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Ms Kami Kaur
Acting General Manager
Australian Energy Regulator
GPO Box 520
Melbourne, Victoria, 3001

Lodged via email: aerinquiry@aer.gov.au

Dear Ms Kaur

Issues paper – Demand management innovation allowance mechanism

TransGrid welcomes the opportunity to provide comments on the Australian Energy Regulator's (AER) issues paper on the demand management innovation allowance mechanism (DMIAM).

We the operator and manager of the high voltage transmission network connecting electricity generators, distributors and major end users in New South Wales and the Australian Capital Territory. Our network is also interconnected to Queensland and Victoria, and is instrumental to an electricity system that allows for interstate energy trading.

We support the work the AER is undertaking to allow a demand innovation allowance (DMIA) for Transmission Network Service Providers (TNSP) with the objective to lower long term network costs through funding research and development in demand management projects. A DMIA will promote innovation in non-network solutions and encourage TNSPs to trial new technologies and techniques that have the potential to address constraints that manifest at the transmission level and provide benefits to consumers through lower transmission and total system costs consistent with the DMIAM objective. However, we are concerned that some of the proposed characteristics of the DMIA outlined in the AER's issues paper may discourage TNSPs from accessing the DMIA. In order for the objectives of the DMIAM to be achieved, it is important to ensure that the scheme is designed in a way that supports meaningful investment in innovation.

Our concerns with the scheme design relate to the following issues, which are explained further below:

1. Proposed allowance
2. Opex only and ex post allowance
3. Independent expert advice

1. Proposed allowance

The AER is proposing to adopt a cap for the DMIA that can be accessed by a TNSP at 0.1 per cent of Maximum Allowed Revenue (MAR) per regulatory period. We are concerned that an allowance of 0.1 per cent of MAR is insufficient for us to undertake projects that we consider would meet the objectives of the DMIAM by providing meaningful benefits to consumers through trialling innovative approaches to address network issues. We supplied the AER with an example list of projects (which are outlined in the AER's issues paper) that we think would be beneficial for consumers for us to undertake if provided with an allowance reasonably proportionate to the objectives of the DMIAM. Our initial internal costing indicates that an allowance of 0.1 per cent of MAR would only provide sufficient funding to undertake one or two of our identified innovative projects across the regulatory period. We encourage the AER to adopt an allowance of 0.2 per cent of MAR as this would proportionately incentivise TNSPs to undertake more consumer-benefiting projects. In addition, the reporting and compliance obligations that are being proposed by the AER will further disincentivise TNSP's participation in the scheme as the proposed 0.1 per cent of MAR allowance will further be eroded by the costs of meeting these obligations.

We support the AER's proposal to apply an uplift to non-network solutions above the cap to encourage investment in innovative project that meets the schemes objectives of lower long-term costs to consumers. We support a 50 per cent uplift similar to the NCIPAP scheme.

We also support the AER's proposal to provide flexibility to pool funds into larger projects (provided the aggregate allowance is sufficient) and across regulatory periods, as this would optimise consumer benefits through the ability to accommodate different spending patterns.

2. Opex only and ex post allowance

The AER is proposing that the DMIA be spent on opex only to ensure consumers do not continue to pay for assets used in innovation projects once those projects have been completed. We have concerns that limiting the DMIA to opex only will have unintended consequences for projects that involve relatively small amounts of capex and encourage the AER to design the DMIAM such that there is flexibility for a TNSP to use part of the DMIA for minor capex where this is required for efficient project delivery. For example, if the innovation project was a special protection scheme with monitoring and customised hardware attached to loads and generation, a restriction on using the DMIA for capex would mean a TNSP would need to pay a third party to acquire the relevant assets. In this instance, the TNSP would likely incur further removal and decommissioning costs if the payback period for the relevant assets is longer than the trial.

We support the AER's intent to minimise resources in submitting and reviewing our revenue proposals. However, we consider that the AER's proposal to approve the allowance on an ex-post review basis would not give the necessary certainty to TNSPs in advance of making an investment and therefore may deter businesses from investing in innovation. We encourage the AER to consider an ex-ante approval of the allowance, which is consistent with distributors.

3. Independent expert advice

The AER is proposing that TNSPs must use an independent expert to review, critique and endorse a TNSP's proposed demand management projects before implementation. We consider that this appraoch may unduly increase costs to consumers with no tangible benefits or/and outcomes where TNSPs have the necessary experts in-house to review and evaluate any proposed demand management project. Furthermore, if an ex-ante approach is adopted the AER will undertake the necessary reviews.

We look forward to working with the AER to finalise the DMIAM for TNSPs that meets the objectives of the scheme by funding research and development in innovative projects that lowers long-term costs to consumers.

If you would like to discuss this submission, please contact Zainab Dirani on [redacted] or [redacted] or myself on [redacted] or at [redacted]

Yours sincerely

[redacted]

Stephanie McDougall
Head of Regulation