

# Public forum

Improving guidance for better application of  
the regulatory investment tests

Holiday Inn Sydney Airport

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# Welcome

AER Board member, *Jim Cox*

# Introduction

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1. Overview of the RITs
2. The AER's role in the RITs and the application guidelines
3. Today's discussion topics

# Regulatory investment tests

- 'RIT-T' for transmission, 'RIT-D' for distribution
- Economic cost-benefit test, with purpose to:

... identify the *credible option* that maximises the present value of net economic benefit to all those who produce consume and transport electricity in the *market* (the *preferred option*). For the avoidance of doubt, a *preferred option* may, in the relevant circumstances, have a negative *net economic benefit* (that is a net economic cost) where the *identified need* is for *reliability corrective action*.

- Market wide → includes things like market benefits across regions and changes to costs of other parties

# RIT process

Step	RIT-T	RIT-D
1. No RIT if investment is: for an urgent & unforeseen network issue, maintenance, or...	The most expensive option costs <\$6m	The most expensive option costs <\$5m
2. Consultation report with min 12 week consultation period	'Project specification consultation report'	'Non network options report'. Skip if there are no non-network options.
3. Draft decision with min 6 week consultation period	'Project assessment draft report'. Skip for projects <\$41m	'project assessment draft report'. Skip for projects <\$10m
4. Final decision	'Project assessment conclusions report'	'Project assessment final report'
5. Parties have 30 days to provide a dispute notice to AER for RIT misapplication or assessment errors		

## AER role in the RIT process

- Dispute resolution
- Revising cost thresholds
- Deciding interested parties
- Granting RIT proponents: timeline extensions, reapplication exemptions, new market benefit classes
- Monitoring role
- Translating the NER into the RITs and application guidelines

## Why are the guidelines important?

- Clear, transparent, AER-endorsed guidance enables the RIT process to operate successfully
- At a high-level, a cost benefit analysis seems simple: Expected benefits less costs, discounted over time

$$\text{Net present value} = \sum_{t=0}^N \frac{\text{benefit}_t - \text{cost}_t}{(1 + \text{discount rate})^t}$$

Where  $N$  = investment horizon,  $t$  = year

- In practice, it is difficult
  - E.g. calculating benefits across the market → assumptions, forecasts, complex interrelationships → market development modelling, scenario analysis

## Why are the guidelines important?

- More certainty for network businesses:
  - Relationship with revenue determinations, especially for contingent projects
  - Where will AER fall on disputes (current uncertainties, desire to build for supply rather than load)?
- Guidelines promote consistency and transparency required for stakeholders to challenge outcomes and propose alternative options.
- Principles-based to balance certainty/consistency with flexibility/discretion



# Issues to consider: Response to survey

Discussion topic	Times voted 1 <sup>st</sup> -2 <sup>nd</sup> -3 <sup>rd</sup>
<ul style="list-style-type: none"> <li>Issues specific to replacement projects</li> </ul>	<ul style="list-style-type: none"> <li>4-3-3</li> </ul>
<ul style="list-style-type: none"> <li>Interplay between the future ISP &amp; RIT assessments</li> <li>Selecting the base case</li> <li>What constitutes an identified need</li> </ul>	<ul style="list-style-type: none"> <li>8-2-0</li> <li>3-4-0</li> <li>1-4-4</li> </ul>
<ul style="list-style-type: none"> <li>Calculating option value, forecasting &amp; testing states of the world</li> <li>Scenario analysis &amp; accounting for high impact, low probability events</li> </ul>	<ul style="list-style-type: none"> <li>4-1-3</li> <li>1-4-6</li> </ul>
<ul style="list-style-type: none"> <li>Consideration of non-network options</li> <li>Consumer engagement when applying RITs</li> </ul>	<ul style="list-style-type: none"> <li>3-1-4</li> <li>2-1-0</li> </ul>
Selecting an appropriate value for the VCR	1-1-0
RIT's interplay with proposed NEG (or other policies)	0-4-1
The impact of external funding when applying RITs	1-1-1
Determining which discount rate to use	0-0-2
Required processes around cancelling RIT assessments	0-0-0

# Breakout session discussion topics

#	What guidance should the application guidelines provide on how to...
1	...apply RITs to replacement projects?
2	...work effectively with the ISP, particularly when identifying needs and selecting the base case?
3	...deal with uncertainty, including through calculating option value, forecasting, performing scenario analysis, and accounting for high impact low probability events?
4	...engage with non-network options and consumers when applying RITs?

# 1. Application to repex projects

- Asset retirement & costs unique to repex (asset disposals)
- Applying cost thresholds to projects with replacement and augmentation drivers
- Applying cost thresholds to asset replacement programs
- What costs are included in the 'base case'?

## 2. Working effectively with the ISP

- AEMO to publish first ISP in June
- Strategic infrastructure development plan, which will consider:
  - Transmission development options,
  - What makes a successful renewable energy zone, and how to develop these zones.
- Grouped with topics on selecting the base case and identified need, given interrelationships.

### 3. Accounting for uncertainty

What additional guidance or worked examples would you like to see on:

- How to formulate credible options that confer option value across scenarios and how to undertake scenario analysis?
- How to account for high impact, low probability events and related system security requirements? Should the guidance or worked example differ between the RIT-D and RIT-T application guidelines?

## 4. Non-network engagement

- How can guidance better facilitate consumer engagement?
- How can guidance → better use of:
  - 'non network options report' under the RIT-D, which distribution businesses can skip
  - 'project specification consultation report' under the RIT-T, which has a lighter emphasis on non-network options than the NNOR
- Should the AER have greater oversight of these stakeholder engagement activities?

## Breakout session

- 4 groups / 4 topics– try to spread out so groups are relatively even and diverse
- Introduce yourselves
- Pick a scribe & a presenter
- 50min for brainstorming – how should the RIT guidelines address the topic?
- During morning tea: Use Post-It notes to add ideas/questions to others' notes
- After morning tea: Re-group for presentations + Q&A

# Breakout sessions

#	Discussion topic	Facilitator/s
1	Applying RITs to replacement projects	Mark Wilson / Richard Khoe
2	The ISP and its implications on the RITs, identified needs and selecting the base case	Peter Adams
3	Accounting for uncertainty: option value, forecasting, scenario analysis, high impact low probability events	Darryl Biggar / Rajat Sood
4	Engaging with non-network options and consumers when applying RITs	Lisa Beckmann / Samantha Markham



## Morning tea

- AER staff will stick the butchers paper up on the walls
- At your leisure, use the Post-It notes on your tables to add ideas or questions to others' notes
- Presenters – get ready to present your groups ideas after the break!

## Roundtable discussion

1. Applying RITs to replacement projects
2. The ISP & its implications on the RITs, identified needs, selecting the base case
3. Accounting for uncertainty: option value, forecasting, scenario analysis, high impact low probability events
4. Engaging with non-network options & consumers when applying RITs

# Next steps

- Submissions on Issues Paper close COB 6 Apr
- Aiming to publish draft amendments in May/Jun  
– followed by submissions and a workshop
- Aiming to publish final amendments in Sept/Oct