

5th May 2011

John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South
NSW 1235

Dear John

Scale Efficient Network Extensions - response to draft rule determination (Project no. ERC0100)

Brookfield is pleased to have the opportunity to respond to the Australian Energy Market Commission's (AEMC) draft rule determination for Scale Efficient Network Extensions (SENEs).

Brookfield is an experienced international developer and owner of energy transmission infrastructure. Given appropriate regulatory and market frameworks, we would be a keen participant in the sector in Australia, where we have now established a significant platform for infrastructure investment.

We are, however, disappointed with the proposed draft rule, which we believe does not strike an appropriate balance between the interests of investors and consumers. We strongly encourage the AEMC to return to the more practical solution put forward by the MCE.

Brookfield Credentials

Brookfield is a global asset manager focused on property, renewable power and infrastructure assets, with over US\$100 billion in assets under management and a market capitalisation of approximately US\$17 billion. Brookfield is listed on the New York and Toronto stock exchanges under the symbol "BAM" and on the Euronext under the symbol "BAMA".

Brookfield's Infrastructure Group currently has US\$32b in assets under management including US\$20b in the power generation and transmission sector. We have operations in North America, Europe, Australasia and South America. Our cornerstone investments in this sector include the Transelec electricity transmission business in Chile which owns and operates 8,750km of transmission system serving 98% of the population, and the North Ontario Transmission System. We are also currently involved with the development of major new independent transmission projects in Texas, USA.

Brookfield has established a significant platform for infrastructure investment in Australia, where substantial new investment in energy transmission networks, including for the connection of remote renewable generation sources, is required. We believe that the involvement of the private sector in this expansion is critical and we are keen to participate.

The draft rule determination

In February 2010, the Ministerial Council on Energy (MCE) submitted a rule change request to the AEMC that sought to address the risk of being unable to recover the potentially significant costs of building speculative transmission capacity in anticipation of future connections. The proposed rule would allow for the cost of the network extension (designated a Scale Efficient Network Extension or SENE) to be included in the regulated asset base of the Network Service Provider (NSP). Connecting generators would be required to pay for the share of the network assets they use, while any shortfall in required revenue that occurs where fewer generators connect or connect later than anticipated, would be recovered from all customers connected to the network. Customers would be protected through the regulatory oversight of the Australian Energy Regulator (AER) and the Australian Energy Market Operator (AEMO). AEMO would review the NSP's forecast generation profile and the AER would have the ultimate authority to disallow the project.

We recognise that the risk of underutilised or stranded assets where capacity is built in anticipation of future connections is challenging, however arguably there may be a greater negative impact if network extensions do not get built at all. The MCE's proposal seems to us to be a practical and equitable solution, which provides certainty for investors that they will recover the costs of the network extension, while at the same time providing protection for customers through the regulatory oversight of AEMO and the AER.

The AEMC, responding to arguments put forward in submissions, has now proposed a draft rule that seeks to allocate all risk and costs to market participants or investors, and none to consumers. The only obligation that the draft rule proposes is on the NSP to undertake, on request, specific location studies to reveal to the market the potential opportunities for efficiency gains from the coordinated connection of expected new generators in a particular area.

The draft rule does not regulate charges for use of the SENE. The terms and conditions of connection, including network charges, would be negotiated subject to the existing rules. No component of the cost of the SENE would be added to the regulated asset base or would be recoverable from customers.

We are very disappointed with this draft rule, which we view as a significant watering down of the changes intended by the MCE. The proposed rule provides no certainty for investment.

The issue is not being addressed

The challenge of investing in new transmission capacity in advance of new connections will not be addressed by the mere introduction of a requirement to conduct a market study.

This challenge that is not unique to Australia and has been grappled with overseas, where a number of different solutions have been formulated. Some solutions have been successful in facilitating rapid and efficient connection of renewable sources, others not.

In our experience the successful solutions are those that find an equitable balance between the interests of investors and consumers by:

- subjecting the designation of approved zones for network extensions to thorough independent regulatory scrutiny and approval;
- introducing a transparent process for the selection of the transmission solution that is the most cost effective and beneficial to the consumer; and
- providing certainty of recovering the cost of the network expansion through the regulatory process.

The proposed rule does not strike this balance.

Furthermore, while we agree that a market study should be the starting point for the designation of expansion zones, such a study should be conducted by an independent party, not the NSP, or should be subject to independent regulatory review and approval.

A good example of a scheme with these characteristics is the CREZ process established in Texas.

CREZ

The Competitive Renewal Energy Zones (CREZ) process was established by the Texas legislature in 2005. It was created to help encourage development of wind generation in Texas by facilitating the construction of electric transmission lines to areas of the state determined to have superior wind energy resources.

The legislation directed the Public Utility Commission of Texas (PUCT) to identify geographic zones (CREZ) where wind generation facilities would be constructed. The Electric Reliability Council of Texas (ERCOT), which operates the state's electric grid, was designated to collect wind data and nominate CREZ based on transmission cost calculations. In 2008, PUCT designating five CREZs for the generation of wind power and defined the required transmission upgrades and extensions required.

The PUCT sets the procedure for the qualification and designation of a NSP to build, operate, and maintain CREZ facilities. A NSP must demonstrate that it has the ability to construct, operate, and maintain a facility identified in the CREZ plan to become qualified. A qualified NSP can then file proposals to construct and operate a CREZ transmission facility.

The PUCT selects designated NSPs based on its ability to provide the needed CREZ transmission facility in the manner that is the most cost effective and beneficial to consumers.

The scheme has been very successful. Texas, better known historically for its fossil fuel reserves, now leads the United States in wind development. Adopting proactive transmission planning as part of legislative strategy laid the groundwork for large transmission lines to be built and enabled rapid growth of the state's wind industry.

From the investor's perspective the key ingredient for the success of the scheme is the ability to recover the cost of network expansions built in advance of anticipated connections from customers through the regulatory process. The legislation (Senate Bill No. 20) requires that if a CREZ is designated by PUCT, then PUCT must find that the facilities are "used and useful", prudent and includable in the rate base, regardless of the extent of the actual use of the facilities.

This requirement provides certainty to the investor, while consumers are protected through the requirement that PUCT designates the CREZ based on independent market advice from ERCOT and must select the transmission option which is “most beneficial and cost effective for the consumer”.

Further information on the CREZ scheme can be obtained from www.texascrezprojects.com
Brookfield's investment in Texas

In January 2009, Brookfield and a partner were awarded the right to build, own and operate US\$600 million of transmission lines in Texas in order to facilitate delivery of renewable wind power to population centres in the state. Commercial operations of the partnership, named Wind Energy Transmission Texas (WETT) are anticipated to commence in 2013, once construction has been completed.

WETT was the only successful participant in the CREZ process without existing power operations in Texas.

Conclusion

Brookfield would be pleased to have the opportunity to make similar investments in Australia. However, we are of the firm view that it would not be possible to meet our investment criteria under the proposed rule.

The rule provides for no additional investor certainty beyond the existing rules.

We would strongly encourage the AEMC to reconsider the draft rule and return to the more practical solution proposed by the MCE.

Contact Details

The legal identity of the Brookfield party making this submission is Brookfield Australia Pty Ltd (ABN: 95 126 164 145) which is located at Level 22, 135 King Street, Sydney NSW. The principal contact is:

Adriaan van Jaarsveldt
Senior Vice President, Regulatory
Office: +61 2 9692 2823
Mobile: +61 (0) 402 328 911
Email: adriaan.vanjaarsveldt@au.brookfield.com

Adriaan would be pleased to elaborate on our submission or answer any questions that you may have.

Yours sincerely



JEFF KENDREW
Chief Development Officer
Brookfield Infrastructure Group