

Dr Kerry Schott AO
Energy Security Board

17th January 2020

Submitted via e-mail to: info@esb.org.au

Dear Dr Schott,

Consultation on Draft ISP Rules

The Australian Energy Council (the “**Energy Council**”) welcomes the opportunity to make a submission in response to the Energy Security Board’s (“**ESB**’s”) *Consultation on Draft ISP Rules Paper*.

The Energy Council is the industry body representing 23 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, sell gas and electricity to over ten million homes and businesses, and are major investors in renewable energy generation.

Introduction

While the Energy Council supports the role of the Integrated System Plan (“**ISP**”) as providing a unified design towards the development of transmission, the need for robust cost-benefit analysis of augmentation to the monopoly network remains paramount to protect customers from wasteful expenditure, but equally importantly, to provide predictability for competitive investors about the circumstances in which networks will expand.

The Energy Council cautiously supports the ESB’s initiatives to expedite the assessment of transmission projects and deliver the benefits identified promptly. The plans to incorporate much of the Project Specification Consultation Report work into the analysis already being performed by the Australian Energy Market Operator (“**AEMO**”) for the broader market make sense, and, if a high degree of consultation is required in the development of the ISP, stakeholders will be comfortable that the assumptions used will have been appropriately reviewed.

Discussion

Actionable ISP Projects

The Consultation Paper (and the draft Rules) define “actionable ISP projects” as those projects which address an identified need, and form part of the optimal development path. There is no limitation on the timeframe for actionable ISP projects.

The Energy Council is very concerned about the inference to be drawn from such a definition. While projects requiring action within the period between the issue of the ISP and the two years until the next ISP is issued are clearly “actionable”, any projects beyond that timeframe are increasingly speculative, and the action required to progress them would be increasingly limited. Compounded by the reduced likelihood of AEMO’s future occurring as expected (since it only considers currently available options), the need for projects further in the future diminishes markedly, and the epithet of “actionable” is not appropriate for such projects, and should not be used by Transmission Network Service Providers (“**TNSPs**”) to justify anything other than very limited planning. Such long-term future projects are better described as “possible”.

Timeframes for Action

The ISP sets out one possible future, based on limited cost-benefit analysis and risk assessment, and it will be important for TNSPs to retain the flexibility to plan their own network expansions, and not be bound by the ISP’s findings. To this end, requiring TNSPs to publish Project Assessment Draft Reports (“**PADRs**”) within statutory timeframes seems unnecessarily restrictive, and an unfair imposition on the way TNSPs conduct their business. Such obligations make assumptions about businesses’ resource and capital availability, and their appetite for conducting the work. TNSPs have a natural incentive to expand if the circumstances warrant it, and if they choose not to go ahead this would likely be because of a compelling change in circumstances not

predicted at the time of the ISP. The Energy Council therefore questions the removal of the Australian Energy Market Commission's Last Resort Planning Power.¹

Optimal Development Path

The whole concept of "optimal development path" remains unclear, particularly the unjustified position that the path will not need to have the highest nett benefit in the central case.² At a minimum, the Energy Council submits that the ISP should seek to maximise the nett benefit, and this should be done by considering a weighted average of possible scenarios, not just the most likely case (but subject to other considerations such as power system security needs). However nett benefit still has the shortcoming that more expensive projects will be more likely to have greater nett benefits than cheaper projects. The Energy Council therefore believes that AEMO must consider capital efficiency when identifying multiple possible solutions, and this suggests that a better assessment measure for projects on the optimal development path would be rate of return, which considers the capital employed.

The Energy Council also believes that expediting the ISP should not provide latitude for the scrutiny involved in the Regulatory Investment Test for Transmission ("RIT-T") process to be reduced. Draft Rule 5.22.5(d)(4)(i) specifies that the Cost-Benefit Analysis Guidelines (and hence the Cost-Benefit Analysis conducted by AEMO) must consider the counterfactual development path, and the Australian Energy Regulator's ("AER's") initial view is that the ISP counterfactual development path "should contain no ISP projects that are not already committed".³ This suggests that the optimal development path may consider projects in aggregate, which risks including projects which may not be economically successful in their own right. The Energy Council stresses the need for projects to be individually viable, and not carried by related projects.

The divergence between "positive nett benefit" (as proposed in the "Developing and Publishing the Cost Benefit Analysis Guidelines" section of the draft Rules)⁴ and "maximum nett economic benefit" (as set out in the RIT-T Principles within the current Rules)⁵ is also problematic since it may encourage marginal projects to be built which, should costs or benefits differ from initial estimates, may result in significant detriment to consumers. (As mentioned above, the effect of variations will be magnified, since the ISP only considers the "most likely scenario",⁶ rather than weighting a number of possible scenarios.) Therefore the Energy Council believes that it is important to ensure that, irrespective of the ISP's expectation for future power system development, the RIT-T process continues to be followed, with individual projects being required to meet the tests set out in Rule 5.16, and embodied in the AER's Application Guidelines.⁷

Maintaining the RIT-T, and in particular the diligence necessary for the PADR, also has implications for the currency of the ISP. Should a project's PADR reveal significantly different costs or benefits from those developed by AEMO for the ISP, it may change the merit order of actionable projects within the ISP, and cause the optimal development path to vary. The Energy Council therefore supports proposed Rule 5.22.12, which includes provision for the ISP to be updated should AEMO receive material, new information.

Public Policy Needs

The Energy Council disagrees that "public policy needs" should be included in AEMO's assessment of the optimal development path. While acknowledging that individual jurisdictions may have particular desires for the energy industry, it would be disruptive to incorporate such considerations into a document like the ISP which should be underpinned by the defensible, national concepts enshrined in the National Electricity Objective.

There is already a body of literature on how the economic effects of legislated environmental schemes, such as renewable energy targets and carbon pricing, can be correctly incorporated into cost-benefit analyses in a way that is entirely consistent with the National Electricity Objective. There should be no ability for planners to incorporate vague notions of "public policy" which would introduce subjectivity and unpredictability into network development.

¹ National Electricity Rule 5.22

² Consultation Paper p.7

³ Australian Energy Regulator, *Guidelines to Make the Integrated System Plan Actionable – Issues Paper*, November 2019, p.25

⁴ Proposed National Electricity Rule 5.22.5(e)(3)

⁵ National Electricity Rule 5.16.1(b)

⁶ Proposed National Electricity Rule 5.22.5(e)(3)

⁷ Australian Energy Regulator, *Application Guidelines – Regulatory Investment Test for Transmission*, December 2018

ISP Panel

It has been suggested that AEMO should establish an ISP Panel to advise it in preparing the ISP. The Energy Council supports increased consultation and sees no reason why existing fora, such as the NEM Wholesale Consultative Forum and the Forecasting Reference Group *inter alia*, cannot be used for this purpose, since there is a risk that a separate panel may have a subset of stakeholders, which may not represent all interested parties.

Interactions with TNSP Planning Processes

AEMO's development of the ISP will need to align with the TNSPs' planning processes. The Energy Council is therefore supportive of the ESB's proposals to ensure that the processes marry, and that AEMO's National Transmission Planner costs are borne by the TNSPs. TNSP cost allocation has always been closer to the "reflective of involvement" principle of AEMO cost recovery than the present arrangements, and will become more so as the ISP absorbs some of the TNSPs' initial planning activities.

Governance Review

The Energy Council notes that there is no scheduled assessment of the new ISP framework's efficacy after it has been implemented. It is suggested that a governance review should be conducted by the Australian Energy Market Commission after the proposed new rules have been in effect for three years.

Conclusion

In conclusion, the Energy Council believes that it will be helpful to streamline the processes necessary for the assessment of transmission projects, but rigorous assessment, in compliance with the RIT-T, of individual projects must be maintained, in order to ensure that appropriate development occurs, and speculative costs are not incurred to the detriment of consumers.

Any questions about this submission should be addressed to the writer, by e-mail to Duncan.MacKinnon@energycouncil.com.au or by telephone on (03) 9205 3103.

Yours sincerely,



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