14 July 2022

Alisa Toomey
Acting Director
Australian Energy Market Commission
Level 15, 60 Castlereagh Street
Sydney, NSW 2000
(via online submission)

Transmission Planning and Investment Review – Stage 2, Draft Report Submission

Dear Alisa,

The Clean Energy Finance Corporation (**CEFC**) welcomes the opportunity to make a submission in response to the Australian Energy Market Commission's (**AEMC's**) Transmission Planning and Investment Review – Stage 2, Draft Report (the **Report**).

The CEFC is responsible for investing $10 billion in clean energy projects on behalf of the Australian Government and was established to facilitate increased flows of finance into the clean energy sector. The CEFC supports the development of a secure, reliable and affordable electricity system whilst lowering emissions through its investment activities, including large-scale renewable energy, energy storage and other initiatives in accordance with the 'grid firming' focus of our Investment Mandate. The CEFC considers the potential effects on reliability and security of supply when evaluating renewable generation investments and prioritises investments, including network solutions, that will support reliability and security of electricity supply.

Given the CEFC's unique role in the Australian energy market, we are of the view that the most valuable perspective we can bring to policy makers is as an investor who invests in the public interest with commercial considerations in mind. The observations we make are from our perspective as a financial investor (albeit one with a specific policy objective to facilitate a low-carbon transition). The views and approach of the financial investment community are critical to Australia's ability to cost-effectively fund our energy transition.

We estimate that somewhere in the order of $100 billion will be needed to fund new solar, wind, transmission, storage and ancillary services over the coming two decades. The cost of capital will be a key determinant of end-consumer charges, given the high fixed cost / low operating cost nature of the investments to be made. There is ample domestic and international capital available if the risk and return settings are appropriate for financial investors. However, we note that large financial investors are generally risk averse. Given the complexity of the Australian energy market, any market redesign should consider how it might impact the investment community's perception of risk.

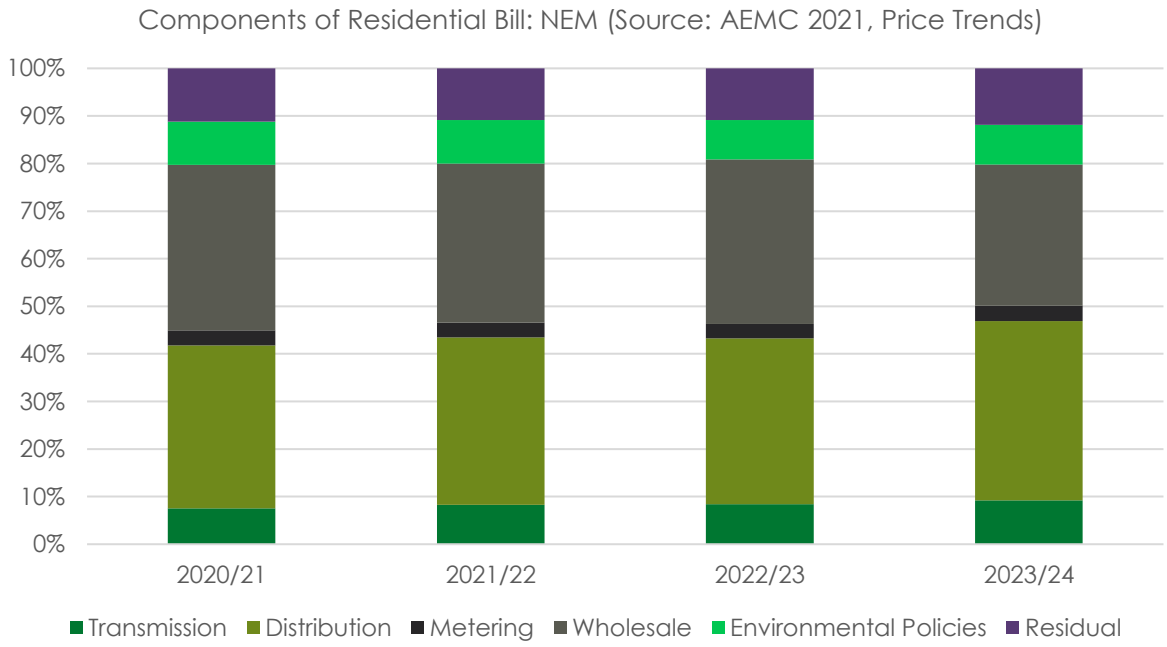
The CEFC has a strong focus on investing in essential grid expansion and augmentation as part of Australia's important renewable energy transition. The CEFC has committed market gap financing of $295 million to support the construction of Project EnergyConnect and $125 million to support the grid connection needs of Snowy 2.0.

Our submission focuses on issues that are most relevant to our role and experience as a clean energy investor, and notably, our recent experience in financing transmission projects.

Context

We are supportive of the view that the assessment and validation of the impact of network investment on consumers is important. We would note that based on the historical data, the impact of transmission investment for consumers has been frequently found to be positive. It is difficult to identify major transmission projects, particularly interconnectors, that have not provided tangible benefits to consumers. Historical concerns of over-investment can typically be differentiated between the outcomes achieved in the distribution network, as opposed to the transmission network. Timely investment in enabling transmission assets will be critical for Australia to ultimately achieve an orderly and efficient energy transition as we move towards net zero.

As shown in AEMC analysis (figure below), transmission costs are expected to make up less than 10 per cent of residential bills to 2023/24. The currently unfolding increase in wholesale costs may see this percentage reduce further.



Flexibility of revenue framework: financeability

The CEFC agrees that financeability challenges could arise due to the large scale and immediacy required of ISP investments. We view that the unprecedented speed and scale of increases in regulated asset bases of TNSP's relative to their current business will distort cash flows and risk profiles that may impact credit ratings to the downside.

The risk profile of large scale greenfield actionable ISP projects are distinct from business-as-usual TNSP capital expenditure. CEFC believes that there is merit in considering incentives such as accelerated depreciation to TNSPs to compensate for the increased risk profile. In the absence of amendments to the rate of return instrument, reviewing the depreciation rules may meaningfully address financeability challenges, where:

1) The cash flow profile achieved under a revised depreciation profile is adequate to address relevant credit metrics (where applicable); and

2) Importantly, the regulatory framework provides TNSPs with sufficient certainty of their cash flow profile with enough lead time (6-12 months ahead of the final investment decision) to allow them to consider the impacts of the investment on their corporate strategy, engage with credit rating agencies (where applicable) and engage with the financial community to raise the necessary debt and equity capital. Where the AER has the discretion to apply (or not) an alternative depreciation profile (for example, through the Commission's proposal that a variation of depreciation profile is only to be used by the AER in 'exceptional circumstances' where the 'consumer benefits of timely investment outweigh the short-term negative impacts') this introduces a degree of uncertainty, which increases risk and may lead to delays in investment decisions and ultimately delays in the delivery of transmission projects. If a key objective of the TPIR is to provide greater investment certainty and timely delivery for transmission investment, CEFC would suggest that the AEMC establish pre-determined prescribed parameters to provide TNSPs with certainty to progress their transmission investments and avoid increases in costs arising from delay.

In developing a pre-determined framework, relevant factors to consider include the following:

1) The net dollar impact on consumers, given the significant benefits of transmission investment and the relatively small difference between the net market benefits associated with the Optimal Development Pathway (**ODP**) and the least favourable pathway in the context of the transition task ahead. The Final 2022 ISP shows there is a significant net market benefit of $28 billion associated with building the ISP projects, with the difference between the ODP and least favourable pathway being equivalent to an approximately 2% variation[1].

   We consider that the risk of delay (resulting in threats to energy reliability and higher wholesale price impact with a generation shortfall as coal retirements occur) outweighs the potential short term customer bill impact. We note recent analysis that found on average NEM-wide, households would pay a total of approximately $600 more in electricity bills over a 15-year period if the expected transmission build-out is delayed by 2 years.[2]

2) When considering the benefits of timely investment this should include an analysis of the cost of delay and should also be assessed across the entire customer bill (i.e. including impact on wholesale power prices) rather than being confined to the transmission-related impact. Our view is that this would reflect the true overall potential cost to consumers and is more appropriate as a means of measuring costs / benefits for an electricity system undergoing transformational change.

3) When considering issues of intergenerational equity, we also note that whilst not currently assessed by the AER under the NEL / NER, there are also intergenerational equity issues to consider in relation to greenhouse gas emissions. Where a delay in

[1] Except in the case where Marinus is removed from the ODP and net benefits drop by approximately 14%.

[2] https://nexaadvisory.com.au/site/wp-content/uploads/2022/06/Report-Modelling-Electricity-bill-impact-due-to-transmission-delay_2022-06-07.pdf

transmission buildout delays investment in renewable generation and emissions reductions, this in turn contributes to the additional costs borne by future generations.

Cost recovery for preparatory activities

We note the Commission's draft position that the existing framework provides the appropriate tools to manage uncertainty in cost recovery for preparatory activities. In particular, it is understood that preparatory activities may be nominated as a cost pass-through under existing arrangements, and the staged Contingent Project Application ('**CPA**') process provides a means of managing cost recovery uncertainty for actionable ISP projects.

We largely agree with this position but note the need to ensure that the framework is effective in practice – if jurisdictions still need to underwrite preparatory activities despite the increased clarity around definitions of planning activities proposed under the Report, then AEMC should revisit this item. A further review in, for example, 2 years' time after these changes are legally effective may be appropriate.

Feedback loop

We would be supportive of the CPA process and the feedback loop running concurrently to minimise delays in delivering actionable ISP projects.

Overall, we note while inputs, assumptions and scenarios will continue changing, it is important to take a view at a point in time by 'locking down' these variables in order to facilitate timely investment decisions on the actionable ISP projects.

Further engagement / consultation

We very much value the opportunity that the AEMC has provided to enable the CEFC to provide input into this process. Should you wish to discuss this submission further, please contact Owen Pascoe (Associate Director – Research): owen.pascoe@cefc.com.au.

Yours sincerely

Ian Learmonth
Chief Executive Officer