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Economic Regulation Authority  
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### **New Facilities Investment Test and Net Benefit guideline**

The Australian Energy Council (the “**AEC**”) welcomes the opportunity to make a submission to the Economic Regulation Authority (the “**ERA**”) on the *Guideline on factors that will be considered in new facilities investment test determinations including methods to value net benefits* consultation paper (the “**Consultation Paper**”).

The AEC is the industry body representing 22 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

The AEC makes the following comments:

#### **Acceptable methodologies**

The *Electricity Networks Access Code 2004* (“**Access Code**”) states:

*“Net Benefit Valuation Guidelines*

*6A.6 The Authority must:*

*(a) make and publish guidelines that provide guidance as to **acceptable** methodologies for valuing net benefits by a service provider, which methodologies must include, but are not limited to, for the SWIS, consideration of changes in costs and benefits for participants in the Wholesale Electricity Market;”<sup>1</sup>*

The Consultation Paper notes that the service provider must demonstrate that the new facility investment provides a net benefit in the covered network. In assessing the net benefits, the ERA will consider a range of factors, including the engineering and economic models, assumptions, the changes in costs and benefits for participants in the Wholesale Electricity Market, consultation with AEMO, the exclusion of benefits that are transfer payments, and sufficient evidence. The Consultation Paper also notes that “the analysis may include” items such as changes in fuel consumption, voluntary load curtailment, involuntary load shedding, and changes in costs, losses and essential system services.<sup>2</sup>

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<sup>1</sup> See p116-117, [Electricity Networks Access Code 2004](#). Emphasis added.

<sup>2</sup> See p15-16, [Guideline on factors that will be considered in new facilities investment test determinations including methods to value net benefits](#)

The AEC agrees that these matters should be considered in a net benefit assessment. However, it is concerning that they are approached in the Consultation Paper as high-level concepts absent of detail. Without a prescriptive approach outlining the acceptable methodologies, the network operator will have insufficient guidance and the impacts of the project will be open to interpretation. This point was raised by Oakley Greenwood when it considered the net benefit guidelines:

*“There is no reason to believe that Western Power is expert in the conduct of net benefit analyses or that it has sufficient expertise to assess the value of the various impacts that the services ... can have on the various parts of the electricity value chain. As such, it would be helpful for the ERA Guideline to prescribe the methodology and key inputs to be used by Western Power ...”<sup>3</sup>*

A more prescriptive and detailed approach will also assist in preventing the network operator from inadvertently flexing methodologies to suit particular outcomes. Eliminating room for discretion will put all projects on a level playing field and assist with a considered assessment. For instance, the Consultation Paper states that “the service provider must demonstrate that the new facility investment provides a net benefit in the covered network **over a reasonable period of time** that justifies the approval of higher prices.”<sup>4</sup> Without adequate definition, a reasonable period of time could potentially change based on the project and whether you are viewing the project from the perspective of the network operator, regulator or industry stakeholder.

For this reason, Oakley Greenwood went on to suggest:

*“The methodological guideline should specify how the test is to be undertaken, the form in which results are to be presented, and the specific areas of benefit to be included as well as how they are to be assessed. This will ensure consistency in the test across projects and that the test is carried out in a way that the ERA feel provides as accurate and meaningful an assessment of the benefits as possible. The guideline should also provide the values to be used for at least the following key inputs and parameters:*

- *The time horizon for over which the analysis is to be undertaken*
- *The current and projected value of each benefit to be included in the test*
- *The discount rate to be used.”<sup>5</sup>*

The AEC supports this view and notes that the handling of the environmental benefits is another area which isn't addressed with detail but will be a key issue in the assessment of the net benefits. The Access Code states that:

*“efficient investment in, and efficient operation and use of, services provided by means of networks in Western Australia for the long-term interests of consumers [includes] . . . the environmental consequences of energy supply and consumption, including reducing carbon pollution, considering land use and biodiversity impacts, and encouraging energy efficiency and demand management.”<sup>6</sup>*

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<sup>3</sup> See p26, [Implications of network ownership of grid-side battery assets on competition in the Wholesale Electricity Market](#)

<sup>4</sup> See p15, [Guideline on factors that will be considered in new facilities investment test determinations including methods to value net benefits](#). Emphasis added.

<sup>5</sup> See p26, [Implications of network ownership of grid-side battery assets on competition in the Wholesale Electricity Market](#)

<sup>6</sup> See p43, [Electricity Networks Access Code 2004](#)

The AEC expresses caution in including virtuous concepts such as environmental benefits in a net benefit assessment. Environmental considerations are a responsibility for government outside of the industry. It is government's role to identify and manage environmental externalities through environmental legislation which will naturally affect the competitive position of various technologies. Only those benefits that are explicitly priced following a government decision should be included in a net benefit assessment, and the guideline should identify the specific environmental benefits to be assessed, the specific values to be used for each and the conditions that give rise to them. Other matters, particularly the environmental consequences of energy supply and consumption along with land use and biodiversity impacts, are difficult to quantify and attempts to quantify these will lead to considerable responsibility confusion between the industry and government.<sup>7</sup> Western Power does not have expertise on these matters and the ERA will need to be highly prescriptive in the environmental component of a net benefit assessment.

## Other guidelines

The AEC considers that the ERA should be more prescriptive and detail the acceptable methodologies to help guide the network operator to apply a consistent, efficient and effective net benefit analysis. There are examples in other sectors or regions where more specific methodologies have been created and used. For instance, the transport sector has the Australian Transport Assessment and Planning Guidelines that "aims to identify and express, in monetary terms, all the gains and losses (benefits and costs) created by an option or initiative to all members of society, and to combine the gains and losses into a single measure of net benefit (benefits minus costs)".<sup>8</sup>

Perhaps more relevant to the Consultation Paper is the regulator investment test for distribution ("RIT-D") published by the Australian Energy Regulator. The RIT-D is a cost benefit analysis that network businesses must perform before making major investments. When undertaking this cost benefit analysis, network businesses must consult and give due consideration to other options before identifying the best way to address needs on their networks. The RIT-D is generally regarded as a means of encouraging competitive industry development in the supply of non – network solutions, and both the Australian Energy Market Commission and the Australian Energy Regulator have considered the RIT-D as a potential model for managing the introduction of competitive non-network solutions into future network services markets.<sup>9</sup>

The RIT-D could be instructive because it gives detailed guidance on selecting inputs, valuing costs, and the methodology for valuing market benefits, assessing uncertainty and risk, and selecting the preferred option. Most notably, whereas the Consultation Paper says these items "may" be included, the RIT-D quantifies specific market benefits including:

- Voluntary load curtailment;
- Involuntary load shedding and customer interruptions;
- Costs to other parties, such as the benefits of delaying network investment;
- Changes in timing of expenditure;
- Load transfer capacity and embedded generators; and
- Electrical energy losses.

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<sup>7</sup> For further discussion as to why the National Electricity Market has at several times considered, but rejected, an environmental objective, see <https://www.energycouncil.com.au/analysis/objecting-to-the-objectives/>

<sup>8</sup> See [Australian Transport Assessment and Planning Guidelines](#)

<sup>9</sup> See Australian Energy Market Commission, Economic Regulatory Framework Review: Promoting Efficient Investment in the Grid of the Future, July 2018, p 98; and Australian Energy Regulator, Consultation paper: Assessing DER integration expenditure, November 2019, p5- 12.

The AEC suggests that the net benefits guideline should at a minimum include this level of detail to promote investment efficiency by imposing consistency, transparency and accountability on major investment decisions.

### **Adequate engagement**

In addition to the RIT-D quantifying values and specifying the methodology for a cost benefit analysis, it also stresses the importance of stakeholder engagement as part of the assessment process and includes minimum consultation periods. The AEC agrees with this approach and considers that engagement should form part of the efficiency test. There have been instances in the recent past where the network operator has conducted limited tenders with inadequate notification. The perception is that this reflects a preference by the network operator to provide these services internally.

The AEC suggests that, in many cases, the proper role for the network operator is as the provider of last resort of these services, in which they would adequately advertise the need but have plans for implementation only in the event that the competitive market was unable or unwilling to provide services to meet the identified need. The ERA is encouraged to consider this issue and include engagement as part of the guideline.

### **Conclusion**

The AEC appreciates this opportunity to provide feedback on the Consultation Paper and encourages the ERA to consider the issues raised above.

Please do not hesitate to contact Graham Pearson, Western Australia Policy Manager by email on [graham.pearson@energycouncil.com.au](mailto:graham.pearson@energycouncil.com.au) or by telephone on 0466 631 776 should you wish to discuss this further.

Yours sincerely,

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