

# **Attachment 3: Rectification actions and options report**



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## 1. Purpose and key messages

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This Attachment forms part of Transgrid's application to reopen the 2023-2028 Revenue Determination in accordance with clause 6A.7.1 of the NER (**Application**).

The event referred to in this Application is Contract Failure which meant that PEC would not be completed by the competitively procured contractor, Secure Energy Joint Venture (**SEJV**), under the existing Engineering, Procurement and Construction (**EPC**) contract.

The purpose of this Attachment is to explain the options considered and steps taken by Transgrid to rectify the Contract Failure and achieve the best outcome for consumers. In December 2024, Transgrid executed an Incentivised Completion Cost (**ICC**) contract with Elecnor Australia<sup>1</sup> as contractor, having explored all credible options and conducted detailed net market benefit analysis.

### Key messages

- In response to the Contract Failure, Transgrid considered the practical, legal and project implications as well as the impact on the net benefits for consumers if Transgrid attempted to enforce the EPC contract. Transgrid concluded that this was likely to result in Elecnor Australia entering voluntary administration, with significant adverse consequences for the project (delays and increased costs) and consumers. Instead, Transgrid took immediate steps to maintain project continuity including by making additional payments to Elecnor Australia and by committing additional resources to the project outside the terms of the EPC contract.
- In order to make an informed assessment of all available options, Transgrid undertook a tender process to try to identify a potential alternative contractor. Following an extensive process, it was evident that this pathway would not deliver a cost effective or timely outcome for consumers. Instead, the negotiation of new contract terms with Elecnor Australia would likely produce a lower price and avoid additional delays of at least 12 months in project delivery that would arise if an alternative contractor were appointed. An additional 12-month delay was estimated to increase the net project costs by between \$550 million and \$937 million and substantially decrease the incremental net market benefits.
- In order to confirm that a new contract with Elecnor Australia would be the most prudent and efficient option, Transgrid undertook a detailed analysis of all potential options. An important component of this analysis was a net market benefit assessment. This confirmed that the proposed contracting approach with Elecnor Australia would maximise the net market benefit, which is expected to be \$964 million in present value terms.

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<sup>1</sup> Technically, the 'contractor' under the ICC contract remains Secure Energy Joint Venture; however, for ease, Transgrid will refer to Elecnor Australia (being the only solvent member of SEJV) as the contractor for the remainder of this Attachment.

- At each stage of the process, Transgrid has acted prudently and efficiently to minimise the cost impact of the Contract Failure and to secure the best outcome on behalf of consumers.

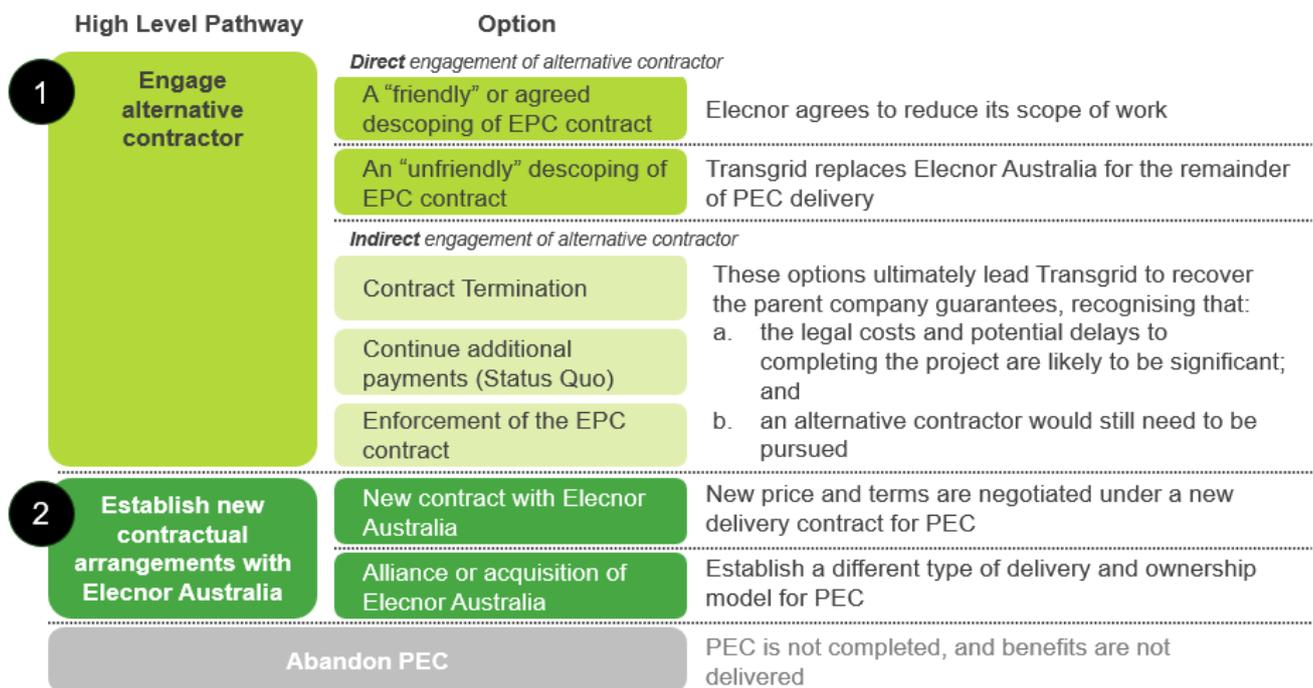
## 2. Overview of pathways and potential options

As explained in the main Application, Transgrid actively pursued two high-level pathways to deliver PEC following the failure of the EPC contract:

- engage an alternative contractor, and
- establish new contractual arrangements with Elecnor Australia.

For each of these pathways, a number of specific options were considered as shown in Figure 1 below.

Figure 1: High level pathways and options



In the sections below, further information is provided on the following:

- immediate and ongoing actions taken by Transgrid to maintain project continuity and the value those actions provided in terms of securing optionality and avoiding project delays
- the costs and risk of enforcing and possibly terminating the EPC contract, including appeals and counterclaims
- Transgrid's engagement with alternative contractors, and
- the outcome from the options analysis, which demonstrates that the ICC contract maximises net market benefits for consumers.

### 3. Maintaining project continuity

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Following the Contract Failure, Transgrid recognised the considerable value that would be secured by maintaining project continuity, including:

- PEC's status as an actionable Integrated System Plan (**ISP**) project meant that any delay would compromise the most efficient path to maintain reliable and secure electricity supply, as the Australian Energy Market Operator (**AEMO**) had stated that all actionable projects should progress "as urgently as possible"<sup>2</sup>.
- Project delays and increased costs when combined, would significantly decrease the incremental net market benefits that PEC is expected to provide.
- Securing the full range of rectification options available to Transgrid and providing sufficient time to examine those options.
- Maintaining Transgrid's contractual rights, including potential access to Elecnor Australia's parent company guarantee, by continuing to make scheduled payments in accordance with the EPC contract.
- Taking steps to drive productivity and performance improvements from Elecnor Australia during the intervening period between Contract Failure and a longer-term rectification solution.
- Enabling Transgrid to introduce measures to better manage and mitigate Elecnor Australia's insolvency, should it occur.

To ensure project continuity, Transgrid negotiated an Advance Payment Deed (**APD**) which operated from December 2023 through to May 2024 and contained the following rights and obligations:

- Transgrid to make additional payments to Elecnor Australia up to a cap of \$200 million (nominal) and Elecnor Australia's parent company to pay Elecnor Australia \$25 million (nominal) to pay suppliers, subcontractors and blue and white-collar employees.
- A Director of Elecnor Australia was required to declare that these additional payments were only being used to pay suppliers, subcontractors and blue and white-collar employees.
- Transgrid would have open book access to verify that additional payments were only used for subcontractor and supplier invoices.
- Elecnor Australia to provide specific monthly progress reports to Transgrid setting out the status of the works and progress made from these additional payments to verify value for money.
- Elecnor Australia could receive a bonus payment of \$25 million (nominal) to complete SP1 by 7 April 2024.
- Elecnor Australia to provide to Transgrid novation deed polls and copies of all subcontracts with key subcontractors and copies of all design documents. These steps would mitigate delays, should Elecnor Australia be unable to complete the works.

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<sup>2</sup> AEMO, [2024 Integrated System Plan](#), June 2024, p. 16.

In addition to the payments made in accordance with the APD, Transgrid also committed additional resources to the project to ensure that progress continued to be made and to assist Elecnor Australia in rectifying its performance issues. As explained in Attachment 2, Transgrid ramped up its project resources during the period of the APD and provided employees to fill the roles of Site Managers, Construction Managers and Field Technical Staff, which supported Elecnor Australia in achieving practical completion of SP1. These resource commitments were outside those required in an EPC contract.

Transgrid also commenced contingency planning in case Elecnor Australia became insolvent, to ensure that the project team had the resources, access to designs, novated key subcontractors' contracts and other project data necessary to continue work on the project in a safe manner.

## 4. Contract enforcement and possible termination

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Following the Contract Failure, Transgrid considered whether to exercise its rights to enforce the EPC contract.

Under the terms of the EPC contract, SEJV was required to design, construct, test and commission PEC as well as rectify any defects. SEJV had provided bank guarantees with a total value of 10% of the contract price as security for its performance under the EPC contract. In addition, Elecnor Australia and Clough Limited each provided parent company guarantees up to a value of █████ of the contract price (being the limit of SEJV's liability under the EPC contract). Transgrid could access these performance securities in various circumstances, including a breach of the EPC contract by SEJV.

Transgrid contemplated how the parent company guarantee could be enforced. A parent company guarantee provided Transgrid with two possible courses of action, one being to seek performance and the other to seek payment. If Transgrid were to seek performance, whilst it would be legally possible to seek to enforce performance of the EPC contract with Elecnor Australia's parent company, this would not be practical, given that Elecnor Australia's parent company had no capacity to perform the works in Australia, other than via Elecnor Australia. The second course of action would be to seek payment, however, Transgrid needed to first seek recovery from Elecnor Australia. Given that Elecnor Australia had limited assets, it was almost certain that Transgrid would subsequently need to seek payment from Elecnor Australia's parent company. In both circumstances, there would be 'procedural hurdles' in attempting to enforce performance and/or secure proceeds and the requirement to pursue the matter through the courts in Australia and Spain. This process could take up to seven years.

Transgrid concluded that attempting to enforce the EPC contract would lead to counterclaims and appeals from Elecnor Australia and Elecnor Australia's parent company, and for Elecnor Australia to either enter voluntary administration or abandon the project. Transgrid considered that the likelihood of Elecnor Australia continuing to deliver PEC whilst litigation was ongoing was low. Therefore, the most likely outcome for PEC was that Transgrid would need to procure a new contractor, impacting PEC as follows:

- Project works would cease with immediate effect and equipment and materials would be removed from sites.
- No warranties would be provided in relation to partially completed works.
- Background intellectual property and experienced project workers would be lost.
- A replacement contractor would be reluctant to complete the project without significant indemnities, as later confirmed by Transgrid through market testing.
- Significant further project delays of at least 12 months would be expected, resulting in a loss of project benefits to the detriment of consumers.

Furthermore, if Transgrid had terminated the EPC contract, the practical challenges of completing the project with a new contractor would be significant, once the tender process was completed, as summarised below:

- **Extended mobilisation period:** A new contractor would need a significant mobilisation period to review and understand the design and establish key management documents, including the Construction and Environmental Management Plan (**CEMP**), which would need to be approved by the Department of Planning, Housing and Infrastructure.

- **Re-engaging suppliers and subcontractors:** Whilst mobilising, the new contractor would need to re-engage with suppliers and subcontractors that, if available after the project restart (as they may have secured other work in the interim in a very active market), would likely have sought to settle any claims unresolved by Elecnor Australia and have sought additional costs associated with the time delay, such as escalation, wage growth and material price increases. Given the high reliance on overseas workers, it is likely that new visas would also be needed, along with a new Labour agreement, as was required of Elecnor Australia, following the insolvency of Clough Limited.
- **Lower initial productivity:** The new contractor would face a relatively steep learning curve before achieving target productivity levels and would have likely encountered missteps as works progressed, as well as issues caused by the site being closed for at least a year.
- **Interface risks:** Engaging a new contractor following contract termination would introduce interface risks, exposing Transgrid and consumers to increased costs and delay. These interface risks arise because partially completed work, and existing defects, would need to be managed by the new contractor. As a first step, any partially completed works would need to be reviewed by the new contractor to identify any defects or safety risks and may lead to some works being demolished and reconstructed. Similarly, issues arise in relation to large specialist equipment that had not been fully commissioned or energised, which would require commissioning/energisation processes to be restarted. It is also likely that warranties would have expired due to the delay in recommencing works.

For these reasons, Transgrid did not consider contract enforcement and/or termination to be in consumers' interests even though it would have mitigated Transgrid's financial commitment in maintaining project continuity. Nonetheless, the option of contract enforcement, potential termination and litigation to pursue damages under the parent company guarantee remained available to Transgrid and therefore provided leverage in its contract negotiations with Elecnor Australia.

## 5. Tender for an alternative contractor

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While Transgrid and Elecnor Australia were negotiating a friendly descope option, Transgrid with Elecnor Australia's parent company's consent, undertook a tender process for a potential alternative contractor to deliver the remaining works for Separable Portion 2 (**SP2**). As already noted, this pathway was actively considered by Transgrid as an alternative to negotiating new contractual arrangements with Elecnor Australia. Transgrid's overarching strategy was to undertake a robust procurement process, taking into account the current realities of the project, with a view to ensuring project completion in a prudent and efficient manner to achieve the best outcome for consumers.

This tender followed a conventional process, including the engagement of probity advisors, issuing of returnable schedules, holding of workshops with each tenderer and the application of a standard evaluation criteria. Transgrid commenced the tender process in May 2024. It involved three phases: market sounding, Expression of Interest (**EOI**) and Request for Tender (**RFT**), which are described in turn below.

### 5.1 Market sounding

Transgrid undertook a confidential market sounding process in May 2024 to:

- brief selected market participants on the project status and requirements, and
- seek confirmation from the selected market participants on their capabilities, optimal delivery solution and contracting methodology in order to understand the market appetite, capacity, and capability to step into a project where construction was 47% complete and under unusual circumstances.

Transgrid approached [REDACTED]. All entities expressed interest in being part of the procurement process, either as single entities or as Joint Ventures.

From initial market soundings, there was interest in the project from reputable tier 1 contractors, and most had electricity transmission experience. However, there was no appetite for a fixed price contract given the limited procurement timetable, unknown risks and in relation to a project that was partially complete which introduced inherent risks, uncertainties and practical challenges of transferring to an alternative contractor. Based on this engagement, Transgrid recognised that an alternative contractor would likely assume little or no risks and certainly nowhere near the same level of risk that SEJV had assumed under the EPC contract.

### 5.2 Expression of Interest

The purpose of the EOI phase was to shortlist applicants to participate in the RFT phase of the procurement process. During this phase, Transgrid sought formal expressions of interest to deliver the balance of SP2 from participants, and information on their experience and capabilities.

To be shortlisted, contractors would need to demonstrate the following attributes:

- a strong track record of successfully delivering major projects in Australia
- demonstrable project leadership resources in Australia to allocate to the project
- strong health and safety management
- the ability to manage costs and improve the performance of subcontractors, which should reduce the cost through time related savings, and

- strong site leadership and other typical management services required to deliver long linear infrastructure projects.

This approach was designed to minimise the impact on schedule and cost and maximise competition within the circumstances of a partially completed project. Transgrid selected three contractors to proceed to the RFT, [REDACTED].

### 5.3 Request for Tender

The purpose of the RFT phase was to select the tenderers to participate in the development phase to undertake detailed due diligence of the project activities. In June 2024, Transgrid provided the three tenderers a brief on the project which included details of Transgrid's requirements, the current program, equipment used, register of subcontractors and a proposed contract term sheet.

The RFT submissions were evaluated, and weighted, in accordance with the following RFT evaluation criteria:

- project leadership resources
- management capability to deliver transmission lines and substations
- strong safety management
- proposed development phase approach, 90-day mobilisation plan and transition program, and
- initial pricing for the Managing Contractor services.

Transgrid requested that the tenderers use this information to respond to the terms of its term sheet, develop a commercial position, prepare an approach to construction and transition and consider if another contracting structure could be used. The tenderers submitted responses in July 2024. Transgrid requested the tenderers to advise on the tender period they would need to provide a fixed price (lump sum). Tenderers advised that a tender period of between 18 weeks to at least 26 weeks would be required, subject to the provision of complete project records, but that even then they would not likely be in a position to offer a fixed price. The tenderers also advised that if a fixed price contract structure was used:

- There would be no commitment or certainty from these tenderers that they would remain in the tender. Tenderers indicated that as there was a significant risk in taking over the project from Elecnor Australia. One tenderer stated that their Risk Committee may not approve tendering the works under a fixed price arrangement.
- Tenderers indicated that unless they were able to undertake extensive due diligence on the design prepared by Elecnor Australia, have a complete quality review of works under construction, understand subcontractor arrangements and the program, they would not be able to assess or price the risks associated with PEC. Further, tenderers indicated that even with a suitable procurement and due diligence period, they would likely include a substantial risk premium given the circumstances (though could not provide a firm indication of the quantum at that stage).
- In addition, engaging an alternative contractor would result in an extended delay to the completion of SP2, as a result of the time taken to prepare tender responses, a longer contract negotiation process and the need to re-engage with subcontractors whilst work on SP2 was paused during the contract negotiation.

From the information provided by tenderers in the initial RFT, Transgrid calculated that if SP2 was completed by an alternative contractor, the cost to complete PEC would range between \$4,022 million and \$4,061 million. These figures include the cost for Elecnor Australia to complete SP1 and Substation 1 Part b (**S1b**) and an alternative contractor to complete SP2. This was \$547 to \$586 million higher than the revised fixed price that was ultimately negotiated with Elecnor Australia. As already noted, engaging a new contractor would have delayed the project with a consequential loss of net benefits for consumers. While a further tender phase was planned, this was not completed as Elecnor withdrew their willingness to support a 'friendly descope' and it became evident from the RFT process that bringing in an alternative contractor would not be in the best interests of consumers.

## 6. Options analysis

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Prior to executing the ICC contract with Elecnor Australia, Transgrid undertook a detailed analysis of all potential options to rectify the failure of the EPC contract. An important component of this options analysis was a net market benefit assessment to establish the expected benefits from completing PEC compared to the counterfactual where only SP1 was completed, noting that rectification steps had already been taken to complete SP1.

A summary of the options analysis is set out in Table 1 below, with net market benefits of each option measured against project abandonment as the 'do nothing' or base case option. For each option, a brief description of that option is provided, followed by its associated benefits and an overall assessment. It should be noted that:

- The incremental net market benefit assessment includes forward-looking costs and benefits only, from July 2024 (FY25).
- The total net market benefit considers both sunk and forward-looking costs and benefits.

Transgrid's decision was based on the incremental assessment, but under both assessments the ranking of the options is the same, as the sunk costs and benefits are the same across all options.

*Note that this analysis (including assessment of market benefits) was performed at a point-in-time to support Transgrid's decision making following the Contract Failure. Transgrid has not sought to update the net market benefits or gross market benefits reports (Appendices 3a – 3d) for subsequent market developments (e.g. AEMO's August 2025 Inputs, Assumptions and Scenarios).*

Table 1: Summary of rectification options considered

#	Option	Description	Delivery certainty?	Incremental NMB (\$ m)	Feasibility and key challenges
1	A 'friendly' or agreed descope of EPC contract	Agreement with Elecnor Australia to complete SP1 and descope the remaining components with transitional assistance to Transgrid, tenderers and the new contractor(s).	✓	2,199	Not technically possible.  Option initially suggested by Elecnor Australia in May 2024. Transgrid actively pursued this option and engaged with alternative contractors through an EOI process. Elecnor Australia withdrew its support for this option and, therefore, it was not considered technically possible from that date.
2	An 'unfriendly' descope of EPC contract	Unilateral descope of Elecnor Australia and no transition assistance to Transgrid, tenderers or the new contractor(s).	?	1,720	Technically possible.  Without the assistance of Elecnor Australia, it would take significant additional time to procure a new contractor and require a long mobilisation period before works could commence on site. Equipment, plant and project teams would be lost.  Market testing for Option 1 confirmed that a new contractor would need substantial tender time to commit to fixed pricing along with a substantial risk premium.
3	Contract termination	Transgrid terminates the EPC contract, seeks to recover damages from Elecnor Australia (bank guarantees) and makes demands under the parent company guarantee.	?	1,839	Technically possible.  The key challenge for this option is that it would entail a protracted and costly dispute and litigation with Elecnor Australia and its parent company with counterclaims, appeals, and enforcement required in Spain. Equipment, plant and project teams would be lost whilst Transgrid engages a new contractor to complete the works.
4	New contract with Elecnor Australia	Parties enter into a new contract, including a revised fixed price for Elecnor Australia to complete PEC.	✓	2,389	Technically possible.  Key challenges: <ul style="list-style-type: none"> <li>Negotiating new terms and conditions to provide greater assurances regarding future performance.</li> </ul>

#	Option	Description	Delivery certainty?	Incremental NMB (\$ m)	Feasibility and key challenges
					<ul style="list-style-type: none"> <li>Establishing prudent and efficient costs to complete, in the absence of a competitive tender process.</li> </ul> <p>The total net market benefits (i.e. considering expenditure prior to the event) is \$964 million.</p>
5	Continue additional payments (Status quo)	Transgrid continues to provide additional payments to Elecnor Australia outside the terms of the EPC contract.	?	1,839	<p>Not technically possible.</p> <p>Transgrid had already stepped outside the contract to ensure project delivery. It would not be prudent and efficient for Transgrid to proceed to project completion without a clear resolution of the outstanding contractual issues and Elecnor Australia's parent company had signalled it would cease contributing to cash flow relief payments to Elecnor Australia if the contractual issues were not concluded.</p>
6	Project abandonment	Transgrid abandons the project after completing SP1.	X	Base Case	<p>Technically possible.</p> <p>Key challenges:</p> <ul style="list-style-type: none"> <li>All work other than the completion of SP1 ceases immediately.</li> <li>Re-instatement activities and material costs associated with works already done on SP2.</li> </ul> <p>Unacceptable negative outcomes for consumers.</p>
7	Alliance or acquisition of Elecnor Australia	Transgrid and Elecnor Australia form an alliance to complete PEC, or Transgrid acquires Elecnor Australia.	✓	1,675	<p>Technically possible.</p> <p>Key challenges:</p> <ul style="list-style-type: none"> <li>The risk profile of alliance arrangements is significantly different to traditional design and contract arrangements, exposing Transgrid and consumers to sharing of all risks in the project, including areas normally allocated to the contractor including performance.</li> <li>Acquiring Elecnor Australia would be unacceptably risky and would include liabilities and risks associated with involvement on projects unrelated to Transgrid.</li> </ul>

#	Option	Description	Delivery certainty?	Incremental NMB (\$ m)	Feasibility and key challenges
8	Enforcement of the EPC contract	Transgrid ceases additional payments and takes contractual measures under the EPC contract.	?	1,839	Technically possible. Key challenges are essentially the same as Option 3, given the risk of Elecnor Australia entering voluntary administration. This would entail protracted and costly litigation with Elecnor Australia and its parent company with enforcement in Spain also causing delays.

The above analysis showed that Option 4, being a new contract with Elecnor Australia, would deliver the highest incremental net market benefit of \$2,389 million, with a total net market benefit of \$964 million. Therefore, it represented the most prudent and efficient option to address the Contract Failure. The key benefits of Option 4 are:

- **Least impact to project schedule:** Elecnor Australia had provided a fully resourced program and detailed schedule, supplemented with KPIs and milestones, to complete the project by September 2026. Option 4 is the only option that would deliver PEC by that date.
- **Effective and efficient delivery of the Project:** Transgrid would have the advantage of continuity with existing subcontractors. Transitioning to an alternative contractor without the assistance of Elecnor Australia would add significant time and cost to complete the project (as detailed above in section 5). Switching to an alternative contractor mid-way through a major project presents significant challenges. One of the most critical risks is the loss of accumulated knowledge and lessons learned by Elecnor Australia. Without cooperation from Elecnor Australia, this knowledge gap could lead to missteps, rework, inefficiencies and material cost increases. Any new contractor would face a steep learning curve in stepping into a project already in progress, which includes understanding the status of the project, familiarising themselves with novated subcontracts, assessing the inherent risks and resourcing the project in a constrained market where resources are scarce, or already committed to other projects. Misunderstandings or delays in this process could lead to contractual disputes and/or disruptions in supply chains.
- **Greater cost certainty and low dispute risk:** there are significant protections under the ICC contract [REDACTED]. This significantly reduces dispute risk and means avoidance of potentially significant risk exposure, providing greater cost certainty to Transgrid, and in turn consumers.

Transgrid notes that contract termination (Option 3) and enforcement of the EPC contract (Option 8) would achieve net benefits that are \$550 million below those of Option 4. The substantially lower net market benefits of Options 3 and 8 arise from:

- **Reduced benefit due to additional delay:** the project would be delayed at least an additional 12 months compared to Option 4, resulting in deferred realisation of benefits.
- **Increased costs to deliver PEC:** the cost to complete the project under an alternative contractor would be substantially higher than those that could be negotiated with Elecnor Australia.

In summary:

- By ensuring that PEC will be completed as soon as practicable, gross market benefits of \$4.20 billion will be obtained for the benefit of consumers.
- While the new fixed contractual costs in the ICC are substantially higher than the fixed price EPC contract, the estimated net market benefits are \$964 million.
- The alternative option of attempting to enforce the EPC contract would have led to a significant delay and uncertainty to the project, significantly increased delivery costs and a loss of net market benefits of approximately \$550 million compared to the new contractual arrangements Transgrid negotiated with Elecnor Australia.

These observations indicate that these new contractual arrangements are prudent and efficient, as they obtain the best outcome on behalf of consumers.

Accordingly, in December 2024 Transgrid executed an ICC contract with Elecnor Australia as contractor. Significant protections have been obtained to ensure that PEC will be delivered in accordance with these new contractual arrangements. Furthermore, external legal advisors, Allens, confirmed that the protections and guarantees obtained by Transgrid are unique and extremely favourable. Further detail on the negotiation of the ICC contract and its prudence and efficiency is provided in Attachment 4.

## 7. Appendices and Supplementary Information

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The following appendices provide further information to explain the net market benefit assessment that underpinned Transgrid's assessment of the alternative options and the technical assumptions regarding benefits:

- Appendix 3a - Net market benefits assessment, Transgrid
- Appendix 3b - Net market benefits NPV Model (Forward-looking), Transgrid
- Appendix 3c - Net market benefits NPV Model (Total), Transgrid
- Appendix 3d - Gross market benefits assessment, EY
- Supplementary Information 3di - Statement of Facts: Market benefits assessment and loop flows, GHD, and
- Supplementary Information 3dii - Technical Memo: Reduction of minimum Synchronous Generators in SA, GHD.