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Kami Kaur
Acting Executive General Manager
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Australian Energy Regulator

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Dear Ms. Kaur,

Transgrid's Project EnergyConnect reopener application

AGL Energy (AGL) welcomes the opportunity to comment on Transgrid's application to reopen the Project EnergyConnect (PEC) revenue determination.

Overview

AGL suggests that Transgrid's reopener application should be denied.

While on its face this reopener appears to concern cost recovery for flooding and economic conditions, in substance it is about whether Transgrid should be permitted to recover costs after choosing not to enforce a fixed-price construction contract for the completion of PEC, thereby avoiding potential litigation, while potentially adding up to \$1.14 billion to its RAB.

Our key points, which are outlined below, are as follows:

- Transgrid's claim relies on an artificial framing of events that misapplies the rules
- Transgrid did not exercise effective oversight following Clough's insolvency
- Transgrid did not act as a prudent operator in failing to enforce its fixed-priced contract
- The new NMBA mischaracterises contract enforcement as a high-risk optional scenario
- Delaying PEC would not have materially increased NEM security and reliability risks
- The reopener's scale and complexity warrant further stakeholder engagement

Transgrid's claim relies on an artificial framing of events that misapplies the rules

Chapter 6A.7.1 of the NER permits a revenue determination reopening where a TNSP must undertake capital expenditure to rectify the adverse consequences of an event that is both:

- beyond the reasonable control of the TNSP; and
- not reasonably foreseeable by the TNSP.

‘the event’

Transgrid defines the relevant event as the “contract failure” which was its 25 October 2023 realisation that PEC could not be completed under the original fixed-price construction contract. It lists flooding, labour shortages, inflation, and productivity shortfalls as factors that led to this outcome.

Transgrid has however misapplied the rules. The rules make a clear distinction between an event and its “adverse consequences”. The relevant events are of course the flooding, labour shortages, inflation, and productivity shortfalls, while the contract failure was an adverse consequence.

Accepting Transgrid’s artificial framing of events risks establishing a precedent in which the event is defined by its outcome rather than by an external occurrence. This would allow TNSPs to determine when a reopener event occurs and thereby give them effective control over both the definition and timing of the event. This cannot be the intention of the rules.

‘beyond reasonable control’

Transgrid contends the contract failure was beyond reasonable control because it was:

- caused by an accumulation of factors (flooding etc) that were beyond its control
- it was the contractor not Transgrid that was responsible for delivery, and enforcing the contract would delay PEC

The rules assess control over the event, not earlier contributing circumstances, and therefore Transgrid’s lack of control over the flooding etc is not relevant.

Transgrid’s assertion that the contract failure was beyond its reasonable control ignores its obligation to consider all options reasonably available to it, including enforcing contractual obligations. Ex ante incentive regulation would collapse if TNSPs had no obligation to enforce contracts, including through litigation where appropriate.

Transgrid’s increased capital expenditure was not due to a contract failure beyond its reasonable control, but rather due its failure to exercise effective oversight of its contractor and its failure to act as a prudent operator in not enforcing its contract. These were both opportunities for Transgrid to exercise control and avoid its exposure to increased capital expenditure which it did not take. Each is discussed further below.

‘not reasonably foreseeable’

Transgrid’s application states that the contract failure was not reasonably foreseeable, due to the unknown cumulative impact of the factors affecting the contractor’s position. It does not,

however, claim that these factors were individually not reasonably foreseeable, as that would be inconsistent with its use of a fixed-price construction contract intended to allocate such risks to the contractor. In any event, these factors were reasonably foreseeable as flooding was a known risk in the PEC construction area, and both labour shortages and elevated inflation had become well-established risks since covid. These factors drove the increase in capital expenditure and were reasonably foreseeable risks that sat with the contractor under the fixed-price contract, rather than risks that should be transferred to consumers.

Whether or not the contract failure itself was foreseeable is not determinative as it was not the cause of the cost increases. Regardless, if the individual factors affecting the contractor's position were foreseeable, then it follows that the risk that these factors could cumulatively strain the contractor and lead to contract failure was also foreseeable. Transgrid has not explained why the cumulative impact of those factors was not reasonably foreseeable, beyond asserting that their combined effect was unknown.

[Transgrid did not exercise effective oversight following Clough's insolvency](#)

Transgrid's claim that the contract failure was beyond its reasonable control is undermined by its failure to act as a prudent operator and exert control in exercising effective oversight of its contractor prior to the contract failure. Transgrid accepted that the construction of PEC would not be completed by its contractor on 25 October 2023 after the accumulation of adverse circumstances affecting PEC became apparent between August and October 2023. Transgrid however failed to exercise control over its contractor prior to that period despite clear indications that it was in trouble.

Transgrid's application identifies a series of warning signs that should have triggered heightened and earlier oversight of the contractor, including:

- the December 2022 insolvency of Clough, resulting in the loss of key management capability and project systems;
- the contractor's submission of "hyper escalation" claims in March 2023, despite the contractor having no contractual or legal entitlement to those claims;
- advice from the contractor's parent company in April 2023 that forecast project losses were approximately \$400 million and that it would not provide further financial support; and
- material and persistent productivity shortfalls by mid-2023, with key construction activities taking up to five times longer than forecast, tower assembly around 22% slower, and tower erection approximately 40% slower than tendered across more than 200 towers.

Taken together, these warning signs demonstrate that contractor under-performance and financial distress developed progressively and were observable well before October 2023, at a time when Transgrid had full contractual rights and enforcement options. A prudent operator would have responded by escalating oversight earlier, interrogating deliverability, and actively

considering enforcement and alternative delivery options while cost exposure remained more limited. Instead, Transgrid continued delivery under the existing contract framework and deferred decisive control actions in ways that progressively narrowed and complicated its enforcement options.

This delay materially increased Transgrid's cost exposure, eroded the effectiveness of the risk allocation under the initial contract that underpinned the AER's original capex approval, and entrenched a weakened negotiating position by increasing sunk costs and diminishing contractual leverage. This reflects a failure to translate emerging risk into timely control, not a loss of control itself. In these circumstances, the subsequent contract failure cannot reasonably be characterised as beyond Transgrid's reasonable control for the purposes of the reopener rules.

[Transgrid did not act as a prudent operator in failing to enforce its fixed priced contract](#)

Chapter 6A of the National Electricity Rules requires a TNSP, in pursuing its capital expenditure objectives, to plan and manage capex consistent with the behaviour of a prudent operator. That obligation requires timely, proactive and commercially reasonable decision-making to manage delivery risk and protect consumers from inefficient costs. Transgrid did not act as a prudent operator in failing to enforce its fixed-price contract and accepting that the contractor would not deliver PEC as agreed.

On 25 October 2023, Transgrid accepted that construction of PEC would not be completed in accordance with the initial fixed-priced contract. The contractor however remained legally obligated to deliver the project at the fixed price, supported by a parent company guarantee and other contractual securities. At that point, a prudent operator would have acted promptly to protect consumers by enforcing those rights.

Once Transgrid accepted non-performance, a prudent operator would have taken decisive enforcement action. This would have included issuing a notice of default, exercising step-in or termination rights, calling on the parent company guarantee and other securities, and actively progressing alternative delivery arrangements so works could continue under Transgrid's control. Taking these enforcement steps would likely have preserved Transgrid's legal position, maximised prospects of cost recovery, and maintained effective leverage over delivery outcomes.

From AGL's perspective as a commercial entity operating without a regulated return or guaranteed cost recovery, this is precisely how such a situation would be addressed. Where a contractor signals nonperformance under a fixed-price arrangement, a prudent commercial organisation would be expected to enforce its contractual rights promptly, escalate disputes if required, and exhaust available remedies before accepting cost escalation or rebasing delivery on a cost-plus footing. Those disciplines are fundamental to effective risk allocation and cost control in competitive markets.

Instead, Transgrid failed to take those steps. It did not notify the AER in a timely manner of the material change in circumstances, issue a notice of default, or promptly and formally test whether another contractor could complete the works. Nor did it meaningfully pursue recovery from the contractor, including through enforcement of its contractual rights, the parent company guarantee, or preparing or commencing litigation if required, before shifting delivery and cost risk to consumers.

Although enforcement remained available throughout this period, Transgrid's ongoing inaction weakened its position and undermined its enforcement credibility. By allowing works to continue without formal enforcement, Transgrid increased sunk costs, strengthened the contractor's bargaining position, and progressively made enforcement and alternative delivery more difficult and less credible.

Despite recognising nonperformance in October 2023, Transgrid did not take decisive enforcement action before executing the Interim Construction Contract (ICC) in December 2024. The ICC shifted delivery to a cost-plus basis, accepted a \$25 million contractor contribution against a claimed \$1.1 billion cost increase, and transferred delivery and cost risk to consumers without first exhausting available contractual remedies.

The ICC materially compromised Transgrid's ability to pursue enforcement or alternative delivery options. By rebasing incentives, pricing and delivery obligations under a new commercial framework with the same contractor, enforcement of the original fixed-price contract ceased to be a realistic or commercially credible option.

[The new NMBA mischaracterises contract enforcement as a high-risk optional scenario](#)

Transgrid's updated net market benefits analysis (NMBA) assesses the relative costs and benefits of eight options to respond to the contract failure, including contract enforcement. Under the AER's CBA Guidelines, the appropriate base case is the continuation of economically prudent business as usual activities. In this context, business as usual would be contract enforcement, not project abandonment which Transgrid used as the base case. In reality, abandonment represents an extraordinary and discretionary decision, not a continuation of prudent operations.

By adopting abandonment as the base case, Transgrid frames contract enforcement as an optional and inherently high-risk alternative. This framing distorts the comparative analysis by inflating the apparent benefits of entering into a new contract and understating the role of enforcement as the default commercial response to a fixed price failure.

Treating abandonment as the base case also has the effect of shifting costs arising from the contract failure, and from any failure by Transgrid to mitigate that failure, onto consumers. Under this approach, costs that would ordinarily be attributed to Transgrid's commercial decisions are instead embedded in the counterfactual. This framing further reverses the burden of proof such

that Transgrid is not required to demonstrate that the new contract delivers superior outcomes relative to enforcing the existing contract, only that it is preferable to abandoning the project entirely.

The NMBA concludes that completing PEC under a new contract delivers the highest net market benefit, with contract enforcement ranked only as the third best option. This outcome is driven by modelling assumptions that materially disadvantage the enforcement option. In particular, Transgrid implicitly assumes that enforcement would not deliver timely or sufficient recoveries to offset consumer costs. Potential recoveries are treated as uncertain, delayed, and capped, while delay and remobilisation costs are largely assumed to fall on consumers.

The application does not demonstrate that these outcomes were unavoidable, nor that earlier or more decisive enforcement action by Transgrid could not have materially reduced delay, preserved value under the fixed-price contract, or improved recovery prospects. As a result, the NMBA does not provide a robust or neutral comparison between enforcement and the new contract, but instead reflects a modelling framework that embeds negative assumptions about enforcement while favouring negotiated contract replacement.

The NMBA also inflates the cost of delaying PEC by failing to consider credible non-network mitigations to delay such as extending the operation of AGL's Torrens Island B gas-fired generator (TIPS B). This is discussed further below.

In considering Transgrid's assessment of options, it is also relevant to recognise the incentive effects inherent in the regulatory framework. As a regulated monopoly, Transgrid recovers costs and earns a return on additions to its regulatory asset base, whereas options involving delay, downsizing, or aggressive enforcement of fixed-price contractual rights do not attract the same financial treatment. This creates a structural bias toward capital intensive solutions, reinforcing the need for the AER to test carefully whether Transgrid's preferred approach genuinely represents the least cost response from a consumer perspective.

[Delaying PEC would not have materially increased NEM security and reliability risks](#)

Transgrid's application asserts that AEMO has consistently identified PEC as an urgently needed actionable project in every Integrated System Plan (ISP) since 2020. That characterisation materially overstates the ISP position. The ISP has treated PEC as a structural, medium-term transmission augmentation, designed to support system security and reliability as thermal generator retirements accelerate and the generation mix changes through the 2030s, rather than as a project required to address any imminent reliability shortfall.

The 2023 Electricity Statement of Opportunities (ESOO) which was published prior to the October 2023 contract failure included the following regarding the impact of a delay of PEC:

While not modelled, any delays to the commissioning of Project EnergyConnect are likely to lead to significantly higher reliability risks in 2026-27, due to the quantity of generation that has advised retirement at the time this transmission development is advised to complete commissioning.

The potential higher reliability risk if PEC was delayed only existed because on November 2022 AGL announced it planned to close TIBS B on 30 June 2026. This date was chosen to coincide with the planned completion of PEC which was expected to impact gas-fired generation in South Australia and as a result the economic viability of TIPS B. Ultimately, after a one year delay to PEC was confirmed in the July 2024 ISP, the reliability risk was resolved by AGL's September 2025 agreement with the South Australian Government to extend the operation of TIPS B for two years to 30 June 2028.

Delaying PEC therefore did not materially increase NEM security or reliability risks. Any reliability risk associated with a delay was conditional and capable of mitigation, rather than inherent to the project, and a prudent operator should not have assumed that enforcing contractual remedies would expose the NEM to material security or reliability risks. The prospect of a delay of around 12 months did not justify a decision to forgo enforcement of existing contractual rights. Where a project's benefits are predominantly medium-term in nature, the prudent response to delivery challenges is to exhaust reasonable contractual and commercial remedies before transferring costs to consumers.

[The reopener's scale and complexity warrant further stakeholder engagement](#)

Given the magnitude of costs claimed and complexity of Transgrid's application, AGL suggests that a further opportunity for stakeholder engagement on this reopener would be appropriate to ensure stakeholders have sufficient time to consider the application.

If you have any queries re this submission, please contact [REDACTED] at [REDACTED]

Yours sincerely,

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