AUSTRALIAN ENERGY REGULATOR

23 Marcus Clarke Street
Canberra ACT 2601
GPO Box 3131
Canberra ACT 2601
tel: (02) 6243 1111
fax: (02) 6243 1199
www.aer.gov.au

30 May 2018

Mr John Pierce AO
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

Re: Coordination of Generation and Transmission Investment - AER Submission on Stage 2 Discussion Paper

Thank you for the opportunity to comment on the AEMC's Coordination of Generation and Transmission Investment stage 2 discussion paper. Our submission focuses on one issue raised in the discussion paper – the role of the regulatory investment test for transmission (RIT-T). As you are aware, the AER is responsible for developing the RIT-T and associated application guidelines. These responsibilities give the AER a strong understanding of the role that the RIT-T plays, and should play, in the regulatory framework.

As noted in the discussion paper, the RIT-T is a cost benefit assessment of proposed investment options. Under the RIT-T, transmission businesses are required to assess the efficiency of proposed augmentation and replacement investment options (over a $6 million threshold) by estimating the benefits that would result for market participants and consumers, and comparing these to the associated costs. The purpose is to identify the transmission investment or alternative that maximises net economic benefits and, where applicable, meets relevant reliability standards.

We consider that this cost benefit focus of the RIT-T is very important. Transmission assets are funded by customers through network charges over the life of the asset – typically 30 to 50 years. It is important that energy customers only fund those assets that are efficient and are shielded from the risk that network investment is inefficient. The cost benefit framework in the RIT-T is designed to achieve this.

The cost benefit framework in the RIT-T serves a number of other important, related objectives. The RIT-T provides a rigorous and transparent cost benefit analysis to compare competing projects. It recognises that the project that delivers benefits to consumers could

be the network option proposed by the network business, a different network or option, or indeed a demand side or local generation option.

It is also worth noting that while some concerns are being raised with the RIT-T, the COAG Energy Council recently found the RIT-T to be a robust and appropriate mechanism to assess transmission network investments. It found that the RIT-T provides an appropriate balance between rigour and timely investment decisions.

The discussion paper also raises the issue of how the RIT-T framework and AEMO's Integrated System Plan (ISP), including Renewable Energy Zones (REZs), will work together. We consider that the ISP and the RIT-T are designed to play complementary roles.

As noted by the AEMC, a large amount of new, mostly renewable, generation is expected to connect to the network in the medium term. A detailed system plan, such as the ISP, is a very important tool in identifying where these generation sources are expected to locate and the network augmentations that may be required to accommodate them.

The RIT-T should complement the ISP by facilitating a cost benefit analysis of the projects that have been outlined in the ISP. This would potentially identify which projects deliver benefits to the market, such that consumers should fund these projects through network charges.

This intended link between the ISP and the RIT-T was identified in the Finkel Review where it is noted that "augmentations in line with the integrated grid plan would be evaluated through the RIT-T process or its successor."[1] This point was acknowledged by AEMO in its ISP consultation paper.

As noted in your directions paper, some submissions to AEMO on the ISP consultation suggested that the RIT-T process should not apply at all to projects stemming from the ISP. As highlighted above, the ISP and the RIT-T are designed to serve different purposes, with the ISP identifying potential projects and the RIT-T requiring a cost benefit assessment of projects. If a formal cost benefit analysis is not undertaken, the risks of consumers being required to fund projects that do not deliver benefits is heightened.

The RIT-T also has an accountability framework that is very different to the ISP. The National Electricity Rules set out the principles that must be applied by a network business in applying the RIT-T and details the consultation process that must be undertaken. The process of applying the RIT-T is designed to ensure that investment options proposed by network businesses can be scrutinised and contested in an open and transparent manner. Additional accountability around the application of the RIT-T is provided by the fact that RIT-Ts can be formally disputed (with the AER as the dispute resolution body) and subject to compliance and enforcement action (in the event of any breaches of the National Electricity Rules). There is no similar accountability around the ISP.

While the ISP is not a substitute for a rigorous and transparent cost–benefit analysis, we consider that the ISP may assist in streamlining RIT-T assessments. The involvement of transmission businesses in the development of the ISP should mean that the process of identifying RIT-T options for consultation should be more straightforward.

A final point highlighted in the directions paper is that similar issues are being considered through our RIT-T work (including the revision of the RIT-T application guidelines), AEMO's work on the ISP and this AEMC work on the Coordination of Generation and Transmission

[1] Independent Review into the Future Security of the National Electricity Market: Blueprint for the Future, June 2017, p.124.

Investment. We agree that is important that these issues are considered together and we look forward to working with the AEMC and AEMO.

Yours sincerely

Paula Conboy
Chair

Sent by email on: 30.05.2018