

System security network support payment guideline

For ex-ante reviews of draft system security
network support payment contracts

AER draft guideline

October 2024

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Have your say

Interested parties are invited to make written submissions to the AER regarding our draft System Security Network Support Payment Guideline for ex-ante contract reviews by close of business, 30 October 2024.

Submissions should be sent electronically to anthony.weir@aer.gov.au. Alternatively, you may mail submissions to:

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We ask that all submissions sent in an electronic format are in Microsoft Word or other text readable document form. We prefer that all submissions be publicly available to facilitate an informed and transparent consultative process. We will treat submissions as public documents unless otherwise requested. All non-confidential submissions will be placed on the AER's website.

For further information regarding the AER's use and disclosure of information provided to it, see the ACCC/AER Information Policy. We request parties wishing to subject confidential information:

- clearly identify the information that is the subject of the confidentiality claim
- provide a non-confidential version of the submission in a form suitable for publication.

If you have enquiries about this paper, lodging a submission or would like to meet with us to discuss issues raised in this paper, please contact anthony.weir@aer.gov.au

1 Introduction

The Australian Energy Regulator (AER) exists to ensure energy consumers are better off, now and in the future. Consumers are at the heart of our work, and we focus on ensuring a secure, reliable, and affordable energy future for Australia as it transitions to net zero emissions.

As the independent regulator, the national energy objectives guide the AER's work in the long-term interests of consumers.

The purpose of this Guideline is to outline how the AER will determine whether proposed expenditure for a system security network support (SSNS) service, as set out in a draft contract between a transmission network service provider (TNSP) and SSNS service provider (i.e. typically a generator or battery), is consistent with the operating expenditure objectives, criteria and factors and network support pass through factors in the NER.¹ The AER is required to make these determinations and publish this Guideline under the [Improving Security Frameworks for the Energy Transition Rule Change](#), published on 28 May 2024.

1.1 The AER's role

The *Improving Security Frameworks for the Energy Transition Rule Change* (the ISF Rule), published on 28 May 2024, changes the way TNSPs recover the costs of SSNS payments made for system security services. System security services include system strength, inertia, and network support and control ancillary (NCAS) services typically provided by a synchronous generator or battery to ensure the power system is secure as we transition to more renewable generation.

In addition to introducing a revised method for forecasting and recovering TNSP expenditures for SSNS services through a new annual transmission pricing process² and revisions to the existing ex-post network support payment (NSP) pass through process,³ the ISF Rule:⁴

- allows (but does not require) TNSPs to seek an ex-ante AER review that proposed expenditure for a SSNS payment, or a methodology for such a payment (as set out in a draft contract between the TNSP and SSNS provider (e.g. a generator or battery)) will likely be prudent and efficient (i.e. consistent with the operating expenditure objectives, criteria and factors, and amended NSP pass through factors)

¹ NER, 6A.6.6A.

² ISF Rule, 6A.23.3(h)(2). This rule change does not require a change to the AER's existing [Transmission Pricing Methodology guidelines](#).

³ ISF Rule, 6A.7.2(i)(3a). The AER Guideline [Procedural guideline for preparing a transmission network support pass through application June 2011](#) outlines the existing (pre-ISF Rule) process for undertaking annual NSP pass throughs. The AER is currently considering what, if any updated may be needed to this guideline to reflect the modified annual cost pass through approach in the ISF Rule.

⁴ ISF Rule, NER 6A.6.6A.

- requires the AER to publish a guideline by 1 December 2024, setting out a process for the AER to undertake these ex-ante reviews on the prudence and efficiency of expenditure for a proposed payment or payment methodology in relation to select (i.e. significant) draft SSNS payment contracts.

Enabling TNSPs to seek an AER review of significant draft contracts aims to improve TNSPs' confidence in their ability to recover efficient operational costs, thereby helping to level the playing field between network and non-network solutions to meeting system security requirements.⁵

This Guideline sets out how the AER undertakes these ex-ante reviews of draft SSNS payment contracts. In particular, it sets out:

- the nature of the determination and the NER criteria we must have regard to
- the processes, eligibility criteria and thresholds, timing, consultation processes and information the AER may have regard to when undertaking an ex-ante review of a draft contract
- the information TNSPs must provide when preparing an application for a review.

We encourage TNSPs to engage with us before applying for determinations dealt with in the Guideline. This will help to ensure that parties are making high quality applications, that are appropriately justified by relevant information included with the application.

1.2 Consultation on this draft guideline

The AER has engaged with stakeholders including transmission network service providers (TNSPs) to inform the development of this draft Guideline. This has included:

- a TNSP consultative forum
- one-on-one discussions with TNSPs and consumer representative groups.

In developing this Guideline, we have also considered issues raised in consultations between the AER, TNSPs, the Australian Energy Market Commission (**AEMC**) and AEMO, including through the regular Market Bodies System Strength Implementation Working Group. These consultations have informed the development of the related *Efficient Management of System Strength Framework* draft guidance note currently being consulted on by the AER in parallel with this Guideline.⁶

We are now seeking feedback from TNSPs and other interested stakeholders on this Guideline. This includes, but is not limited to, the questions set out in the box below.

Consultation questions

⁵ AEMC, *Rule determination, National Electricity Amendment (Improving security frameworks for the energy transition) Rule 2024*, 28 March 2024, p. 42.

⁶ The purpose of the AER's draft *System Strength Guidance Note* is to provide guidance to aid TNSPs to proactively plan for, and procure, system strength under the [Efficient management of system strength on the power system rule change](#), made on 21 October 2021.

- What are your views on the Guideline? What, if any, amendments would you suggest?
- What, if any, additional issues might the Guideline need to consider?

1.3 Next steps

The AER released this draft Guideline on 9 October 2024 and calls for submissions by 30 October 2024.

The AER will consider stakeholders' views and publish the final Guideline by 1 December 2024.

1.4 Confidentiality

The AER's obligations regarding confidentiality and the disclosure of information provided to it by a TNSP is governed by the *Competition and Consumer Act (2010)*, National Electricity Law and the NER.

This Guideline discusses information that may be commercial in confidence and / or confidential. When a TNSP provides us with information in an application seeking an ex-ante review or in subsequent information provided, it can claim confidentiality over any part of the information. To make a claim for confidentiality, we ask that the confidential information is clearly identified, and reasons are provided to support the confidentiality claim. Any such information must be of a genuinely confidential in nature and not otherwise publicly available. We encourage parties to limit confidentiality claims to the extent possible, so that the AER can conduct reviews as transparently as possible.

Further details on how TNSPs should make confidentiality claims over information submitted to us is provided in the [AER's Confidentiality Guideline](#). Further guidance on how the AER collects, uses and discloses confidential information is available in the [ACCC/AER Information Policy](#).

1.5 Structure of the guideline

The Guideline is structured as follows:

- Chapter 2: Regulatory framework for ex-ante reviews of SSNS payment contracts
- Chapter 3: Processes, timelines, thresholds and information we may have regard to
- Chapter 4: Information requirements to make an application
- Appendix A: TNSP decision tree on contracting system security network support services

1.6 Process for revision

The AER may amend or replace this Guideline from time to time. This Guideline is not subject to the Transmission Consultation Procedures under NER 6A.20.

2 Regulatory framework

This chapter outlines the regulatory framework established under the ISF Rule for the AER's ex-ante review of draft SSNS payment contracts.

2.1 Purpose of the determination

The purpose of the ISF Rule clause NER 6A.6.6A is to enable TNSPs to seek a determination from the AER that a proposed payment or payment methodology in a draft SSNS payment contract likely meets the relevant opex and network support payment criteria, which we collectively refer to as 'prudence and efficiency'.

Box 1 lists the full NER requirements under clause 6A.6.6A, including the NER criteria we must have regard to in making an ex-ante determination, and the nature of the SSNS payment Guideline.

The AEMC states that the aims of these ex-ante reviews include:⁷

- providing a level of comfort to TNSPs, before signing the contract, about the AER's expectations and approaches to making ex-post assessments of expenditures incurred under the executed contract (i.e. as part of the AER's subsequent NSP pass through determinations). This should improve TNSPs' confidence when entering into a contract that they will be able to recover efficient operational costs.
- improving the efficiency and ability of TNSPs to contract SSNS services
- leveling the playing field between network and non-network expenditure in meeting system security needs.

Clauses 6A.6.6(e)(13a) and 6A.7.2A(i)(3a)(iii) also requires the AER to take into account an ex-ante determination made on a draft contract in any future related NSP pass through determination for costs incurred under the same contract.

Box 1: NER clause 6A.6.6A AER power to make advance determination with regard to future operating expenditure

- (a) The AER may, on application by a Transmission Network Service Provider, make a determination that expenditure for a proposed system security network support payment, or a methodology for such payment, specified in the determination, will be consistent with:
- (1) the operating expenditure objectives (6A.6.6(a));
 - (2) the operating expenditure criteria (6A.6.6(c));
 - (3) the operating expenditure factors (6A.6.6(e)); and
 - (4) the factors in clause 6A.7.2(i) relevant to a system security network support payment.

⁷ AEMC, *Rule determination, National Electricity Amendment (Improving security frameworks for the energy transition) Rule 2024*, 28 March 2024, pp. 51-52.

- (b) An application submitted by a Transmission Network Service Provider under paragraph (a) must comply with any relevant requirements in the system security network support payment guidelines.
- (c) The AER may (but is not required to) consult in a manner it considers appropriate on the application submitted under paragraph (a) before making a determination.
- (d) A determination made by the AER under paragraph (a) must be consistent with the system security network support payment guidelines.
- (e) The AER must make and publish, and may amend, guidelines (system security network support payment guidelines) that set out:
 - (1) the information to be included in an application submitted under paragraph (a);
 - (2) any eligibility criteria or thresholds that will apply for system security network support payments before the AER will accept an application for under paragraph (a);
 - (3) the process and timeframes for the AER to make its determination under paragraph (a); and
 - (4) any other matters the AER considers relevant.
- (f) The transmission consultation procedures do not apply to the making or amendment of the system security network support payment guidelines.

2.2 Nature of the determination

The opex objectives, criteria and factors under 6A.6.6A (a)(1)-(3) are the same criteria the AER is required to assess when deciding whether to accept a TNSP's proposed forecast opex in a revenue determination under clause 6A.6.6. In the context of a revenue determination, we interpret these criteria together as requiring consideration of whether forecast opex can be reasonably considered to be 'prudent and efficient'.

Clause 6A.6.6A(a)(4) also requires the AER to determine whether the expenditure or payment methodology in a draft contract is consistent with the factors in clause 6A.7.2(i) relevant to a SSNS pass through determination. We consider that all the factors in clause 6A.7.2(i) would be relevant to a SSNS payment ex-ante review, with the exception of subclause 6A.7.2(i)(2) and (3).⁸

We will interpret the factors under NER 6A.6.6A (a))(1)-(4) together as requiring that the AER can, on application from a TNSP, make a determination on whether a SSNS payment, or a methodology for such a payment, as described in a draft contract provided by the TNSP,

⁸ Clause 6A.6.6A(a)(4) does not explicitly specify the factors in clause 6A.7.2(i) that are relevant to a system security support payment. We consider that the factors in clauses 6A.7.2(i)(2) and (3) are not relevant to a system security support payment due to the opening text "except to the extent subparagraph (3a) applies". The meaning of this expression is that if subparagraph (3a) is applicable, subparagraph (2) and (3) does not apply. As subparagraph (3a) specifically relates to system security support payment, it would always be a relevant factor to the AER's assessment under clause 6A.6.6A(a)(4). It follows that subparagraphs (2) and (3) would not be regarded as relevant factors to a system security network support payment for the purposes of the ex-ante determination under clause 6A.6.6A(a)(4).

is likely to result in future expenditure which can be reasonably considered to be prudent and efficient.

We note that we do not approve a specific forecast amount of expenditure as part of an ex-ante review, rather we assess if the proposed payment or payment methodology in the draft contract is likely to result in a prudent and efficient amount of expenditure if the contract terms are followed. We are also not required to provide a view on other terms in the proposed draft contract, or on the efficiency of AEMO's operational enablement of the contract, once executed, to meet real-time system security needs.

2.3 Operationalising clause 6A.6.6A

Chapter 3 sets out how we will implement clause 6A.6.6A, including:

- the processes and timeframes for the AER to make its determinations
- eligibility criteria and thresholds that will apply before the AER accepts an application
- the information we may have regard to in order to:
 - determine that a draft contract is eligible for review (under 6A.6.6A(e)(2))
 - make a determination on the prudence and efficiency of a proposed payment or payment methodology in a draft contract (under 6A.6.6A(a))
- and any other matters the AER considers relevant.

3 Processes, timelines, thresholds and information we may have regard to

This chapter outlines the processes, timelines, eligibility criteria and thresholds, and information we may have regard when undertaking an ex-ante review of a draft SSNS payment contract.

Appendix A of this Guideline provides a flowchart showing key decision points a TNSP may need to navigate in contracting SSNS services, and how this Guideline, and the AER's System Strength Guidance Note, may help inform TNSP decision making.⁹

3.1 Pre-application

We encourage TNSPs to engage with us before applying for a determination. This will help to ensure that the TNSP is making an eligible application, and providing all the relevant information in the application to enable a timely decision.

Early engagement with the AER may also assist a TNSP to determine if a network support payment, or payment methodology is unlikely to be considered prudent and efficient and further options should be investigated. This may include whether a TNSP should reapproach the market or consider alternatives to contracting an offer (**Appendix A**).

3.2 Lodging an application – timing

Applications to the AER for an ex-ante draft contract review should be made after the regulatory investment test for transmission (RIT-T)¹⁰ and any related regulatory processes to identify the preferred option have been completed, but prior to contract execution.

RIT-Ts should be complete, including the resolution of disputes to enable confirmation that the RIT-T does not need to be redone due to a material change in circumstance (for example, if contract costs are materially above the assumptions in the RIT-T, such that the preferred options could change).

Tender processes should be largely finalized to enable TNSPs to provide information on costs and pricing methodologies in an application that is likely to reflect the contract that is executed.

3.3 Lodging an application – eligibility & thresholds

Consistent with 6A.6.6A(b), an application submitted by a TNSP must comply with all relevant requirements in this Guideline, including any eligibility criteria or thresholds that apply before the AER will accept an application for review under paragraph 6A.6.6A(e)(2).

⁹ The flow chart also shows how the AER's *Efficient Management of System Strength Framework* draft guidance note being developed in parallel with this Guideline, may inform TNSP decisions to proactively plan for, and procure system strength services under the *Efficient management of system strength on the power system* rule change, made on 21 October 2021.

¹⁰ Where required.

Box 2 lists the eligibility criteria and materiality threshold that the AER will apply under paragraph 6A.6.6A(e)(2) to determine if we will accept an application for review.

The eligibility criteria and materiality threshold will ensure that the AER has all relevant information needed to begin to assess an application, and that reviews will target only financially significant SSNS payment contracts as intended by the ISF Rule.

Chapter 4 outlines the type of information and supporting documentation TNSPs must include in an application to demonstrate a draft contract meets the eligibility criteria and the threshold set out in **Box 2**.

Box 2: Eligibility criteria and materiality threshold to make an application for an ex-ante review

Eligibility criteria

- The application must be made after completion of all relevant regulatory processes (including RIT-T appeals and material changes in circumstances) and before a contract is executed.
- All services in the draft contract being reviewed must be ‘preferred options’ under a completed RIT-T, or a ‘secondary option’ approved by the AER on the basis it is a lower cost option than the RIT-T preferred options.
- The application must include the relevant information outlined in Chapter 4 of this Guideline.

Materiality threshold

- The draft contract’s expected average annual payment must exceed 1% of AER approved unsmoothed revenues in a regulatory year for the current regulatory control.

3.4 Consultation on an application

6A.6.6A(c) states that the AER may, but is not required to, consult in a manner it considers appropriate on the application before making a determination.

We propose to adopt a similar consultation approach as used for pass through applications under the NER.¹¹ In the case of an ex-ante draft contract review, this means the AER may consult with the relevant TNSP and such other persons as the AER considers appropriate, on any matters arising out of application as the AER considers appropriate.

In practice, the consultation process can include:

- publishing the application with appropriate redactions for confidential and commercial-in-confidence information
- calling for submissions on the application

¹¹ NER 6A.7.3 (i).

- using information requests and targeted consultation with the TNSP or other parties as necessary
- publishing the determination, with appropriate redactions for confidential and commercial-in-confidence information.

3.5 Assessing prudence and efficiency

Consistent with clauses 6A.6.6A (a)(1)-(4), this section describes the information the AER may have regard to when determining whether a SSNS payment, or a payment methodology described in a draft contract provided by the TNSP, is likely to result in future expenditure that can be reasonably considered to be prudent and efficient. The specific information the AER considers in any assessment will vary on a case by case basis depending on the circumstances of the TNSP and the nature of the contract being reviewed.

Prudence is based on providing sufficient evidence and information to enable the AER to establish that there is a reasonable need to include the proposed SSNS payment or payment methodology in the draft contract being reviewed.

Information we could have regard to determine this includes whether the payment and / or payment methodology in a draft contract is for a SSNS service that:

- is required to comply with the minimum level of system security identified by an AEMO shortfall forecast
- has been identified as a 'preferred option' through the RIT-T process, or an amendment to the process or a 'secondary option' approved by the AER on the basis it is a lower cost option than the RIT-T preferred options

AEMO has identified payment components that a SSNS payment contract should include for enablement, including availability, activation and usage payments.¹² We could also have regard to the prudence of the components of a proposed payment, the mix or structure of the components, and conditions for triggering a payment or component of a payment. For example, a draft contract may include unnecessary fixed cost components, or triggers for costs that could be considered unnecessary, or overly ambiguous and likely to result in unnecessary costs being incurred.

Efficiency is based on providing sufficient evidence and information to enable the AER to establish that the payment or payment methodology in a draft contract is reasonably likely to reflect efficient or least cost.

Information we could have regard to determine this includes the extent to which the payment and / or payment methodology for a given service:

- is the outcome of a competitive approach to market, or where a competitive process is not available, reflects the least cost the TNSP could reasonably achieve in the circumstances through a direct / negotiated approach to a SSNS service provider
- is not unreasonable, having regard to:

¹² AEMO, [Provisional Security Enablement Procedure \(Improving Security Frameworks\)](#), 30 June 2024.

- the economic cost and / or other relevant cost information used in the RIT-T process, including any early or indicative quotes from SSNS service suppliers (e.g. generator or battery)
 - the compensation that the SSNS service supplier (e.g. generator or battery) would otherwise receive in similar circumstances if directed on by AEMO, having regard to AEMO's direction compensation recovery approach¹³
 - payments and / or payment methodologies for similar services in similar circumstances, including in other draft SSNS payment contracts reviewed by the AER or other publicly available cost information
- does not include unreasonable costs, cost components, mix of cost components, or triggers (i.e. there is no evidence of unnecessary costs or an unreasonable risk that triggers of cost components will lead to unnecessary costs).

Chapter 4 outlines the type of information and supporting documentation TNSPs must include in an application to demonstrate a payment, or a payment methodology in a draft contract is prudent and efficient.

3.6 Timeframe for decision

We propose to adopt a similar timeframe for a decision as set out by the NER for assessing cost pass through applications.¹⁴ In the case of an ex-ante draft contract review, the AER will make a determination within 40 business days from the later of the date it receives an application that meets the eligibility criteria and materiality threshold out in section 3.2, or the date it receives any additional information sought by the AER in a subsequent information request.

This timeframe aims to balance the need to ensure that a draft contract subject to review can be executed in a timely manner, while allowing for any consultation processes that the AER may carry out as part of the determination process, including seeking further information from the relevant TNSP, or other parties as necessary.

If the AER is satisfied that the making of a determination involves issues of such complexity or difficulty that the 40-business day limit should be extended, the AER may extend that time limit by a further period of up to 60 business days. In this case, the AER will advise the TNSP in writing of the additional time required. It is expected this option to extend the timeframe for a decision will only be used in exceptional circumstances.

¹³ <https://aemo.com.au/en/energy-systems/electricity/national-electricity-market-nem/data-nem/settlements-data/direction-compensation-recovery>

¹⁴ This timeframe is consistent with the timeframe for a cost pass thought determination under NER clause 6A.7.3(e).

4 Information requirements to make an application

Consistent with 6A.6.6A (e)(1), this section sets out the information a TNSP must include in an application for an ex-ante review of a draft SSNS payment contract:

- to demonstrate the draft contract meets the eligibility criteria and threshold set out in section 3.3
- to demonstrate a payment or payment methodology in a draft contract is prudent and efficient as set out in section 3.5.

4.1 Demonstrating eligibility and thresholds

The AER considers that the TNSPs must provide the following information to demonstrate that an application meets the **eligibility criteria** for an ex-ante review:

- all relevant details for the draft contract, including the SSNS services being engaged, the service provider(s), the proposed payments and payment methodologies in the draft contract, and details of any other costs, costs components and triggers for all potential expenditures included in the draft contract
- a statement with supporting documentary evidence demonstrating that:
 - the TNSP has completed all relevant regulatory processes (including RIT-T appeals and any material change in circumstances) and that the draft contract has not yet been executed
 - all SSNS services in the draft contract are ‘preferred options’ under the completed RIT-T process, or ‘secondary options’ approved by AER as a lower cost option than RIT-T preferred options under ‘material change in circumstances’
 - all required information outlined in Chapter 4 of this Guideline has been provided.

To determine that a draft contract meets the **threshold** the TNSP must provide the AER with details of all assumptions and calculations used to show that the draft contract’s expected average annual payment is forecast to exceed 1% of the TNSP’s AER approved unsmoothed revenues in a regulatory year for the current regulatory control.

This information should be presented in a spreadsheet that shows how the draft contract’s expected average annual SSNS payment was calculated, the basis of the AER approved unsmoothed revenues, and include the application of CPI, and estimates of the time cost of money. The spreadsheet should show all formulas and input data.

4.2 Demonstrating prudence and efficiency

In addition to the information provided in 4.1, the AER considers that the TNSPs must provide the following information to demonstrate a payment or payment methodology in a draft contract is **prudent**:

- an explanation with supporting documentary evidence outlining why the TNSP believes contracting the SSNS service(s) in the draft contract is prudent (necessary). This can include:

- a statement with supporting documentary evidence showing that the payment and / or payment methodology in the draft contract is for a SSNS service(s):
 - o required to comply with the minimum level of system security identified by the TNSP as informed by an AEMO forecast
 - o that has been identified as a ‘preferred option’ through the RIT-T process, or an amendment to the process or a ‘secondary option’ approved by the AER on the basis it is a lower cost option than the RIT-T preferred options.

The TNSP must also provide an explanation and supporting documentary evidence to demonstrate the prudence of the structure of the components of the payments, and the conditions for triggering a payment or component of a payment in the draft contract. For example, unnecessarily large cost components, or unnecessary cost components may be considered not prudent. Likewise, triggers for costs that could be considered unnecessary, or overly ambiguous and likely to result in unnecessary costs being incurred may be considered not prudent.

The AER considers that the TNSPs must provide the following information to demonstrate a payment or payment methodology in a draft contract is **efficient**:

- an explanation with supporting documentary evidence outlining why the TNSP believes the payment and / or payment methodology in a draft contract is efficient. This can include:
 - a description of a competitive tender or procurement process used to establish the payment and / or payment methodology in a draft contract, including the type of approach(es) used, the offers received, any subsequent negotiations or actions taken to achieve a competitive payment and / or payment methodology
 - where a competitive process was not available, a description of why a competitive process was not possible, the approach(es) to supplier(s) used in place of a competitive process, the offer(s) received, what steps the TNSP took to achieve the least cost offer, including any subsequent negotiations or actions to achieve the best available offer in the circumstances
 - an explanation of why the payment methodology or cost structure and triggers used in the draft contract are efficient and do not result in unreasonable costs, or an unreasonable risk of unnecessary costs.

Where a TNSP seeks AER review of a draft contract that is part of a portfolio of draft contracts, the TNSP should consider what / if any information from the other draft contracts in the portfolio (which may not be eligible for an ex-ante review) may be required to enable the AER to assess the prudence and efficiency of the draft contract under review.

Glossary

Term	Definition
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
CPA	Contingent Project Application
IBR	Inverter-Based Resources
ISP	Integrated System Plan
NEO	National Electricity Objective
NER	National Electricity Rules
PACR	Project Assessment Conclusions Report
REZ	Renewable Energy Zone
RIT-T	Regulatory Investment Test for Transmission
SSSP	System Strength Service Provider
TAPR	Transmission Annual Planning Report
TNSP	Transmission Network Service Provider

Appendix A: TNSP decision tree on contracting system security network support services

