

Ref: ERC0192

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Ms Claire Richards
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Australian Energy Market Commission
PO Box A2449
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Dear Claire

re: Response – Draft Determination on Transmission Connection and Planning Arrangements Rule Change Proposal

As the primary transmission business in South Australia ElectraNet welcomes the opportunity to provide this submission to the Australian Energy Market Commission's (AEMC) Draft Determination on the Transmission Connection and Planning Arrangements Rule Change Proposal. ElectraNet is also a member of Energy Networks Australia and so endorses the submission it has prepared for this consultation. The purpose of this submission is to provide additional comments on the specific connection related matters of the Draft Rule.

A key outcome of the rule change will be an extension of contestability for the provision of assets that form part of the shared transmission network (the Identified User Shared Assets) and, as such, were previously undertaken only by local Transmission Network Service Providers (TNSPs). While ElectraNet accepts that extending contestability to these assets has the potential to promote the National Electricity Objective (NEO), this will involve extending contestability to assets whose design and operation can impact substantially on the shared network, and so it is critical for the advancement of the NEO that the adoption of a contestable framework is implemented carefully.

This means ensuring:

- The risks created through contestability are minimised, properly allocated, and able to be managed in the best possible way, including that providers/purchasers of contestable services are exposed accurately to the costs associated with their choices. This is a particular issue in the context where the design, construction and ownership of the Identified User Shared Assets is proposed to be separated from their subsequent operation and maintenance;
- That the rules framework and associated allocation of roles and responsibilities are sufficiently clear and transparent as to not repeat the concerns raised by stakeholders through the Transmission Frameworks Review that the current arrangements are overly complex and ambiguous and so increase the costs of negotiation as well as the prospects for conflict, and

- The competitive benefits sought from the rule changes cannot be undermined by inappropriate ring-fencing arrangements, noting in particular the potential (which would come from applying distribution based ring fencing measures to transmission) for the intended coordinated operation of the whole of the shared transmission network to be precluded and the further potential for some local TNSPs to need to withdraw from competition to provide contestable services.

The remainder of this submission sets out ElectraNet's comments on specific matters related to the proposed changes to the connection arrangements.

Arrangements for IUSAs

The Draft Rule creates a new defined term called 'Identified User Shared Assets' (IUSA). These assets were previously provided by TNSPs as a monopoly service and subject to a negotiate / arbitrate regulatory regime. The Draft Rule makes the provision of these assets contestable where a threshold is met and in doing so removes the application of the negotiate / arbitrate regime. ElectraNet endorses the AEMC's decision to create a level playing field for the contestability of IUSAs. Equally, removing the requirement for TNSPs to provide these as monopoly services under a negotiate / arbitrate regime in a competitive market ensures that TNSPs are not exposed to obligations that their competitors are not exposed to.

The Draft Rule also requires that TNSPs maintain responsibility for the operation and maintenance of IUSA's even where they are designed, built and owned by a third party provider. While ElectraNet maintains the view expressed in previous submissions to which it has been party that aligning the responsibility for operation and maintenance with the construction and ownership of the assets is the best way to ensure that connecting parties take into account the long term implications of their design and investment options, it recognises the desire of jurisdictions to hold a single party accountable for shared transmission network outcomes, particularly in light of recent events.

If the separation of roles is maintained in the Final Rule, it is necessary that it be implemented in a way that minimises the risk of harm to the shared system. That is, the security and reliability of electricity for electricity customers over the long term needs to remain a primary objective. Further, it is necessary also that shared network customers and TNSPs do not bear the burden from the misallocation of the risks or costs imposed by the separation of shared network roles.

Minimising and managing the risks of separation between design/construction and ongoing operation and maintenance

The potential exists for shared network users to be exposed to risks, and TNSPs exposed to risks and costs, as a consequence of permitting shared network assets to be designed and constructed by a party other than the local TNSP. This is particularly the case where the TNSP is required to undertake the ongoing operation and maintenance of assets that it has not designed or constructed.

The risks and costs include:

- Poor quality assets that expose shared network customers to greater risks of network failure and / or increased maintenance costs;
- Network remediation costs that may be incurred at the end of the connection agreement;
- In the event spares are not obliged to be held by the IUSA owner, the need for the primary TNSP to hold spares for non-standard assets in the context of its network¹;and

¹ ElectraNet notes also that in any event, any spares related to an IUSA that are held by the TNSP, even those that are consistent with the TNSPs network, will need to be costed on a stand-alone basis and fully allocated to the connecting party.

- The need for primary TNSP staff to be trained with respect to alternative design solutions, technologies, and / or equipment brands.

The current Draft Rule contains a number of uncertainties with respect to the arrangements for the separate ownership and operation and maintenance of IUSAs. If these uncertainties persist, in addition to increasing the costs associated with contract negotiation, they will increase the potential for inappropriate risks being imposed on participants and/or customers.

For example:

- It is not clear if TNSPs are able to define the maintenance standards and the impact these may have for the shared network;
- There is no clarity about who bears the responsibility for holding spares and also specifying what spares are required to be held;
- There is ambiguity around what contractual arrangements and connection agreements are required; particularly in a circumstance where the connection applicant does not own the IUSA, and
- TNSPs will be required to publish a number of ‘standard’ versions of agreements, such as connection agreements or operation and maintenance agreements. However, the concept of there being a ‘standard’ agreement is inconsistent with the many scenarios for ownership and connection design of various aspects of a connection that are possible under the new framework. As such, it is not clear what the AEMC actually expects to be published in this regard that will be of practical use to connecting parties for the purposes of contract negotiations.

In light of the uncertainties of the current design, as well as the potential costs and risks, ElectraNet therefore recommends two refinements to the AEMC model.

First, allow the functional specification to:

- Place bounds around the choice of equipment, and hence obviate the most likely source of risk and conflict;
- Define the maintenance standard that will be required and so what this means for the retention of spares and related matters; and
- Provide information to any third party supplier about how their detailed design choices will affect the operating and maintenance cost associated with the IUSA, and thereby make an informed choice.

Secondly, strengthen the principles for negotiated services to clarify the ability of the TNSP to recover the actual prudent cost of operating and maintaining a third party’s IUSA; including via pass-through arrangements where necessary.

In relation to the upfront guidance that the TNSP is able to provide in the **functional specification**, it is necessary that this properly reflect the full role that has been assigned to TNSPs. The TNSP’s role is much more than merely an outsourced maintenance service provider. Under the Draft Rule TNSPs are responsible for operating and maintaining assets to a standard that achieves seamless operation of the shared network. More specifically, proposed new clause 5.2A.7(d)(6) requires that a third party IUSA be treated as forming part of the primary TNSP’s transmission network in all material respects. Consequently, to avoid further risk and cost being imposed, the TNSP requires control over the asset management approach. This will allow the asset management approach for

connection assets to be integrated with the overall asset management approach for the shared network.

Achieving this requires that the guidance in the functional specification include identifying:

- Acceptable technology solutions
- Acceptable equipment suppliers, and
- The standard equipment employed in the network and for which appropriate spares are carried, with the implication that non-standard equipment may be costlier to operate and maintain, and require dedicated spares that are more costly for the TNSP procure than its usual inventory.

In relation to the **negotiated service principles**, ElectraNet recommends that, as for above standard or below standard transmission services, a provision should be included in the new Schedule 5.11 to make it clear that if the negotiated transmission service is for the operation and maintenance of an IUSA that the price must allow the recovery of the actual, prudent cost, associated with the operation and maintenance of the IUSA. This would include any additional costs (such as preparation of additional plans/training and holding of spares) as a consequence of the third party choosing non-standard equipment together with the pass-through of costs where certain operation or maintenance events occur². This is to put it beyond doubt that these are costs caused by the connecting party and so should be incurred by that party.

Retaining the efficiency and operational benefits of an integrated TNSP entity

The AEMC's Draft Rule is premised on the local TNSP being able to achieve the economies of scale and scope that come from it providing prescribed transmission services, negotiated transmission services and contestable network services. That is, having a TNSP provide each of these services within its current structure is deemed to be the best way to promote the NEO, while opening up more of these services to competition. Specifically, it recognises that TNSPs are best placed to deliver a safe, secure and reliable network in the most efficient way, but also that their participation in the market for contestable services is highly desirable in terms of creating competition for those services and in turn promoting efficient solutions for customers.

The AER recently amended the ring-fencing arrangements that apply to distribution businesses. Specifically, the AER's approach in distribution has been to require separate staff (as well as offices and brand name) between those involved with the provision of prescribed services and those involved with negotiated or non-regulated distribution services. If these arrangements were imposed onto TNSPs in the same form it would mean that the AEMC's preferred framework set out in the Draft Rule may be undermined and the benefits of that approach may consequently be lost.

There are clear differences between distribution and transmission services that justify a different approach to ring-fencing. For transmission, negotiated services and unregulated connection services are core network services that require the same skill set and types of assets as prescribed transmission services. The main difference being that negotiated services and unregulated connection services are for identifiable and separable customers rather than for the broader shared customer base.

² Where a TNSP owns the assets it will take on the risk associated with certain operation or maintenance events occurring. However, this is less feasible where the TNSP is required to operate and maintain different design solutions and non-standard assets. As such, similar to pass-through arrangements for prescribed transmission services, it may be more efficient for costs to be passed-through to connected parties when events occur rather than for this to be factored into the price up-front. ElectraNet considers it is beneficial for this potential to be recognised up-front in the Rules.

Conversely, distribution unregulated services, and even some negotiated distribution services, are services that may interact with the network but are not necessarily core network services. These include metering, solar panel supply, distributed generation, street-lighting and the provision of other emerging technologies. This means that the competition concerns, as well as the costs and benefits associated with imposing severe ring-fencing arrangements, are materially different between transmission and distribution.

For instance, the safety, security and reliability of the distribution network is much less dependent on whether or not distributors are participants in the market for solar panels or street lights. Further, it is more feasible for these services to be provided by independent teams within an organisation given the different skill sets they require relative to core network services, and the scale and scope of these services.

ElectraNet considers that given the significance of the role of TNSPs in the proposed contestable connection services framework, and that the promotion of the NEO under the Rule is premised on TNSPs undertaking the functions given to them, it is important for the AEMC to affirm this in its Final Determination. Specifically, the AEMC should at a minimum include explanatory statements that guide the AER's consideration of the approach to ring-fencing for TNSPs so that it is fully aware of the costs that would be imposed by repeating the distribution arrangements. More preferably, ElectraNet recommends that this intent be reflected directly in the rules. This issue is addressed further below.

Ring fencing for monopoly connection services

Under the Draft Rule, TNSPs would be obliged to undertake certain services as a monopoly with these subject to a negotiate / arbitrate regulatory framework (i.e. negotiated transmission services). These services include cut in works, preparation of functional specifications, operation and maintenance functions and provision of IUSA's below \$10m or that are not new or a complete replacement and not distinct and definable from the existing transmission network.

The key justification for assigning certain roles to TNSPs as a monopoly service – and most notably the obligation to undertake the ongoing operation and maintenance of a third party's IUSA – is the view that the seamless operation of the shared network (and a single point of accountability) is highly desirable. Specifically, the AEMC stated that the regulatory framework must deliver a safe, reliable and secure shared transmission network and that this is best achieved where there is clear accountability on incumbent TNSPs undertaking negotiated transmission services seamlessly with prescribed transmission services:³

Given the criticality of system safety, security and reliability, accountability for outcomes on the shared transmission network should be clearly defined. This is best achieved when one party is singularly accountable for shared network outcomes. The incumbent TNSP is, relative to others, best placed to manage its obligations under the NEL, Rules and jurisdictional electricity legislation with regard to the provision of a safe, reliable and secure transmission system. It follows that an explicit assumption in the AEMC's model is that these negotiated transmission services are undertaken by the TNSP seamlessly with its prescribed service activities.

As indicated above, the AER's ring fencing model for distribution requires functional separation (technical staff and offices) between the equivalent of prescribed and negotiated services. If the same distribution model was applied to transmission, then the AEMC's objective of seamless operation could not be met.

³ AEMC, 'Transmission Connection and Planning Arrangements, Draft Rule Determination', 24 November 2016, p.43.

Therefore, the AEMC should make it clear that if ring-fencing arrangements meant that there could not be a seamless operation of both prescribed transmission services and negotiated transmission services that the promotion of the NEO would be threatened. Indeed, given the potential risks to the promotion of the NEO through inappropriate ring-fencing arrangements, ElectraNet recommends that the AEMC seek to protect the efficiency benefits of the contestable connection services model through the Rules. This could take the form of a requirement in the ring-fencing rules along the following lines:

Any ring fencing requirements with respect to services for the transmission system must not be inconsistent with the same technical staff and senior management having responsibility for, and making decisions in relation to, the operation of a TNSP's shared transmission network.

The purpose of the additional guidance is to provide an assurance that any ring-fencing arrangements that are put in place are consistent with how the regulatory framework for connections and the broader shared network is intended to operate. Without such guidance it would be possible for a review of ring-fencing arrangements to be launched at a future time that would undo the framework that the AEMC is establishing as part of this process; bringing with it additional inefficient costs and risks for customers and TNSPs.

Moreover, ElectraNet understands the basis of the AER's approach to ring-fencing in distribution was to address concerns about cost allocation and any competitive advantages, such as access to information, that may be available for the distribution business. These are not concerns for the monopoly services that TNSPs are required to provide with respect to connections.

Firstly, in transmission, there is no scope for competitive provision of negotiated services and so competition concerns cannot exist. The reason for the services being classified as negotiated is that while they are a monopoly service they are directly attributable to a particular entity and so most efficiently charged to that entity. It is also a key characteristic of negotiated transmission services that those seeking the service are well informed and resourced and backed by a negotiated/arbitrate framework. The absence of competition in both prescribed and negotiated services means that there are no concerns associated with preferential access and any ring-fencing of staff and information serves no purpose and so is unnecessary.

Secondly, a robust cost allocation method already applies to TNSPs to ensure that there is no cross-subsidy between the different services provided by TNSPs.

Ring fencing for contestable services

Clause 5.2A.4(a)(1) provides that if the service is classified as “*contestable – then the Primary Transmission Network Service Provider may (but is not obliged to) provide that service as a non-regulated transmission service on request from a Connection Applicant*”.

As such, the Draft Rule makes an explicit assumption that the local TNSP can provide contestable connection services. This is consistent with ElectraNet's understanding that the intent of the Rule change is to impose more competitive discipline on TNSP connections, rather than fundamentally re-shape the connections market to include only independent providers. ElectraNet believes that without an active local TNSP in the market for contestable services it is unlikely that there would be sufficient competition among suitability qualified participants to promote the NEO. Therefore, ElectraNet supports the AEMC's approach.

ElectraNet considers that it would be helpful for the AEMC's final determination to be clear on the intention behind this Rule drafting and that active participation of the local TNSP is necessary for there to be confidence of there being an effective market for these contestable services. Conversely,

if the TNSP was required to create a separate entity with separate staff to undertake these connection works it would likely be difficult to justify and maintain staff to undertake the projects. This is because transmission connection projects are relatively small in number and bespoke in nature. That is, the scale and complexity may be too small to justify a stand-alone connections entity. As such, a TNSP may withdraw from this market. This is clearly not an intended outcome of the approach.

The existing approach to what are currently referred to as Dedicated Connection Assets (DCAs) confirms that an integrated TNSP can perform contestable services without causing distortions to the market. Indeed, access to the experience and expertise of TNSPs for these services is more likely to lead to efficient outcomes for customers. In particular, it is clear that the current cost allocation method is robust in the context of TNSPs providing contestable services. This is the mechanism that allows TNSP resources to be used as required for these works while also ensuring that costs are properly allocated between regulated and unregulated services.

Importantly, ElectraNet also considers that the AEMC has successfully designed an approach to IUSAs that does not provide TNSPs with any material advantage over alternative providers. As such, there is no need for the ring-fencing provisions imposed on distributors to be replicated in transmission. In particular:

- There is no timing advantage for the local TNSP. While TNSPs will be informed about a potential connection at the connection enquiry stage, there is nothing that prevents connecting parties informing other potential providers at that stage, or earlier. As such, it cannot be assumed that there is any advantage provided to TNSPs in this respect. In any event, a TNSP is required to produce a functional specification within 15 business days. Given it would be expected that a tender process for an IUSA would take several months, even if other parties were not informed at this time it is not clear these additional 15 days provides any meaningful advantage to the local TNSP.
- The upfront transparency requirements imposed on TNSPs substantially overcome any information asymmetry concerns. Under the AEMC's proposed model, the technical requirements the TNSP imposes for an IUSA (i.e., through the functional specification, expanded as discussed above) will be transparently established upfront – the TNSP will not have a subsequent capacity to veto a project on technical grounds if the connection meets the specification. Further, to the extent there are any concerns about the technical information provided by TNSPs, connecting parties are able to confirm the arrangements in a low-cost way through the Independent Engineer.
- There is no scope for TNSPs to provide preferential network access relative to its competitors. Again, the requirement for transparency as well as the upfront functional specification mean that the TNSP will not be able to undertake connections in a preferential way where it is chosen as the party to construct and own the asset. The ability to draw on the expertise of the Independent Engineer would also provide a further protection against this; to the extent this is needed.
- A concern may exist with the potential sharing of asset information gained by the local TNSP from a party offering a contestable IUSA service, where that local TNSP may also seek to offer an alternative IUSA service. This issue exists under both model A and model B as the local TNSP would require the same level of technical information on proposed IUSA plant and arrangements to provide a quotation for required cut in works, protection and control and secondary systems as it would require to provide an operation and maintenance quote for the IUSA. This is readily addressed by a proportionate response to limit the flow of information between the contestable and non-contestable activities of the TNSP to the extent that information has the potential to provide an unfair competitive advantage.
- The framework provides that operating and maintenance prices will be cost reflective irrespective of whether the TNSP builds and owns the assets. The negotiating framework, including the option

for remedy through a commercial arbitrator, means that there should not be an expectation that operating and maintenance prices associated with third party assets are not cost reflective (noting that the price may be higher because of solutions that, while having lower upfront costs, impose higher operating and maintenance costs over time, and further, pass-through arrangements may also be needed to better address circumstances where certain events occur). TNSPs will be required to demonstrate how the prices are cost reflective and if a customer is not satisfied by this it can seek arbitration.

Given the framework proposed by the AEMC, and in light of the points raised above, it is clear that there is no reason that competitors would be dissuaded from participating in the market. Indeed, even in the current environment the evidence demonstrates that connecting parties have been able to find alternative providers to the incumbent TNSP to provide non-regulated connection services.

Dedicated Connection Assets

The Draft Rule clarifies that DCAs are subject to contestability and there is no obligation for TNSPs to provide this service. ElectraNet supports this approach because it is consistent with the existing arrangements that work well and ensures that TNSPs are not exposed to an unlimited investment requirement.

The Draft Rule also requires third party owners of DCA's to register with the Australian Energy Market Operator (AEMO) in order to ensure that they will comply with certain technical requirements of the Rules. ElectraNet supports this approach as it will assist in ensuring the robustness and integrity of the electricity system.

While ElectraNet supports the AEMC finding that no material changes are required in order for DCAs to be transferred to the shared network where this is the lowest cost means of addressing a network need, it is concerned that the framework proposed is not sufficiently clear to withstand the challenges of time. ElectraNet supports the position set out in the Energy Networks Australia submission that the clarity of the draft Rule should be improved and that it is necessary that a wide variety of possible scenarios are able to be accommodated. This matter requires more time to consider and would benefit from additional public consultation and time for the necessary clarifications to be appropriately workshopped with TNSPs and connecting parties.

More broadly, ElectraNet also notes that limited time has been allowed for stakeholders to fully assess the changes proposed in the Draft Rule, including the associated savings and transitional provisions which have been published subsequently. Given the complexity of this area of the Rules and breadth of the proposed changes, ElectraNet recommends that further time be allowed for the making of a final decision to allow for detailed consultation with stakeholders to ensure the drafting of the final Rule fully delivers on its objectives, without any unintended consequences.

Should you wish to discuss any aspects of this response, please contact Bill Jackson on (08) 8404 7969 or Simon Appleby on (08) 8404 7324.

Yours sincerely



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