



24 February 2006

Dr John Tamblyn
Australian Energy Market Commission
PO Box H166
AUSTRALIA SQUARE NSW 1215

By email: submissions@aemc.gov.au

Dear Dr Tamblyn

REFORM OF REGULATORY TEST PRINCIPLES: AUSTRALIAN ENERGY MARKET COMMISSION CONSULTATION ON THE MINISTERIAL COUNCIL OF ENERGY PROPOSED RULE

Stanwell welcomes the opportunity to respond to the consultation by the Australian Energy Market Commission (**AEMC**) on the Rule proposal lodged by the Ministerial Council on Energy (**MCE**) concerning reform of the Regulatory Test.

Stanwell noted in its response to the Chapter 6 review currently being conducted by the AEMC the importance of accurate price and non-price signals in the National Electricity Market concerning network services that provide incentives to generators to behave efficiently. In particular, the submission concerned Rule reform to reduce risks for generators caused by network reconfigurations.

This submission raises a related, but separate, issue concerning the reform of the regulatory test principles. Stanwell considers that by focusing on the fact that the NEM's networks are generally growing, the Regulatory Test regime has a glaring gap or loop-hole in respect of major network reconfigurations or replacements.

Stanwell regards this issue, and the proposals to address it contained in this submission, to fall within the ambit of the AEMC's consideration of the MCE's Regulatory Test because the issues raised in this submission are closely intertwined with those raised by the MCE. However, if it is the AEMC's view that the material submitted is not within that ambit:

- (a) Stanwell itself applies for a Rule to address the issues raised pursuant to section 91(1) of the National Electricity Law; and
- (b) submits that its application should be considered with the MCE's proposal pursuant to section 93 of the National Electricity Law.

For the purposes of Regulation 8(1) of the *National Electricity (South Australia) Regulations* (as amended by the *National Electricity (South Australia) Variation Regulations 2005*) the request is made by Stanwell Corporation, xx Eagle Street, Brisbane, Queensland, 4000.

1. ROLE OF THE REGULATORY TEST IN THE RULES' REGULATORY SCHEME

The role of the Regulatory Test is to promote efficient network planning decisions with respect to:

- whether expenditure is warranted or net beneficial; and if so
- which project should be pursued or preferred.

Rule 5.6.6(b) provides that "an analysis of the ranking of the proposed *new large transmission network asset* and all reasonable alternatives [must be undertaken by the applicant] in accordance with the principles contained in the *regulatory test*".¹

A new large transmission network asset is an "asset of a *TNSP* which is an *augmentation* and in relation to which the *TNSP* has estimated it will be required to invest a total capitalised expenditure in excess of \$10m."²

An *augmentation* is "works to enlarge a network or to increase the capacity of a *network* to transmit or distribute *active energy*" (emphasis added).

Generally speaking NEM networks are continually growing and, therefore, the above requirements to undertake the regulatory test have by-and-large applied where there are significant expenditures to be undertaken.

¹ Rule 5.6.6A provides that the AER must take into account, in the context of setting the revenue cap for a transmission network service provider whether each *new small transmission network asset* identified in the Annual Planning Report satisfies the regulatory test and there are analogous concepts for distribution network assets.

² A *new small transmission network asset* has a similar meaning but with an expenditure in excess of \$1m and there are analogous concepts for distribution network assets.

However, significant expenditures need not always entail “enlargements” and “increases in capacity”. As well as the tendency for networks to be ever expanding, there are also many aging network links that have reached, or will reach, the end of their useful lives. Transmission assets are generally long life assets and in the half century or more that typically elapses between the building of an asset and the need for it to be replaced, loads or generation can have grown, shrunk or shifted, the terrain can have altered or the regulations concerning land use and network routing can have altered. Therefore, when rebuilding or replacing a network, the question arises anew as to whether that infrastructure continues to be efficient and the relative merits of different network options again becomes relevant.

From a policy perspective exactly the same issues arise concerning substantial replacement, reconfiguration and rebuild works:

- *whether* expenditure is warranted or net beneficial; and if so
- *which* project should be pursued or preferred.

The same regulatory framework should apply to such substantial replacement, reconfiguration or rebuild projects.

Many of the costs and benefits of particular network augmentations which are taken into account in the application of the regulatory test are the costs and benefits accruing to network users. Similarly, network planning decisions concerning whether and how assets are replaced or reconfigured have profound costs and benefits to network users.

The next section sets out from a generation perspective why it is important for the regulatory test to apply to replacement, reconfiguration or rebuild projects. Stanwell would expect that analogous considerations would arise in respect of loads.

2. IDENTIFICATION OF ISSUE AND EXPLANATION OF HOW THE PROPOSED RULE ADDRESSES THIS ISSUE

In making an initial investment in a generating facility a number of factors will influence this decision, with one of the most critical factors including the capacity, reliability and effective cost of evacuating power through the transmission network from that location. Similarly, substantial ongoing investments are typically made such as expanding the generating capacity of the facility or maintaining its compatibility with the system as a whole.

The generator faces the risk that the transmission network service provider may decide to reconfigure the transmission network in a manner that is deleterious to the generator. A

decision by a transmission network service provider to reconfigure the transmission network in the area in which a generator is located may harm a generator in two ways:

- first, it may result in assets that were previously shared network assets being reclassified as connection assets, the costs of which may be sought to be recovered from an individual generator;
- second, where a generator may have previously had access to the transmission network at a number of points, it may result in a change to these lines such that while the generator is still connected to the transmission network, the generator is unable to offer particular services that it was previously able to offer such as black start services or the reliability of its connection may be reduced.

This risk can only effectively and efficiently be managed through the National Electricity Rules governing network planning, connection and pricing. The first matter was the subject of Stanwell's submission to the AEMC's Chapter 6 review concerning electricity transmission revenue and pricing rules. The second is the subject of this submission.

The most appropriate way to take into account the impact that reduction or reconfiguration of the transmission network may have on generators would be to make it explicit through the reform of the regulatory test principles that the regulatory test is to apply to network investment that involves not just augmentation of the network, that is enlargement of the network or an increase in the capability of a network, but also reconfigurations of the network. Stanwell's proposed approach is outlined below.

3. REFORM PROPOSAL CONCERNING THE REGULATORY TEST

The Rules should provide that the regulatory test must be undertaken not only in the context of augmentations but also reconfigurations.

The attachment to this submission proposes specific wording.

4. HOW THE PROPOSAL CONTRIBUTES TO THE ACHIEVEMENT OF THE NATIONAL ELECTRICITY MARKET OBJECTIVE

The National Electricity Market Objective is set out in section 7 of the National Electricity Law, and is reproduced below.

The national electricity market objective is to promote efficient investment in, and efficient use of, electricity services for the long term interests of consumers of electricity with respect to price, quality,

reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.

Under the National Electricity Law, the AEMC has rule making functions and powers in respect of the National Electricity Rules. In performing or exercising these functions and powers the AEMC must have regard to the National Electricity Market objective.³

The Rule change proposed above will contribute to the National Electricity Market Objective as:

- (a) the proposed Rule will operate in such a way as to decrease the riskiness of already risky investments by generators in establishing, maintaining and expanding generation facilities, ensuring that decisions regarding removal or reconfiguration of the transmission network are transparent and that any costs from the proposed removal or reconfiguration of the transmission network in terms of the inability of generators to offer ancillary services is recognised;
- (b) in helping to ensure that efficient investment is not deterred, the proposed Rule should encourage competition in the upstream generation market, with consequential benefits in terms of price and quality for consumers of electricity, as well as enhancing reliability and security of supply;
- (c) the proposed Rule will not effect the ability of the transmission network service provider to configure its network in the most efficient way – but it does require such providers to take into account the costs of reductions or reconfigurations of the transmission network in terms of any consequential inability of a generator to provide ancillary services – ensuring that the long term interests of consumers are promoted.

Should you have any questions in relation to this submission please contact Denis Warburton on (07) 3335 3846.

Yours sincerely



Andrew Bills

General Manager Marketing and Trading

³ Section 32 of the National Electricity Law.

ATTACHMENT A: AMENDMENTS TO THE DEFINITIONS IN CHAPTER 10

new large distribution network asset

An asset of a *Distribution Network Service Provider* which is an *augmentation or network replacement or reconfiguration* and in relation to which the *Transmission Network Service Provider* has estimated it will be required to invest a total capitalised expenditure in excess of \$10 million, unless the *Jurisdictional Regulator* for the *participating jurisdiction* in which the relevant distribution network is located publishes a requirement that a *new large distribution network asset* is to be distinguished from a *new small distribution network asset* if it involves investment of a total capitalised expenditure in excess of another amount or satisfaction of another criterion. Where such a specification has been made, an asset must require total capitalised expenditure of that amount or satisfaction of those other criteria to be a *new large distribution network asset*.

new small distribution network asset

An asset of a *Distribution Network Service Provider* which is an *augmentation or network replacement or reconfiguration* and:

- (a) in relation to which the *Distribution Network Service Provider* has estimated it will be required to invest a total capitalised expenditure in excess of \$1 million, unless the *Jurisdictional Regulator* for the *participating jurisdiction* in which the relevant distribution network is located publishes a requirement that a *new small distribution network asset* if it involves investment of a total capitalised expenditure in excess of another amount or satisfaction of another criterion. Where such a specification has been made, an asset must require total capitalised expenditure of that amount or satisfaction of those other criteria to be a *new small distribution network asset*; and
- (b) is not a *new large distribution asset*.

new large transmission network asset

An asset of a *Transmission Network Service Provider* which is an *augmentation or network replacement or reconfiguration* and in relation to which the *Transmission Network Service Provider* has estimated it will be required to invest a total capitalised expenditure in excess of \$10 million, unless the *AER* publishes a requirement that a

new large transmission network asset is to be distinguished from a *new small transmission network asset* if it involves investment of a total capitalised expenditure in excess of another amount or satisfaction of another criterion. Where such a specification has been made, an asset must require total capitalised expenditure of that amount or satisfaction of those other criteria to be a *new large transmission network asset*.

new small transmission network asset

An asset of a *Transmission Network Service Provider* which is an augmentation or network replacement or reconfiguration and:

- (a) in relation to which the *Transmission Network Service Provider* has estimated it will be required to invest a total capitalised expenditure in excess of \$1 million, unless the *AER* publishes a requirement that a *new small transmission network asset* if it involves investment of a total capitalised expenditure in excess of another amount or satisfaction of another criterion. Where such a specification has been made, an asset must require total capitalised expenditure of that amount or satisfaction of those other criteria to be a *new small transmission network asset*; and
- (b) is not a *new large transmission asset*.

network replacement or reconfiguration

Works to:

- (a) maintain the size or capability of a network to transmit or distribute active energy, or
- (b) re-route the path, technical capabilities or usability for Network Users of all or parts of the network.

[Drafting Note: The definition of network replacement or reconfiguration is based on the definition of augmentation.]