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Dear John

### **Submission on Reform of Regulatory Test Principles**

VENCorp welcomes the opportunity to comment on the Australian Energy Market Commission's (AEMC) Draft Rule Determination on the Reform of the Regulatory Test Principles.

VENCorp is unique in the National Electricity Market as it is the only network planner that carries out an assessment of the market benefits of all proposed new network augmentations.

VENCorp broadly supports the proposed changes to the National Electricity Rules (Rules) and the principle of codifying Regulatory Test principles, but has the following concerns with the proposed draft Rules.

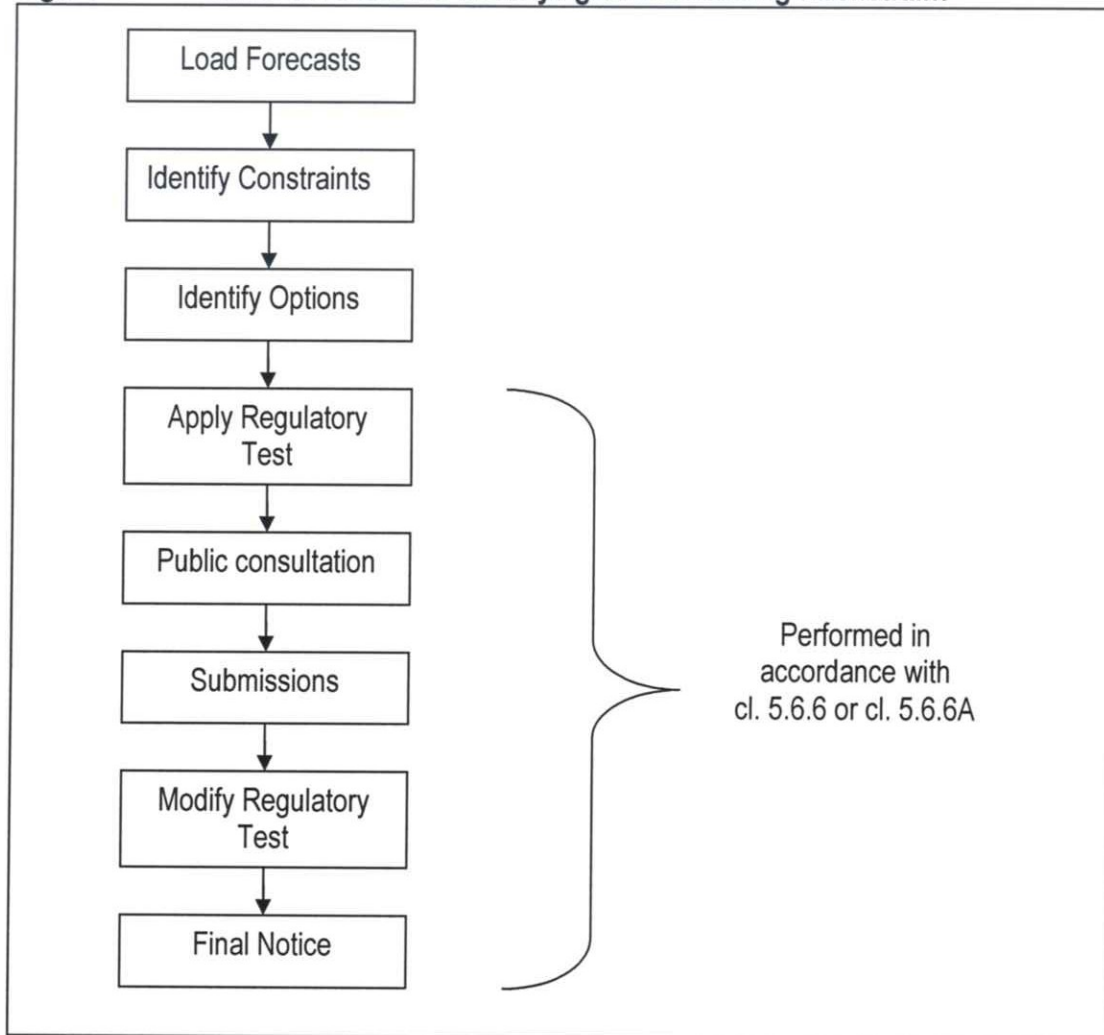
#### **The Proposed Request For Information Process**

The AEMC proposes to require that a Request For Information (RFI) process be undertaken as part of the market benefits limb of the regulatory test. The intent of the RFI process is to ensure that all the alternative options to a proposed augmentation have been considered by a Network Service Provider (NSP).

VENCorp supports the principle of requiring a NSP to undertake a public process that encourages interested parties to propose workable, commercial alternatives to a proposed network investment.

However, VENCorp is concerned that the RFI process requires a NSP to identify the optimal new network investment *before* considering all genuine and practicable options. Under the current regulatory test process VENCorp identifies a system constraint and a number of potential options to address it. The regulatory test is then applied so as to select the optimal solution to the system constraint and modified as necessary following a public consultation process. This process is set out in Figure 1 below.

**Figure 1** Current Process for identifying and addressing a constraint

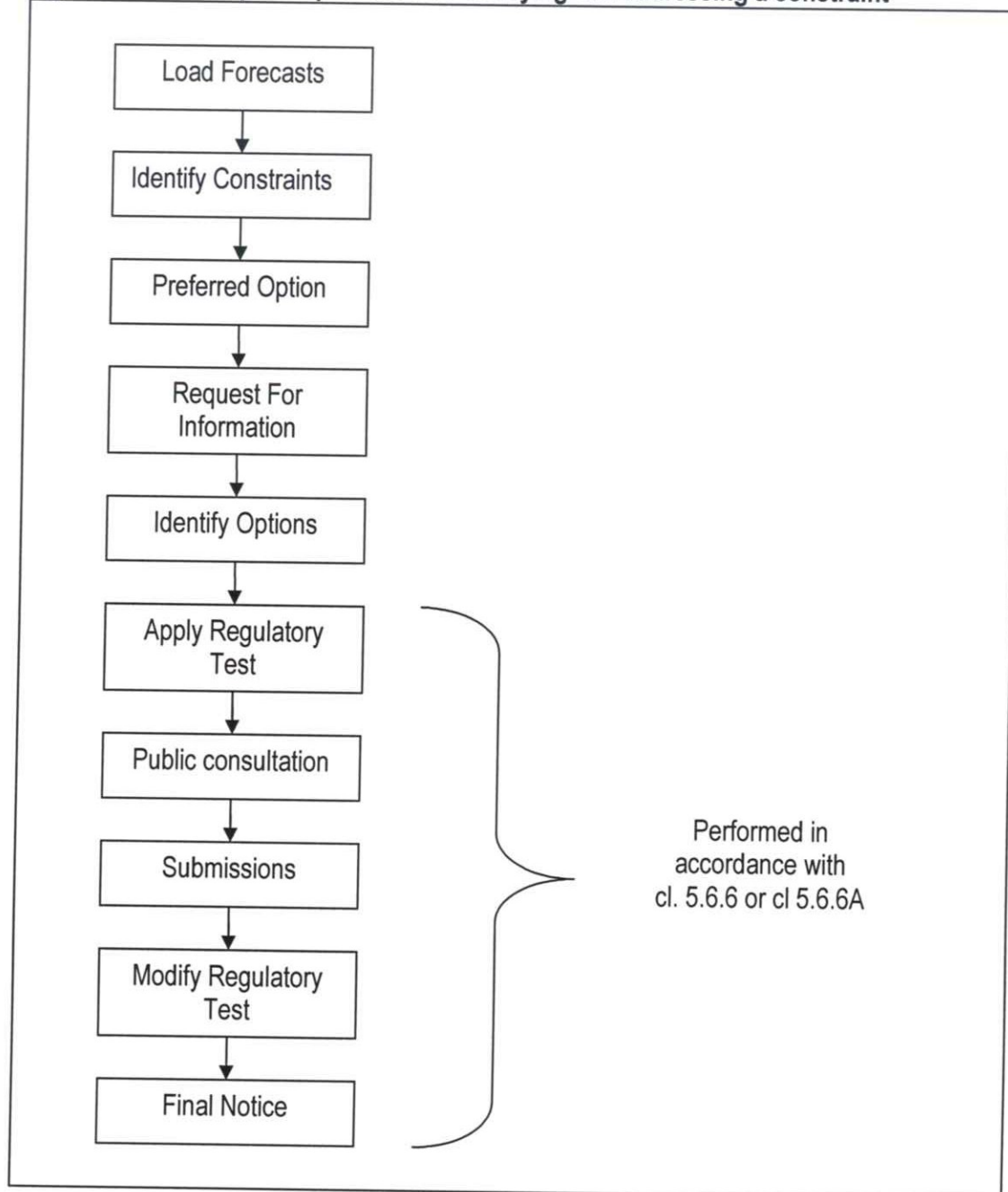


On its face, the proposed RFI process would first require the NSP to identify a problem or opportunity *and* propose an optimal new network investment to address it. The following RFI would then seek alternative projects to the proposed new network investment. The AEMC then states that:

*“the proposed project satisfies the Regulatory Test , it may proceed. If an alternative option has a higher net market benefit, the proposed project fails the Regulatory Test and does not proceed.”* (see page 58 of the Draft Determination)

In turn, the proposed project and the associated cost-benefit analysis of the regulatory test would then be subjected to the disclosure requirements of clauses 5.6.6 and 5.6.6A. Therefore, the proposed new network investment would be published by the NSP twice. VENCORP’s understanding of the proposal is outlined in Figure 2.

**Figure 2** Proposed process for identifying and addressing a constraint



It is questionable whether the approach proposed by the AEMC delivers benefits as it will effectively require the NSP to pre-judge the outcome of a regulatory test assessment.

VENCorp suggests that the AEMC should consider the following changes to the RFI process:

- that the NSP be required to publish a problem or opportunity and request possible approaches to solve the problem and *not* identify the proposed new network investment at that time; and
- that any other informational requirements, such as details of the proposed new network investment, be included in the disclosure requirements of clauses 5.6.6 and 5.6.6A.



VENCorp also supports the AEMC introducing a similar arrangement for augmentations assessed against the reliability limb of the regulatory test.

### **Alternative Options**

The draft Rules introduce a number of process requirements that an NSP must adhere to for a new network investment to pass the regulatory test, including:

- the requirement to publish details of the proposed new network investment - clause 5.6.6(d)(1); and
- the “with and without test” where the proposed new network investment is the basis for selecting which alternative options are included in the counterfactual – clause 5.6.6(b).

VENCorp understands that as a consequence of these process requirements if, in the course of the RFI or clauses 5.6.6 or 5.6.6A consultation processes, an alternative option is found to have higher net market benefit than the new network investment which was being proposed, then the NSP’s finding must be that the new network investment does not satisfy the regulatory test. The NSP cannot accept the alternative option as having satisfied the regulatory test. The effect of this would be to have the NSP re-consult on the option beginning at the RFI process.

This is contrary to the manner in which the regulatory test is currently performed where a number of network and non-network options are considered to address an identified problem.

VENCorp seeks clarification from the AEMC as to whether an alternative option satisfies the requirements of the regulatory test.

### **Requirements of the Regulatory Test**

Clause 5.6.5A(c)(1) of the Draft Rules requires that the market benefit limb of the regulatory test must:

“be based on the cost-benefit analysis of the future were the *new network investment* to take place, compared to the likely alternative outcome or outcomes, were the *new network investment* not to take place;’

VENCorp understands that the intent of the clause is to create a:

“higher hurdle for alternative projects, which should limit the ability of a project which is purely speculative or unlikely to proceed, from being used to block a proposed transmission augmentation.” (page 59 of the AEMC report)

VENCorp notes that clause 5.6.5A(c)(1) introduces the terms “likely” and “alternative outcomes” into the market benefit limb of the regulatory test. VENCORP questions whether the current wording of this clause provides sufficiently clarity to the AER when amending the regulatory test. In particular, it is not clear whether the term ‘alternative outcome’ is intended to refer to the ‘outcome’ of a new investment under the (most) likely market development scenario, or to an alternative investment proposal itself.

Furthermore, VENCORP is unsure of the role that market development scenarios have in the new market benefits limb of the regulatory test. VENCORP notes that market scenarios are an important component of the current regulatory test and provides a level of certainty that the optimal project is selected given the inherent uncertainty of future market developments.

## **Guidelines for the Application of the Regulatory Test**

Clause 5.6.5A(h) of the draft Rules compel the AER to develop and publish guidelines for the application of the regulatory test.

VENCorp believes that published AER guidelines on the regulatory test would assist in the uniform application of the test. VENCorp strongly supports this proposed requirement.

## **Application of reliability limb of the Regulatory Test**

In the Draft Rule Determination the AEMC sought submissions on the issue of whether the proposed approach to the assessment of alternative projects under the market benefit limb should also be applied to the reliability limb of the regulatory test.

VENCorp supports a consistent application of the regulatory test to all network augmentations. A consistent application of the regulatory test minimises the possibility of investment distortions.

Should you have any questions please don't hesitate to contact Mr Louis Tirpcou on (03) 8664 6615.

Yours sincerely



Matt Zema  
**Chief Executive Officer**