28 January 2021

Ms Merryn York
Acting Chair, Australian Energy Market Commission
GPO Box 2603
Sydney NSW 2001

Draft Rule Determination – Connection to Dedicated Connection Assets (ERC0294)

Dear Ms York,

The Clean Energy Finance Corporation (**CEFC**) welcomes the opportunity to make a submission on the Australian Energy Market Commission's (**AEMC**) Connection to Dedicated Connection Assets Draft Rule Determination.

The CEFC is responsible for investing $10 billion in clean energy projects on behalf of the Australian Government and was established to facilitate increased flows of finance into the clean energy sector. The CEFC supports the development of a resilient, balanced and secure electricity system through its investment activities, including large-scale renewable energy, energy storage and other initiatives in accordance with the 'grid firming' focus of its Investment Mandate. The CEFC considers the potential effects on reliability and security of supply when evaluating potential renewable generation investments and prioritises investments, including network solutions that will support reliability and security of electricity supply.

CEFC continues to support approaches being adopted to facilitate an ability for multiple market participants to utilise connection assets and see rule changes as instrumental in its ability to facilitate renewable energy zone (**REZ**) opportunities and complement activity that the Energy Security Board (**ESB**) is undertaking to establish frameworks to support REZ activity. Whilst the market's view of what constitutes a REZ is varied, CEFC consider that the framework established under this rule change has the ability to create a platform to attract investment in shared connection assets and facilitate the co-ordination amongst market participants in a manner which some would deem a 'REZ'.

The pivot to a dedicated network asset (**DNA**) under AEMC's preferable draft rule appears to reduce the complexity that could be caused by nested dedicated connection assets by facilitating a clearer nexus between the market participants and the network resulting in greater transparency and accountability between the parties.

Whilst the proposed DNA approach appears to overcome barriers to the application of shared connection assets, there are two areas within the draft rule that the CEFC believe warrants further consideration:

1. Party Responsible for Establishing Access Policies

   Under the current rules, CEFC understands that the party responsible for establishing access policies is the dedicated network asset service provider (**DNASP**). Under the draft determination, this responsibility is proposed to transfer to primary transmission network service providers (**PTNSPs**). Whilst CEFC agrees

that having the PTNSPs operate and maintain DNAs has significant security benefits, transferring access policy responsibilities would likely reduce contestability and potentially harm the investment signal for shared connection assets.

A DNASP relinquishing this control may significantly impact the appetite that an investor has for DNAs and raise potential areas of conflict between the objectives of the DNASP and the PTNSP. For example, a DNASP would likely focus on maximising the utilisation of the DNA asset and in a timely manner. In doing so the DNASP would likely play a co-ordination role with market participants to maximise demand for connection, possibly identifying or targeting a combination of technologies that would complement each other to extract maximum value for that investment.

The same incentives for the utilisation of connection assets and coordination do not appear likely where the PTNSP does not have a financial interest in the DNA.

Prohibiting the DNASP from access policy decision making would dampen the investment signal and potentially restrict the size of DNA assets as DNASPs would have a limited ability to directly address risks associated with under-utilisation of the connection assets. Under-utilisation of assets is inefficient from a whole-of-system perspective and should be expected to indirectly result in an increase in costs to consumers.

The investment proposition would likely be enhanced where the DNASP is responsible for developing the access policy (with approval from the AER), as is the case under the current rules for the dedicated connection asset service provider (**DCASP**). This being the case because the DNASP would be able to tailor the access policy that is needed to support its individual investment case, and to appropriately incentivise further generators to connect. This is best illustrated through the following examples:

- If the DNASP is also a foundation generator, it may be able to absorb a higher connection charge at the outset (in its capacity as generator) by taking a view on the additional return from further generators connecting and paying connection fees (in its capacity as the DNASP). The investor would require flexibility to enable such a 'blending' of returns to work practically.
- The DNASP also may require a more flexible methodology for cost allocation amongst market participants in the DNA e.g. to incentivise more foundation generators to connect earlier the DNA investor may want to charge these generators a lower connection fee, with subsequent generators to be charged a higher connection fee; alternatively, the foundation generators may be able to sustain a higher connection fee at the outset to cover costs, with these generators being prepared to collectively take risk on additional generation connecting, by reducing their connection fee costs over time as additional generation connects.

2. <u>Compensation / Cost Allocation Arrangements amongst market participants in DNAs</u>

CEFC considers that protecting the interest of first movers and disincentivising free riders, on a balanced basis, is critical to facilitating investment in shared assets such as REZs or DNAs.

The existing framework, and potentially even the proposed framework, appears to consider DNA assets in the context of the foundation generator, where any adverse impacts on their project are compensated by subsequent generators. This poses a challenge in that every subsequent generator becomes increasingly disincentivised to connect to the DNA as a portion of their cash flows are compensating the existing generator/s. Under the proposed S5.12 *Negotiating Principles for DNA*, principles (6) and (7) may unduly impact an oversized DNA and these principles may be more appropriately applied once the capped capacity has been exceeded.

These disincentives have to date not appeared to be a significant concern given generators have traditionally sized their connection to meet their needs. If the ESB and AEMC see the regulatory framework for DNAs as a means to establish a mechanism for the market to encourage scale efficient network solutions (i.e. REZs), CEFC suggest that the principles within the access policy may need to be reviewed to facilitate an outcomes based approach.

To demonstrate this point, take a hypothetical, where a DNASP proposes to construct a DNA that can accommodate 1GW of generation capacity, and from the outset the DNASP collates interest from multiple generators. With amendments to the access policy framework/ principles, the DNASP could establish parameters such as caps on capacity and cost allocation principles based on the 1GW solution that it considers is necessary to maximise demand for generators. The parameters set by reference to the scaled solution are disclosed to all interested parties and this information forms the basis of their due diligence (grid studies, transmission loss factor forecasts, etc).

Subsequent generators would not compensate foundation generators due to the deterioration of the latter's project (if within the DNA's access policy parameters) because the basis of their investment was with full knowledge that capacity up to a cap was permitted. Establishing an outcomes based approach would seek to incentivise the utilisation of scale efficient solutions by balancing the value transfer amongst participants in the DNA. DNASPs should have sufficient flexibility over the cost allocation principles to be agreed upfront to allow them to attract different generators (i.e. lower costs for foundation customers or parties with complementary generation profiles such as storage, firming assets).

Increasing the utilisation of DNAs should deliver a more efficient grid (which ultimately benefits consumers) by not only lowering the cost solution for connection assets through scale efficiencies but also increasing contestability by attracting more investors to this asset type.

We look forward to the opportunity to engage further with the AEMC. Should you wish to discuss this submission further, please contact Bobby Vidakovic (Director – Clean Futures Team) on bobby.vidakovic@cefc.com.au or 1300 002 332.

Yours sincerely

Ian Learmonth
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