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13 August 2009

Dr John Tamblyn
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Dr Tamblyn

Review of national framework for electricity distribution network planning and expansion (AEMC reference EPR0015)

Please find attached the AER's submission on the AEMC's draft report for the review of the framework for electricity distribution network planning and expansion.

Please contact me if you have any questions in relation to the matters raised in our submission.

Yours sincerely

Michelle Groves
Chief Executive Officer
Australian Energy Regulator

AER Submission

Review of the national framework for electricity distribution network planning and expansion

Response to AEMC draft report

13 August 2009

Introduction

The Australian Energy Regulator (AER) welcomes the opportunity to respond to the Australian Energy Market Commission's (AEMC) draft report for its review of the national framework for electricity distribution network planning and expansion.

Among its roles, the AER is the economic regulator of electricity distribution services in the National Electricity Market. The AER has also been responsible for developing the regulatory test and is currently responsible for developing the new regulatory investment test for transmission (RIT-T). These responsibilities leave the AER well placed to comment on the design of distribution network service providers' (DNSPs) planning processes and the regulatory investment test for distribution (RIT-D).

This submission comments on the AEMC's proposed recommendations regarding:

- DNSP's annual planning requirements and reporting requirements
- the RIT-D project assessment process and
- the RIT-D dispute resolution process.

The draft report commented that further review is needed regarding the process for determining jurisdictional reliability standards, asset management practices and reporting, and target setting for reliability performance. While this is outside the scope of the current review and not addressed in this submission, the AER agrees with the AEMC's assessment and would welcome this type of review.

Annual planning process and reporting requirements

The AEMC has proposed that DNSPs will carry out an annual planning process covering a minimum forward planning period of five years. The planning process will apply to all distribution network assets and activities that have a material impact on the distribution network. DNSPs will be required to use reasonable endeavours to engage with non-network proponents and consider non-network alternatives. They will also be required to establish and implement a Demand Side Engagement Strategy.

The AER supports the approach taken by the AEMC in its review of DNSP planning processes. The movement towards a nationally-consistent approach to network planning is a positive development and the proposed annual planning process appears to provide a reasonable framework for distribution network planning.

The AEMC also proposes that DNSPs publish a distribution annual planning report (DAPR) each year. The proposed DAPR will include detailed information on the DNSP's forecasting, details of system limitations and proposed network investments, characteristics of the network and a summary of any joint planning activities.

The AER welcomes the increased transparency on the forecasting processes and considers that this will enhance opportunities for better comparisons of differing

methodologies across jurisdictions. It may also provide a platform for the future development of a common approach to forecasting in each jurisdiction.

The AER supports creating a national framework for reporting (including the proposed DAPR). The information proposed to be included in the DAPR should provide a valuable resource to market participants and the publication of the DAPR may act as a discipline on DNSPs by aiding transparency and accountability. The information contained in the DAPR may also be a valuable resource for the AER in its regulatory and enforcement roles.

The AER also considers that there may be merit in developing a consistent format and approach to DAPRs for all DNSPs over the longer term. A standard format would allow market participants to more easily compare the outcomes of annual planning processes across each of the networks and jurisdictions.

The AEMC considers that a guideline which sets out a standard format and content of DAPRs is not required. The AER recognises that the Electricity Rules should provide sufficient guidance on the content of the DAPR, however, in the longer term a guideline may assist to ensure that a consistent format and approach is adopted for all DNSPs.

Regulatory investment test for distribution

The AER welcomes the introduction of a new RIT-D project assessment process for distribution investment. The RIT-D should ensure that DNSP's conduct robust economic assessments of alternative projects including non-network solutions.

This part of the submission comments on the proposed:

- level of prescription for the RIT-D requirements
- framework for analysing costs and benefits, and
- RIT-D threshold and assets subject to the RIT-D
- RIT-D consultation process.

Level of detail in RIT-D specifications

The AEMC has attached proposed specifications for the RIT-D and dispute resolution process in appendix B of the second interim report. While these specifications are not draft rules, they prescribe a significant amount of detail on the proposed framework. In previous submissions to the AEMC, the AER has outlined problems associated with adopting an overly prescriptive approach for the Electricity Rule requirements for the RIT-T. Similar problems could arise in the context of the RIT-D.

However, if the AEMC considers that heavily prescribed principles for the RIT-D are appropriate, the AER notes that the proposed specifications will require a thorough review before they can be used as a basis for draft rules. Although the AER has only conducted a very high level review of the proposed specifications, it has identified a number of areas where the drafting of the specifications may have unintended consequences.

Framework for analysing costs and benefits

The AEMC has proposed that the RIT-D include consideration of costs and market benefits for each credible option. DNSPs would be required to quantify all costs, but would have the discretion to quantify market benefits.

The AER recognises the reasons for adopting this approach however there is merit in moving to a regime which is more consistent with the framework for transmission. The RIT-T will require transmission network service providers to consider market benefits that are material. If the need for an investment is to meet a reliability standard and no options have material market benefits, the RIT-T effectively becomes a least cost test analogous to the reliability limb of the regulatory test. This ensures that the RIT-T does not require a disproportionate level of analysis. A similar framework could be adopted in distribution.

RIT-D threshold and assets subject to the RIT-D

The AEMC proposed that DNSPs will undertake the RIT-D when a distribution system limitation exists and the most expensive option is expected to cost $2 million or more. The RIT-D will also not apply to urgent and unforseen investments, negotiated services, replacements, refurbishments or connection services. The AEMC has also sought views on whether primary distribution feeders should be excluded from the RIT-D.

Cost threshold

In its previous submission, the AER noted that a $2 million threshold may create a significant RIT-D assessment burden. To maintain consistency with transmission, the AER proposed that the RIT-D assessment should be conducted where the most expensive option is over $5 million.

The AER maintains this view, but notes that the AEMC is proposing to only require DNSPs to quantify costs when conducting the RIT-D and is considering excluding primary distribution feeders from assessment under the RIT-D. Given this, the proposed $2 million threshold may not impose a significant regulatory burden on DNSPs.

As noted in the AER's previous submission, DNSPs may potentially be able to divide distribution programs into smaller projects to avoid triggering a RIT-D assessment process. To give effect to the proposed $2 million threshold, the AEMC should ensure that the Electricity Rules are drafted to prevent distribution programs being divided in this manner.

Assets excluded from RIT-D assessment

It is unclear in the draft report how the AEMC propose to define primary distribution feeders. The report refers to a proposed exemption in section 2(a)(vii) in the detailed specifications in appendix B of the draft report, however the appendix does not appear to provide a definition for the term *primary distribution feeder*.

In its report to the AEMC on developing a national framework for electricity distribution network planning, SKM appeared to identify 11/22kV feeders as primary

distribution feeders.[1] SKM also noted that the typical cost range for these projects is between $250 000 and $2 million.

The AER is unable to comment on the effect of the proposed exclusion without further detail. However if the AEMC intends to exclude the types of asset identified by SKM, then SKM's advice appears to suggest that the majority of these assets will not be subject to analysis under the RIT-T (as they will not meet the AEMC's proposed $2 million cost threshold).

Dispute resolution process

The proposed dispute resolution process set out in the draft report and in the detailed specifications in appendix B appear to be similar to the process that will apply to RIT-T disputes. However unlike in transmission, the AER will have no ability to recover costs associated with engaging consultants from the parties to the dispute. It is unclear why this aspect of this process is different to the regime applied to RIT-T disputes.

[1] SKM, *Advice on development of a national framework for electricity distribution network planning and expansion—Final report*, 2009, p. 98.