

ELECTRICITY TRANSMISSION NETWORK owners

Process Guideline for Contingent Project Applications

Response to AER Draft Guideline

9 July 2007



1. Introduction

On 15 May 2007, the Australian Energy Regulator (AER) released a draft *Process Guideline for Contingent Project Applications under the National Electricity Rules* (the Rules) for public comment. The draft Guideline is intended to assist transmission network service providers (TNSPs) in meeting contingent project requirements contained in the Rules.

This submission is made on behalf of the Electricity Transmission Network Owners Forum (ETNOF), consisting of ElectraNet Pty Limited, Powerlink Queensland, SP AusNet, TransGrid and Transend Networks Pty Limited. Collectively, this group own and operate over 40,000 km of high voltage transmission lines and have assets in service with a current regulatory value in excess of \$9.1 billion. ETNOF welcomes the opportunity to respond to the AER's draft Guideline.

ETNOF recognises that the contingent project regime set out in the Rules places an onus on TNSPs to provide the information reasonably required by the AER to approve a contingent project application and accept the consequential adjustments to a revenue cap. However, because of other regulatory processes associated with major augmentation projects, such as the Regulatory Test process, much of this information is expected to be available in the public domain in any event. For this reason care is required to avoid costly duplication of effort, and delays to the overall development timetable.

It should also be recognised that the Rules have deliberately included a contingent project regime on the basis that such a regime enhances the National Electricity Market (NEM) Objective. As such, it is incumbent on both TNSPs and the AER to work constructively together to give practical effect to this regime. ETNOF members are committed to this outcome. It is with this outcome in mind that this response to the AER's proposed Guideline has been prepared. Similarly, ETNOF would welcome the opportunity to discuss the matters raised with the AER prior to the finalisation of this Guideline.

2. Issues

2.1 Expenditure Criteria and Factors

In order to have a 'realistic expectation' of demand forecasts and cost inputs, the AER considers that the relevant TNSP:

"... must have completed and included in its application all option assessments, feasibility studies, and any other investment appraisals or processes necessary to fulfil the requirements of the Rules."¹

¹ AER (2007), *Process Guideline for Contingent Project Applications under the National Electricity Rules*, Draft, May, p4.

ETNOF is concerned that the term 'realistic expectation' is used in other parts of Chapter 6A where the definition above would be wholly inappropriate. The term is used to describe both the capital expenditure criteria and the operating expenditure criteria as part of a Revenue Proposal, and these same terms are then incorporated into the assessment of contingent projects. The implication of the AER's definition of 'realistic expectations' is that it would be capable of uniform application across a variety of situations. However, the definition contained in the draft Guideline is not meaningful in the context of a Revenue Proposal.

ETNOF is concerned that it is neither necessary nor practical to complete all such assessments and analysis at the time the original revenue cap proposal is prepared, particularly where a probabilistic approach to establishing an ex-ante capex cap is used. The Rules, in this regard are demanding, but not so unreasonable as to require what cannot, in reality, be delivered as the basis for the AER accepting an ex-ante capex forecast.

The Rules require a TNSP to analyse the expected future development and operation of its network taking into account, among other things, relevant forecast loads (or demand). These loads are developed in conjunction with DNSPs and other Rules participants as part of the annual planning review process and have a 10-year horizon. Annual Planning Reports are then published by each TNSP to inform interested stakeholders, inclusive of forecast loads, identified network constraints, proposed augmentations and proposed solutions to address those constraints.

ETNOF considers that demand forecasts developed, consistent with the mandatory and statutory process described above, clearly provides a 'realistic expectation' of demand forecasts and that it would be unreasonable for the AER to suggest otherwise.

Similarly, through practical necessity, a 'realistic expectation' of cost inputs can be, and is, established by means other than a fully completed options analysis and assessment. TNSPs evaluate, plan and undertake necessary investment in their networks in order to meet mandated reliability and other obligations on an ongoing basis, consistent with prudent and good electricity industry practice. In doing so, a number of different methods can be employed. For example, the application of internal unit costs based upon the actual cost of recently completed projects, competitive tender prices on similar plant or equipment and recently sourced contract prices for similar projects. All such methods are commonplace to not only the electricity industry, but are utilised by many other industries more generally.

As to what constitutes a 'realistic expectation', this must vary depending on whether it is applied to a contingent project application or a revenue proposal. ETNOF believes the AER should not be prescriptive on this point. Instead, the term 'realistic expectation' should be given its natural meaning in the context in which it is being applied. Alternatively, if a definition for this term is believed to be necessary, the Guideline should make it clear that the definition only applies in the same context to which the Guideline applies.

2.2 Pre-lodgement Process

In the draft Guideline, the AER proposes that a non-statutory, pre-lodgement process be established and applied to contingent projects. ETNOF believes that this is an area where flexibility and a measure of proportionality will prove useful.

ETNOF has no doubt that some form of constructive interaction between the AER and relevant TNSP will occur in any event, prior to lodgement of a formal contingent project application. However, ETNOF questions the extent to which such an arrangement needs to be formalised and documented in the Guideline. This approach risks creating a “one-size fits all” process which will necessarily gravitate towards handling the largest and most complex projects and be an unnecessary overhead for simpler proposals. Instead, the nature and extent of this interaction should be left for the individual TNSP and AER to agree, as and when a particular contingent project emerges. As set out below, ETNOF does not consider that such arrangements will hinder the AER in its preliminary understanding of a forthcoming contingent project, given the level of information and public consultation that will be undertaken, as a matter of course, some months prior to a TNSP’s formal lodgement of a contingent project application.

TNSPs are required to undertake public consultation with Registered Participants and other interested stakeholders on network augmentations in accordance with the National Electricity Rules and Regulatory Test process to determine the most efficient option to address an emerging supply limitation. For new large network assets, this process involves:

- the publication of an Application Notice detailing the nature and timing of an emerging limitation as well as assumptions, reasonable network and non-network options, technical details, financial analysis, ranking of alternatives and draft recommended solution; and
- the publication of a Final Report containing similar information to that specified in the Application Notice as well as a summary of, and responses to, submissions on the Application Notice, together with the final recommended solution.

In addition to these requirements, a number of TNSPs, in certain circumstances, also release a Request for Information (RFI) Paper prior to publication of an Application Notice. The Annual Planning Report is required to highlight emerging network augmentation needs some years in advance. The Annual Planning Report and RFI document provides early opportunity for stakeholder input into any identified emerging network limitations and, in particular, seeks proposals on possible non-network options to address the need.

ETNOF considers that much of the necessary information required for the AER to determine whether a contingent project application complies with the requirements of the Rules, such as an assessment of feasible options and financial investment analysis (with the exception of incremental operating expenditure and incremental revenue), will be available to the AER as part of the Regulatory Test consultation process. In particular, there will be adequate information available to enable the AER to determine that a trigger event has occurred.

2.3 Independent Expert Assistance

The draft Guideline provides for the AER to seek independent expert advice on whether an identified trigger event has occurred and on the relevant TNSP's evaluation of a contingent project, including justification for selecting the proposed option.

In principle, ETNOF understands that there may be a need for the AER to commission independent expert assistance in the areas identified above in order to give itself a level of comfort on these issues. While the AER must take into account the factors in clause 6A.8.2(g) when making a determination, some of which may be provided by independent experts, the Rules do not limit the AER to only considering those factors.

ETNOF is of the view that the AER should also be mindful of, and give considerable weight to, the analysis and outcomes resulting from the public Regulatory Test consultation process. If no material issues are raised by interested stakeholders as part of this process, TNSPs see no reason why the AER should question the outcome of this robust process, particularly where a dispute has not been raised on the contents, assumptions, findings or recommendations of the final Regulatory Test report.

ETNOF also urges the AER to exercise caution in conducting any further analysis of options at this stage, given the AER's role in the Regulatory Test dispute resolution arrangements. The assessment of contingent projects should be able to be applied consistently for any application, regardless of whether or not any dispute has been raised through the Regulatory Test consultation.

2.4 Due Process

The AER flagged its intention to directly liaise with interested parties throughout a consultation process, should it choose to do so. In addition, the draft Guideline contemplates that interested stakeholders may lodge confidential submissions with the AER on contingent project applications.

ETNOF accepts the AER's position in relation to these matters. However, in the interests of procedural fairness, ETNOF considers that where such undertakings result in claims or information that may be contrary to the relevant TNSP's analysis, the relevant TNSP should be afforded the opportunity to respond to this information prior to the AER's decision.

3. Summary

The Rules clearly provide TNSPs with a strong incentive to assist the AER with the assessment of contingent project applications by providing sufficient, relevant and timely information. With this in mind, ETNOF proposes that:

1. the AER recognises that what constitutes 'realistic expectations' will vary according to the circumstances in which the term is applied and that any definition provided in the Guideline should make it clear that the definition only applies in the same context to which the Guideline applies;
2. much of the information required to process a contingent project application is provided via existing requirements for larger capital projects (e.g. via the Regulatory Test process) and that duplication of effort and stakeholder interaction can and should be avoided; and
3. consideration be given to a more informal approach to the specification of the pre-lodgement process in recognition of the varying requirements of projects of different scope and scale.