCC in 2002⁴⁰.

The Commission therefore considers that based on the evidence presented in its analysis that it would promote the NEO to increase the regulatory test threshold values with respect to transmission network augmentations. The Commission considers that there is no exact science to determining the appropriate thresholds. Instead it is a matter of judgement and ensuring that the appropriate balance is achieved between regulatory scrutiny and transparency for the different levels of projects. This assessment will be undertaken for the two threshold levels below.

The Commission takes this lack of public scrutiny into account in the appropriate weight to be attributed to confidential information contained in a submission.

³⁷ ACCC, Applications for Authorisation – Amendments to the National Electricity Code Network and Distributed Resources, 13 February 2002.

³⁸ VENCorp submission, pp 1-2, ERAA submission pp 1-2, TRUenergy submission pp1-2.

³⁹ Hydro Tasmania submission, p1, NGF submission, p1, Energex submission pp1.

⁴⁰ Ibid

A.1.7 Increasing New Small Transmission Network Asset Threshold

The Commission has determined that the asset thresholds are to be increased. This section shows the Commission's reasoning for the amount that the new small transmission network asset should be increased to.

In considering the quantum of the threshold the Commission has to consider the best regulatory practice threshold amount. The Commission also has regard to the effects of increasing the small asset threshold. These are:

- Projects between \$1 million and \$5 million would now not be required to undertake the regulatory test assessment; and
- The information from undertaking the regulatory test would not be disclosed to the market because such projects are now not required to undertake the regulatory test assessment. Information on these projects is still required to be published under clause 5.6.2A of the Rules (see Appendix D).

The Commission has also ascertained that:

- The information not supplied to the market by raising the threshold was only the regulatory test assessment information, and that clause 5.6.2A of the Rules requires information to be disclosed regardless of the asset threshold (see appendix D);
- That in place of the regulatory test assessment, the Chapter 6A framework provides scrutiny on the economic efficiency of projects when TNSPs seek to obtain approval from the AER for their five year revenue determinations. This effectively provides regulatory scrutiny on TNSPs to minimise the cost of projects and therefore provides safeguards for projects of between \$1 million to under \$5 million projects;
- Information on the costs of undertaking the regulatory test against the capital cost of projects⁴¹ showed that the proportion of costs of undertaking the regulatory test was high in comparison to other project cost bands for the project cost band of \$1 million - \$5 million; and
- Input costs have increased. Appendix C shows that the input cost increases from the various indices from 2002 to the present are: 36% for the general construction PPI; 64% for the power transformer PPI; 102% for the distribution transformer PPI; 20% for the electricity supply PPI and 16% for the CPI

In light of this analysis the Commission has determined that the new small transmission network asset threshold should be increased to \$5 million. In setting this value the Commission has accepted Grid Australia's Rule change proposal. The Commission considers that this amount provides the appropriate balance between the level of regulatory scrutiny applied to augmentation assets and providing the

⁴¹ Information provided on a confidential basis

appropriate regulatory burden on TNSPs in relation to projects. The Commission further notes that increasing the threshold value to \$5 million would ensure that simple minor projects are not unnecessarily delayed.

A.1.8 Increasing Large New Transmission Network Asset thresholds

The Commission considers that the question of how much to increase the large asset threshold is a separate question to the small asset threshold due to the different effects of increasing the large and small thresholds. The effects of increasing the large asset threshold are:

- That information disclosure will be through the APRs and not through application notices and requests for information which include public consultation; and
- There is no mechanism to dispute certain matters.

In determining an increased threshold value for the large asset threshold the Commission is required to balance on the one hand the fact that input costs have increased which has meant that assets that were not intended to be captured by this threshold are now captured, thus increasing the regulatory burden on and the administrative costs of TNSPs. On the other hand however the Commission considers that the regulatory scrutiny in terms of public consultation and the availability of dispute resolution is important for projects of a particular scale.

The Commission has therefore decided not to accept Grid Australia's proposal of raising the new large transmission network asset threshold to \$35 million but instead to raise the new large transmission network asset threshold to \$20 million.

The Commission considers that this figure reflects the increase in input costs as well and also provides the appropriate balance between the regulatory burden on TNSPs and ensuring the appropriate level of regulatory scrutiny to promote efficient market outcomes, and the timely delivery of transmission services to consumers. In providing for this increase the Commission notes that participants will still be able to provide comments to the TNSP on the proposed projects through responding to the information contained in the APRs. The increase will also provide for transmission investment to proceed in a timely manner and not be unnecessarily delayed.

A.2 Information disclosure for network replacements

A.2.1 Proponent

Grid Australia proposes that TNSPs be required to disclose certain information on all network projects (including replacements) in excess of \$5 million in their respective APRs in addition to current disclosure requirements in relation to forecast loads, future connection points, forecast constraints, proposed augmentations and new small transmission network assets. The proposal requires TNSPs to disclose information about replacement projects, such as:

- A brief description of the project; and
- The planned commissioning date.

A.2.2 Submissions

ERAA supports this part of the Rule change proposal as it provides more information disclosure from regulated network businesses.

Energex supports this part of the Rule change proposal as it would provide market participants with advance notice of large forthcoming network replacement requirements.

The NGF supports this aspect of the Rule change proposal to publish information on all network projects above \$5 million. It states that any proposed wording should apply to all material projects replacements, refurbishments, relocations and reconfigurations, which it considers is the intent of the proposal.

A.2.3 Commission's considerations and reasoning

The Commissions agrees with submissions⁴² and the Rule proposal that additional information disclosure by TNSPs on network replacements over \$5 million increases the transparency of the planning process and the operation of regulated businesses. In this way information disclosure promotes the NEO.

The Commission has accepted Grid Australia's Rule change proposal but has made key modifications and enhancements to it. These include:

- Providing for additional information in regards to network replacements over \$5 million that are in accordance with the information currently required for all augmentations (whether they fit into an augmentation threshold or not);
- Clarifying the definition of network replacements in accordance with the policy intent of the proposal; and

The Commission considers that these modifications provide useful information to the market without imposing too onerous a burden on the TNSPs and therefore better promote the NEO than the proposed Rule.

⁴² ERAA submission, p4, Energex submission, pp 1-2, NGF submission, p1.

A.3 Information disclosure for network replacements - Special arrangements for Victoria

A.3.1 Proponent

Grid Australia states that in Victoria, VENCorp has the obligation to publish the electricity transmission APR. It states that acceptance of this Rule change proposal will require a consequential minor amendment to the Victorian derogation to ensure that the proposal operates effectively in Victoria. Grid Australia states that the minor amendments to the derogation would specify that the obligation to publish information on replacement networks belongs to SP AusNet.

A.3.2 Submissions

VENCorp agrees that an amendment to the Victorian derogation is required. VENCorp however is of the view that providing for SP AusNet to publish a separate document outlining replacement information could lead to:

- VENCorp not having SP AusNet's replacement information prior to publishing the Victorian APR; and
- Confusion for market participants who would have to refer to two separate documents to obtain all transmission network information for that year.

VENCorp are therefore of the view that it should retain the responsibility for publishing all network information including information on replacement assets. On this point VENCorp states that replacement asset information should be provided by SP AusNet to VENCorp by 28 February of each year.

A.3.3 Commission's considerations and reasoning

The Victorian derogation relates to the separation of the network planning and ownership functions from the network operation and maintenance functions in Victoria.

The Commission notes that currently VENCorp is responsible for publishing the Victorian APR. The Commission agrees that requiring SP AusNet to publish a separate document would add unnecessary complexity and confusion to the presentation of network information.

Recognising this the Commission considers that it better promotes the NEO for VENCorp to publish the "network replacement information" in the APR, and for SP AusNet to provide the necessary information to VENCorp.

In amending this derogation the Commission has had regard to the matters set out in section 89 of the NEL and considers that this consequential amendment to the Victorian derogation is required.

A.4 Threshold values to be maintained over time

A.4.1 Proponent

In its Rule change proposal Grid Australia states that to ensure that the monetary thresholds are not diminished by movements in cost over time, that the monetary thresholds be indexed by an appropriate escalator. Grid Australia considers that the PPI released by the Australian Bureau of Statistics should be used as the appropriate escalator. Grid Australia states that the PPI appears to better reflect the general movement in prices facing the construction sector than the CPI. Grid Australia also proposes that the thresholds be automatically indexed annually.

In its supplementary submission Grid Australia states:

“[Grid Australia] considers that a reasonable approach is to adjust the thresholds once accumulated annual escalations reach a threshold amount (rounded) of \$5 million for large network assets and \$1 million for small network assets. Once adjusted, any revised thresholds would apply to regulatory test consultations commencing from 1 July in the following year. It is intended that escalation of the thresholds be able to occur without the need for activation of the Rule change process. [Grid Australia] considers that this could be effected by release of a public notice from the AEMC or AER as appropriate.⁴³”

A.4.2 Submissions

The ERAA considers that there is some merit in indexing the threshold values. The ERAA however states:

- “It only allows upward indexation of the thresholds. This would result in the thresholds increasing in real terms over time, by not allowing appropriate deflation of the thresholds in the event that construction input costs were to materially fall in any period.”
- “By always rounding up to the nearest million, the proposed wording would result in the thresholds increasing by at least 1 million dollars in any year that positive inflation occurred. It would seem probable that this would result in the \$1 million threshold increasing to \$6 million in 5 years time – an outcome that would result in a material real threshold increase even in a period of very low cost inflation.⁴⁴”

The ERAA further states that any indexation provision should maintain the thresholds at the current levels in real terms over time and allow for both

⁴³ Grid Australia supplementary submission, p8.

⁴⁴ ERAA submission, p3.

inflationary and deflationary movements. The ERAA also states that the Commission should review whether the PPI is the most appropriate index.

Hydro Tasmania are not supportive of the PPI as an appropriate indicator. It considers that the PPI escalation suggested by Grid Australia will impact disproportionately on those whose incomes are CPI related.

A.4.3 Commission's considerations and reasoning

The Commission has accepted Grid Australia's proposal that the threshold values should be maintained over time in real terms for:

- New small transmission network assets;
- New large transmission network assets; and
- Network replacement information (as proposed in this Rule change proposal);

The Commission considers that this promotes the NEO as it provides that the required projects are captured by the relevant thresholds over time to maintain the appropriate balance between regulatory scrutiny and transparency and the regulatory burden on TNSPs.

The Commission however has made extensive modifications and enhancements to this part of the Rule change proposal. While the Commission accepts the principle of Grid Australia's proposal it notes comments made in submissions questioning the validity of the PPI as proposed by Grid Australia⁴⁵.

The Commission has provided for a review of the threshold values rather than automatic indexation.

The Commission considers that a review would allow for a number of indices to be used and for market consultation to guide the determination of an appropriate value. A review would provide for a more thorough analysis into the input costs of the threshold values. This would also include a consultation period where it is expected that the relevant factors from the various aspects of the industry could be obtained.

The review has been limited to being a review of a change to the input costs only and not a review of the material value of the asset thresholds. In accordance with this principle the Commission has removed the provision currently contained in the definitions of new small transmission network asset and new large transmission network asset that allows the AER to change the value of the asset thresholds.

Having analysed the effects of indexation from 2002 to the present the Commission considers that the review should take place every three years as the analysis found that input costs did not vary considerably on an annual basis.

⁴⁵ ERAA submission, p3; Hydro Tasmania submission, pp1-2.

The Commission considers that the timeframes to conduct the review should allow adequate time for industry consultation, and for a thorough examination of the input costs but should not unduly delay the introduction of changes that would seek to maintain the value of the thresholds where there is a change in input costs. The Commission has therefore provided for a 16 week process, with 6 weeks allocated to the publication of a draft decision, 5 weeks allocated to consultation and 5 weeks allocated to the publication of a final decision.

The Commission considers that the AER be responsible for conducting the review as this function is in accordance with the AER's current roles of monitoring, enforcing and promulgating the Regulatory Test.

The Commission considers that this mechanism allows for the proper consultative consideration of appropriate threshold values over time, and therefore better promotes the NEO over automatic indexation.

This page has been intentionally left blank

B Current Regulatory Test Processes for Thresholds

<u>Type of Asset →</u> Process ↓	<u>Augmentations that are lower than the New Small Transmission Network Asset Threshold</u>	<u>New Small Transmission Network Asset Threshold (Currently \$1 million and above, proposal is to shift this to \$5 million and above)</u>	<u>New Large Transmission Network Asset Threshold (Currently \$10 million and above, proposal is to shift this to \$35 million and above)</u>
Pre-assessment Consultation	Not required	Not required	For non-reliability augmentations, TNSPs are required to issue Request for Information. This must be sufficiently detailed to enable other participants to raise suitable alternatives. This should include (amongst other things) costs, rationale, timetable and technical details. No pre-assessment consultation for reliability augmentations.
Assessment under the Regulatory Test	Not assessed	Assessed under the Regulatory Test (methodology of assessment differs for reliability and non-reliability augmentations)	Assessed under the Regulatory Test (methodology of assessment differs for reliability and non-reliability augmentations)
Information Disclosure	For all augmentation projects the APR must set out: a) reason for project b) proposed solution, c) total cost, d) other reasonable network and non-network options	For all new small transmission assets, APR must contain: a) ranking of reasonable options [including non-network solutions]; b) analysis why project satisfies the Regulatory Test; c) if a small reliability augmentation then why it satisfied the reliability criteria, d) the year the asset becomes operational. APR must also set out: e) reason for project; f) proposed solution; g) total cost; h) other reasonable network and non-network options	For all augmentation projects the APR must set out: a) reason for project b) proposed solution, c) total cost, d) other reasonable network and non-network options

Post Assessment Consultation (Application Notice and Final Report)	Not required	Not Required	<p>Must provide application notice to market which contains a) details of proposed assets; b) reasons for assets [identified constraint]; c) all other reasonable alternatives; d) construction timetables; e) ranking of possible options based on the Regulatory Test; f) detailed analysis as to why the TNSP considers it satisfies the Regulatory Test.</p> <p>For reliability augmentations: g) why the TNSP considers it to be a reliability augmentation; f) detailed calculations as to how the TNSP has determined costs and market benefits.</p> <p>TNSP must review all submissions received within 30 days and use its best endeavours to hold a meeting within a further 21 business days if meeting is requested or the TNSP deems necessary.</p> <p>The final report must address the same matters as included in the Application Notice, summarise submissions, and the TNSPs response to submissions.</p>
Dispute Resolution	Not Applicable	Not Applicable	<p>There is provision for dispute resolution. The grounds of what can be disputed differs between reliability and non-reliability augmentations.</p> <p>The AER assesses the dispute notice and the grounds for dispute.</p>
Possible AER determination on whether proposed asset satisfies the Regulatory Test	Not Applicable	Not Applicable	<p>For non-reliability augmentations only the TNSP may ask the AER to make a determination as to whether the asset passes the Regulatory Test if the findings are not in dispute.</p>

C Indexation Percentage Increases from Inception of Threshold Values to Present

<u>Index</u>	<u>Percentage increase</u>
General Construction Producer Price Index (PPI)	36%
Power Transformer PPI	64%
Distribution Transformer PPI	102%
Electricity Supply PPI	20%
Consumer Price Index	16%

This page has been intentionally left blank

D Information Provided in Annual Planning Reports (APRs) — Clause 5.6.2A(b)(4) and 5.6.2.A(b)(5)

For all proposed augmentations regardless of value and whether or not they are assessed under the regulatory test the following needs to be included in the APRs. This information will still need to be provided whether or not the asset thresholds shift for all augmentations. The information is as follows:

- Project/asset name and the month and year which it is proposed that the asset will become operational;
- The reason for the actual or potential constraint, if any, or inability, if any to meet the relevant network performance requirements;
- The total cost of the proposed solution;
- Whether the proposed solution will have a material inter-network impact;
- Other reasonable network and non-network options considered to address the actual or potential constraint or inability to meet the relevant network performance standards.

For proposed new small transmission network assets (i.e the augmentations that are assessed under the Regulatory Test) the following information is required to be provided. This is the information that will be lost for projects that no longer need to be assessed due to increasing the asset thresholds. The information is as follows:

- An explanation of the ranking of reasonable alternatives to the project including non-network alternatives;
- An augmentation technical report prepared by the Inter-Regional Planning Committee, if the asset is reasonably likely to have a material inter-network impact and the TNSP has not received the consent to proceed with the proposed solution from all TNSPs whose transmission networks are materially affected by the new small transmission network asset; and
- Analysis of why the TNSP considers the new small transmission network asset satisfies the regulatory test. In addition if the TNSP considers that the new small transmission network asset is a reliability augmentation then it must provide analysis as to why it considers it to be a reliability augmentation.

This page has been intentionally left blank