



Hon Lily D'Ambrosio MP

Minister for Energy, Environment and Climate Change  
Minister for Solar Homes

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Mr Chris Pattas  
General Manager, Networks - Distribution  
Australian Energy Regulator  
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Melbourne VIC 3001

Ref: MBR039960



Dear Mr Pattas

**AUSNET SERVICES TRANCHE 3 CONTINGENT PROJECT APPLICATION – SUBMISSION TO THE AUSTRALIAN ENERGY REGULATOR**

I welcome the opportunity to make a submission on AusNet Services' (AusNet) 31 May 2019 contingent project application (CPA) to the Australian Energy Regulator (AER) for \$108.8 million (\$2015) to fund its third tranche of works to deploy Rapid Earth Fault Current Limiters (REFCL).

The Victorian Government remains committed to implementing measures that will reduce the risk of catastrophic bushfires like those that occurred on Black Saturday in 2009. Powerlines were found to have been the cause of 159 of the 173 deaths in that tragic event. AusNet's Tranche 3 CPA proposes critical works associated with implementing the Victorian Bushfires Royal Commission's (VBRC) Recommendations 27 and 32, which are designed to respond to and reduce that risk.

I am pleased to learn that the works for its first deployment tranche has largely been completed, with planning and works underway for the second tranche. I am also pleased to see that AusNet is applying lessons learned from its REFCL deployment and commissioning experience to date in its planning and works going forward. The Victorian Government commends AusNet for its dedication to this important safety initiative, which together with Powercor's efforts, appears to be on course to deliver an unparalleled improvement in safety standards for the benefit of all Victorians.

AusNet is forecasting total capital and operating expenditures of \$108.8 million for its Tranche 3 REFCL installations and associated works. I note that this represents a 65.5 per cent increase from the average expenditure for Tranche 1 & 2. The Victorian Government wants to ensure that all improvements to the electricity network, including works that are the subject of CPAs, are provided at a fair and reasonable cost to electricity consumers. For example, the CPA should not be used as a vehicle to fund the replacement of aged or poor condition assets. These costs should be attributed by AusNet as business as usual expenditure. On behalf of Victorian consumers, I expect that the AER will undertake all regulatory, technical and financial due diligence in its interrogation of the claims put forward in AusNet's Tranche 3 CPA.



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### Specific Comments

AusNet's Tranche 3 CPA and supporting materials have been reviewed closely by the Department of Environment, Land, Water and Planning (DELWP). While the Victorian Government is broadly supportive of AusNet's Tranche 3 CPA, I bring to your attention two specific concerns:

- unwarranted expenditures for works associated with AusNet's Kalkallo substation, as the scope (and cost) of works is uncertain and undergoing revision; and
- non-REFCL costs appear to be included in AusNet's Tranche 3 CPA for the Kalkallo, Benalla, Lang Lang, Mansfield and Sale zone substations and need to be identified and properly accounted for in the AER's review process.

### Unwarranted expenditure for works associated with AusNet's Kalkallo substation

Authorising expenditures for AusNet's Kalkallo works appears unwarranted as the planning for the Kalkallo substation seems premature because there is considerable uncertainty about the costs, and scope of the company's proposed solution to make Kalkallo a 'complying substation'. The proposed solution for the substation appears to have changed considerably from the proposal originally outlined in AusNet's Tranche 3 CPA. I also note that there has been no decision (or agreement) by relevant regulatory bodies regarding a proposal for the substation.

Two of the requirements by the AER for lodgment of a CPA for Tranche 3 REFCL works do not appear to have been satisfied in the case of Kalkallo, namely AusNet has not completed:

- a forecast of capital expenditure required for complying with the relevant regulatory obligation or requirement; and
- a project plan identifying the scope of the work and proposed costings for each of the proposed capital works forming a part of the contingent project.

The total forecast capital expenditure (capex) associated with AusNet's (originally) preferred option for the substation is \$36.828 million (or 34.9 per cent of the CPA's total forecast capex). Given the uncertain and evolving nature of AusNet's proposed works it appears that expenditures for such works may be unwarranted at this stage. In addition, based on the evidence provided, the government is uncertain as to whether all the proposed costs relating to Kalkallo are 'directly attributable' to the REFCL program. As you are aware, this is a requirement for lodgment of a CPA for funding Tranche 3 works.

Based on DELWP's review of AusNet's Tranche 3 CPA, it appears that some portion of the capital expenditure associated with the proposed Kalkallo works are ordinary augmentation expenditure (augex). These works AusNet proposes at the Kalkallo substation are being driven, in part, by the need to accommodate rapidly increasing growth in customer demand. The cost of network upgrades to accommodate demand growth should therefore be considered ordinary augex. For this reason, they should be separated from the costs attributable to bringing Kalkallo into compliance with the 'required capacity' standards established in section 120M of the *Electricity Safety Act 1998* (Vic) and subordinate legislation (collectively, the Act).

DELWP advises that this augex should be appropriately considered through AusNet's upcoming Electricity Distribution Price Review (EDPR) for the 2021-25 regulatory control period. Alternatively, if such capex is authorised as part of AusNet's Tranche 3 CPA, they should be taken into account in its next EDPR determination. Only capex necessary to comply with the Act's 'required capacity' standards should be attributed to earth fault standards.



**Non-REFCL costs appear to be included in AusNet's Tranche 3 CPA for the Kalkallo, Benalla, Lang Lang, Mansfield and Sale zone substations**

Non-REFCL capex needs to be identified and properly accounted for with respect to the other four, rural zone substations included in AusNet's Tranche 3 CPA. Based on the evidence provided, it is not clear whether some of the capex forecast for the other four zone substations (Benalla, Lang Lang, Mansfield and Sale), are directly attributable to the deployment of REFCLs. Those expenditures, not directly attributable to the deployment of REFCLs should be considered as ordinary capex and therefore should not be attributed to the REFCL program.

The government recognises that the regulatory requirements and implementation schedule driving the REFCL works programs make it convenient to assess all costs through the contingent project funding process.

In principle, the CPA process should provide a mechanism for AusNet to recover those capital costs that were not sufficiently certain to be included in its EDPR capital funding allowance for the current regulatory control period. In practice, however, it appears that some general asset replacement capex (repex) and augex costs allowed in the EDPR process are being caught up in the capital cost forecasts in a CPA funding allowance.

This could have the effect of overestimating the real cost of the REFCL program, adding to the cost of electricity for Victorian consumers. The CPA process could increase costs for electricity consumers where:

- there is an overlap between REFCL-related capex funded through the contingent project process, and general 'business as usual' capex funded through the EDPR process; and
- there is no accounting mechanism in place to correct for that overlap in the assessment process for each regulatory control period.

Network planning materials developed by AusNet for its proposal for the forthcoming EDPR process underscore the government's concern about the overlap between treating capex in the CPA process rather than the EDPR process. The Victorian Government considers that some of these works should be funded through the EDPR processes.

Information provided in support of AusNet's Tranche 3 CPA suggests that the capex for these four rural substations is being driven up, in part, by the need to replace much of their plant that is very old and/or in very poor condition. For example, the CPA outlines that several substations have ageing switchgear. This includes the switchgear at Lang Lang that has suffered major internal damage due to water ingress into the control room where the equipment is housed and needs to be replaced. Another example is the inclusion of some capex to augment its 66kV plant at the substation, which is not subject to the law's 'required capacity' provisions.

Works related to replacing or upgrading electrical equipment that is very old, damaged and/or in very poor condition are not 'directly attributable' to deployment of REFCLs to meet the 'required capacity' standard mandated by the Act. Rather than including capex for these works in AusNet's Tranche 3 CPA, the costs should be recovered – or at least accounted for – as 'business as usual' capex in the EDPR determination for AusNet's 2021-25 regulatory control period.

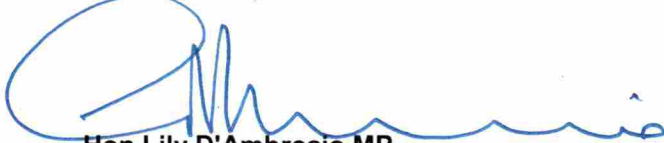
## Conclusion

The Victorian Government remains committed to ensuring that all improvements to the electricity distribution network, particularly those works that relate to implementing the government's enhanced earth fault standards, are provided at a fair and reasonable cost and all expenditures are attributed and allocated in the AER's contingent project and EDPR processes.

We trust that the AER will undertake all regulatory, technical and financial due diligence in its interrogation of the forecast capital expenditures identified in AusNet's Tranche 3 CPA.

Thank you for the opportunity to provide a submission to you on the AusNet CPA. Should you require further information please contact Lorna Mathieson, Energy Programs, at (03) 9194 4010 or at [lorna.mathieson@delwp.vic.gov.au](mailto:lorna.mathieson@delwp.vic.gov.au).

Yours sincerely,



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**Minister for Energy, Environment and Climate Change**  
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20/8/19

cc: Paula Conboy, Chair