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Dr John Tamblyn
Chairman
Australian Energy Market Commission
AUSTRALIA SQUARE NSW 1215

Dear John

**National Electricity Rules: Rule Change Application
Rule to establish a comprehensive inter-participant framework for addressing network
reconfiguration – response to Draft Rule Determination**

Stanwell Corporation Limited (Stanwell) welcomes the opportunity to respond to the Australian Energy Market Commission's (the **Commission**) Draft Rule Determination (**Draft Determination**) and Draft National Amendment (Transmission network replacement and reconfiguration) Rule 2006 (**Draft Rule**), made in relation to Stanwell's Rule Change application lodged on 17 May 2006 and revised on 10 July 2006.

1 Stanwell's response

Stanwell is pleased to note that in the Draft Determination that the Commission has acknowledged and accepted "Stanwell's fundamental proposal that the Regulatory Test should be applied to network reconfigurations as it promotes greater certainty and reduces the asymmetry in application of the Regulatory Test."¹ Stanwell is also pleased to note the Commission has recognised that:

"Efficient investment in the NEM relies in part on maximising transparency, particularly for planning purposes, and ensuring the clarity of locational signals. Clearer location signals work to ensure that generation investment is made where it will serve the long term interests of consumers with respect to price, quality, reliability and security of supply";² and

there is a need to "reduce the degree of unmanageable or unforeseen risk that transmission and generation investments are subject to."³

In response to the Draft Determination, Stanwell makes the following submissions:

- Stanwell considers that it is necessary and appropriate to cover a whole series of reasonably sizable investment projects. This would not be the case under the regulatory framework proposed by the Commission in the Draft Determination and

¹ Australian Energy Market Commission, *Draft National Electricity Amendment (Transmission network replacement and reconfigurations) Rule 2006*, Draft Rule Determination (26 October 2006), 10.

² *Ibid*, 11.

³ *Ibid*.

Stanwell therefore considers that an appropriate mechanism would be to extend the definition of *new small transmission assets*. An appropriate threshold for those *new small transmission assets* threshold would be \$5 million; and

- The Commission has decided not to provide a compensation mechanism within the Rules for third parties affected by reconfigurations, whilst at the same time emphasising the role of connection agreements as the best manner to deal with this issue. There is a gap in the Rules concerning connection agreements that is the same as the gap the Commission's Rule has implicitly recognised, that being the fact that at the time the National Electricity Code was originally drafted it was assumed that the network constantly expanded and elements were not removed or reconfigured. That gap also exists in respect of Chapter 5 and in the connection agreements which were drafted pursuant to that Chapter.

In this regard, the Commission should provide a transitional mechanism in the Rules that allows for the re-opening of connection agreements on the discrete issue of compensation in the event of network reconfiguration. Amendment should also be made to Rule 5.4A such that in respect of future connection agreements, TNSPs and Generators are required to negotiate in good faith in relation to the issue of compensation in the event of network reconfiguration.

2 Definition of new small transmission network asset should be amended to include network reconfigurations

Stanwell is concerned that a whole series of reasonably sizable investment projects would not be considered within the scope of the regulatory framework proposed by the Commission and that it is necessary to extend the definition of a *new small transmission asset* to include network reconfiguration. An appropriate threshold for a *new small transmission asset* would be \$5 million.

Stanwell notes the Commission did consider this in its draft determination:

"In considering the information disclosure requirements, the Commission can see some merit in the currently requirements for small augmentation investments as provided in Rule 5.6.6A being also applied to small replacement and reconfiguration investments",⁴

The Commission did however go on to state that:

"The Commission has decided to not include provisions in the Draft Rule to achieve this outcome because it believes it is beyond the scope of this Rule Change proposal, as the Proposal does not address informational requirements for small reconfiguration or replacement assets",⁵ and

⁴ Ibid, 24.

⁵ Ibid.

“The Commission does however welcome submissions or views on the appropriateness or otherwise of applying Rule 5.6.6A to proposed small reconfiguration or replacement investments”.⁶

On this point Stanwell makes two submissions:

- The extension of the definition of *new small transmission network asset* to cover network reconfiguration investment, such that there is corresponding information and consultation process requirements for TNSPs when undertaking such investment, falls squarely within the scope of Stanwell’s Rule Change application; and
- A failure of the Rule Change to make such a provision would likely defeat the intent of the Commission’s overall rule determination.

In relation to the first issue, Stanwell’s Rule Change application was not confined or limited to a concern about either small or large transmission network reconfigurations. Stanwell’s concern has always been about the impacts of network reconfigurations in general (insofar as they impacted on third parties such as generators). This can be seen from the draft Rules proposed by Stanwell which proposed that the Regulatory test and market participant consultation is required where a reconfiguration either cost a TNSP \$10 million or was likely to cause a market participant to incur a loss of revenue in excess of \$1 million.⁷ The threshold proposed made no explicit reference to either small or large reconfiguration investments.

Clearly within scope of this Rule Change are any issues of \$1 million of value upward and definitely any project costing the TNSP \$10 million.

Furthermore, whilst Stanwell’s focus has in some respects been on the application of the Regulatory Test, always a key element of Stanwell’s proposal has been a concern for effective consultation between TNSPs and affected market participants. Stanwell has always maintained that effective consultation and information flow is required whatever the size of the proposed reconfiguration.

For these reasons, Stanwell submits that a decision to extend the definition of, and corresponding information and consultation requirements, for a *new small transmission network asset* such that it covers network reconfiguration investment, is within the Commission’s power in this Rule Change.

In relation to the second issue, a failure to extend the definition of a *new small transmission network asset* to cover reconfiguration investment will significantly undermine the efficient network planning and market participant objectives of the Commission’s Rules where a significant amount of network investment will not be subject to the Rule.

If the Commission does not extend the definition of *new small transmission network asset* to cover reconfigurations, a broad range of network investments will not be subject to any form of regulatory test oversight. This is despite the fact that:

⁶ Ibid.

⁷ Letter from Stanwell Corporation to Australian Energy Market Commission, 17 May 2006, 11.

- it is likely that projects of significant magnitude could be completed within this cost range;
- projects within this cost range are likely to have similar impacts on third parties as those the Commission has identified as resulting from reconfigurations that constitute a *new large transmission network asset*; and
- projects within this range must also invariably raise similar questions as to whether the proposed network reconfiguration is in fact an efficient investment, i.e. are there non-network options that can be considered better alternatives.

Were this to be the outcome, Stanwell believes that this would be incongruous to the Commission's stated intention of, amongst others, broadening the application of the Regulatory test to:

"reduce the degree of unmanageable or unforeseen risk that transmission and generation investments are subject to;" and

"ensur[e] the consideration of the wider market benefits and costs that may arise from these kind of investments that would not otherwise be considered."⁸

For this reason, Stanwell submits that the threshold definition for *new small transmission network asset* should be redrafted, in a manner similar to the definition for a *new large transmission network asset* such that it captures network reconfigurations.⁹

In relation to the Commission's concern to not introduce additional regulatory burdens on TNSP via such an approach, Stanwell makes two points:

- Stanwell agrees that a \$1 million threshold has always been on the "low side." Stanwell would not oppose the threshold for a *new small transmission network asset* that is a reconfiguration being set anywhere between \$1 million and \$5 million.
- The consultation and information provision requirements for small transmission networks as provided by Clause 5.6.6A only require a TNSP to "consult with any *interested parties* on any matter relating to a proposed *new small transmission network asset* set out in the *Annual Planning Report*."¹⁰ These consultation requirements are significantly less than the Regulatory Test and consultation requirements required in the case of a *new large transmission network asset* as set out in Clause 5.6.6. For this reason, Stanwell does not believe that the inclusion of network reconfiguration in the

⁸ Above n 1.

⁹ The definition for a *new small transmission network asset* would therefore be as follows:

A transmission asset:

- (a) which is an *augmentation* 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 \$1 million, unless the AER publishes a requirement that an asset will be a *new small transmission 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 in excess of that amount or satisfaction of those other criteria to be a *new small transmission network asset*;
- (b) for which a *Transmission Network Service Provider* estimates an investment in excess of \$1 million of total capitalised expenditure is required; and
- (c) is not a *new large transmission network asset*.

¹⁰ National Electricity Rules.

definition of *new small transmission network asset*, and the corresponding consultation and information provision requirements arising from that inclusion, impose an unreasonable regulatory burden on TNSPs.

3 Compensation / Re-opening of Connection Agreements

As noted above, Stanwell is disappointed the Commission has decided not to provide a mechanism in the rules to provide compensation to market participants where they have suffered commercial loss as the result of network reconfiguration.

Stanwell notes that the "Commission has taken the view that whether compensation should be payable under the terms and conditions of a connection agreement is a matter for commercial negotiation between the relevant parties,"¹¹ and "that network users that are considering a long term investment that is reliant on firm access should negotiate this access with the TNSP and any costs factored into the investment decision."¹² This is despite the fact that Stanwell, and other parties in their submissions to Stanwell's Rule Change application noted that "[p]ractical experience amongst members of the NGF [National Generator's Forum] is that it is very difficult to negotiate deep connection rights in a connection agreement."¹³

Implicit in the Commission's draft rule to extend the Regulatory Test to reconfigurations is that there was a gap in the National Electricity Code as originally drafted. It is an important gap. The reason for the gap is that the drafters of the Code clearly assumed, as was their experience up to that time, that the network constantly expanded and elements were not removed or reconfigured. The drafters of the Code included a wide consultation group of transmission providers, generators and other industry participants from every state. At the same time and since, the same range of parties:

- drafted Chapter 5 and its schedules; and
- negotiated and executed connection agreements pursuant to that Chapter.

Obviously none of these documents would generally address the effects of reconfigurations.

An analogous gap exists and a mechanism is required to remedy that gap.

Whilst Stanwell still believes that there is a need for a compensation mechanism within the Rules that deals with reconfiguration, Stanwell acknowledges that in the future this issue can be dealt with via connection agreements. Stanwell's original rule proposal did in fact envisage as much providing that the compensation mechanism in the Rules would apply "unless a connection agreement otherwise provides."¹⁴ In the meantime however, there remains the issue of existing connection agreements that did not provide for this issue.

¹¹ Above n 1, 11.

¹² Ibid, 20.

¹³ National Generators Forum submission, 30 August 2006, 3, cited Australian Energy Market Commission, *Draft National Electricity Amendment (Transmission network replacement and reconfigurations) Rule 2006*, Draft Rule Determination (26 October 2006), 16.

¹⁴ Letter from Stanwell Corporation to Australian Energy Market Commission, 10 July 2006. See proposed Clause 5.3.4B.

For connection agreements currently on foot that have been agreed upon the basis of the existing Rules, which the Commission has acknowledged fail to address the issue of reconfiguration both generally and in relation to the making of connection agreements, there needs to be a limited re-opening amendment process. The issue also should be remedied going forward.

Stanwell therefore proposes the following:

- for existing connection agreements that do not provide for compensation in the case of reconfigurations, the Commission provides a transitional mechanism in the Rules that allows for the re-opening of connection agreements on the discrete issue of compensation in the event reconfigurations that affect the nature of the service enjoyed by users; and
- for future connection agreements, the Commission amend Rule 5.4A such that that it provides that one of the matters that a TNSP and a Generator must negotiate in good faith to agree upon is compensation payable (if any) in the event of a network reconfiguration.

In order to ensure that parties have a comprehensive framework within which to determine the appropriate level of compensation they are to agree upon, Stanwell also believes that the Commission should include in the Rules a set of principles that will guide the parties in determining the manner and rate of compensation payable. Stanwell also thinks that it is important, from the perspective of promoting certainty, transparency and efficiency in the negotiation process, that the Rules should be drafted in such a manner that where parties are unable to come to an agreement in relation to compensation payable the dispute resolution procedures in Chapter 8 can be used to arbitrate a commercially appropriate outcome.

Proposed drafting for both the re-opening of connection agreements and the proposed amendment to Clause 5.4A are located in Attachment A of this submission.

A diagram in Attachment B explains the manner by which the connection agreements can be re-opened and/or negotiated in order to provide for compensation in the case network reconfiguration.

Should you have any questions in relation to the above, please contact Erin Bledsoe on (07) 3335 3804.

Yours sincerely



Andrew Bills
General Manager Energy Markets

Attachment A- Proposed drafting in relation to connection agreements

(A) For existing connection agreements

11.X [Rule Title]

11.X.1 [Rule Title]

- (a) Where a *Network Service Provider* has made a *connection agreement* or deemed *connection agreement* pursuant to clause 5.2.2(a) on or before [DATE] which is the date the (*National Electricity Amendment (Transmission network replacement and reconfiguration) Rule 2006*) commences operation, for the purposes of that *connection agreement*, upon the request of either party, the parties must negotiate in good faith to reach agreement and vary the *connection agreement* (where appropriate) on the:
- (1) compensation to be provided by the *Network Service Provider* to the *Generator* in the event that the *generating units* or group of *generating units* of the *Generator* no longer enjoy the same connection to the *network* as a result of the *Network Service provider* undertaking works which constitute a reconfiguration of the network.
 - (b) For the purpose of clause 11.X.1(a), the level of compensation payable must be fair and reasonable. Without limitation, unless the parties otherwise agree, to be fair and reasonable, the compensation payable must be consistent with the principles in clause 11.x.1(c).
 - (c) *Network Service Providers* and *Generators* must take the following into account when negotiating the compensation to be provided by *Network Service Providers* under clause 11.X.1(a):
 - (1) the legitimate business interests of the *Generator* and the *Generator's* investments in the *power station*;
 - (2) the legitimate business interests of the *Network Service Provider* and the *Network Service Provider's* investment in the *network*;
 - (3) the value to the *Generator* of the *Network Service Provider* maintaining the existing *connection* to the *Network*;
 - (4) the need not to discourage or constrain optional network planning;
 - (5) the decline in the commercial position of the *Generator* or loss in revenue that a *Generator* reasonably expects to suffer as a result of reconfiguration of the *network* particularly where the *Generator* makes a *network service provider* aware of investments the *Generator* makes; and
 - (6) good electricity industry practice.

(B) For connection agreements made after final rule determination

New clause 5.4A(h)(3)

(h) Where the *Connection Applicant* is a generator:

- (3) the compensation to be provided by the *Network Service Provider* to the *Generator* in the event that the *generating units* or group of *generating units* of the *Generator* no longer enjoy the same *connection* to the network as a result of the *Network Service provider* undertaking works which constitute a reconfiguration of the *network*.

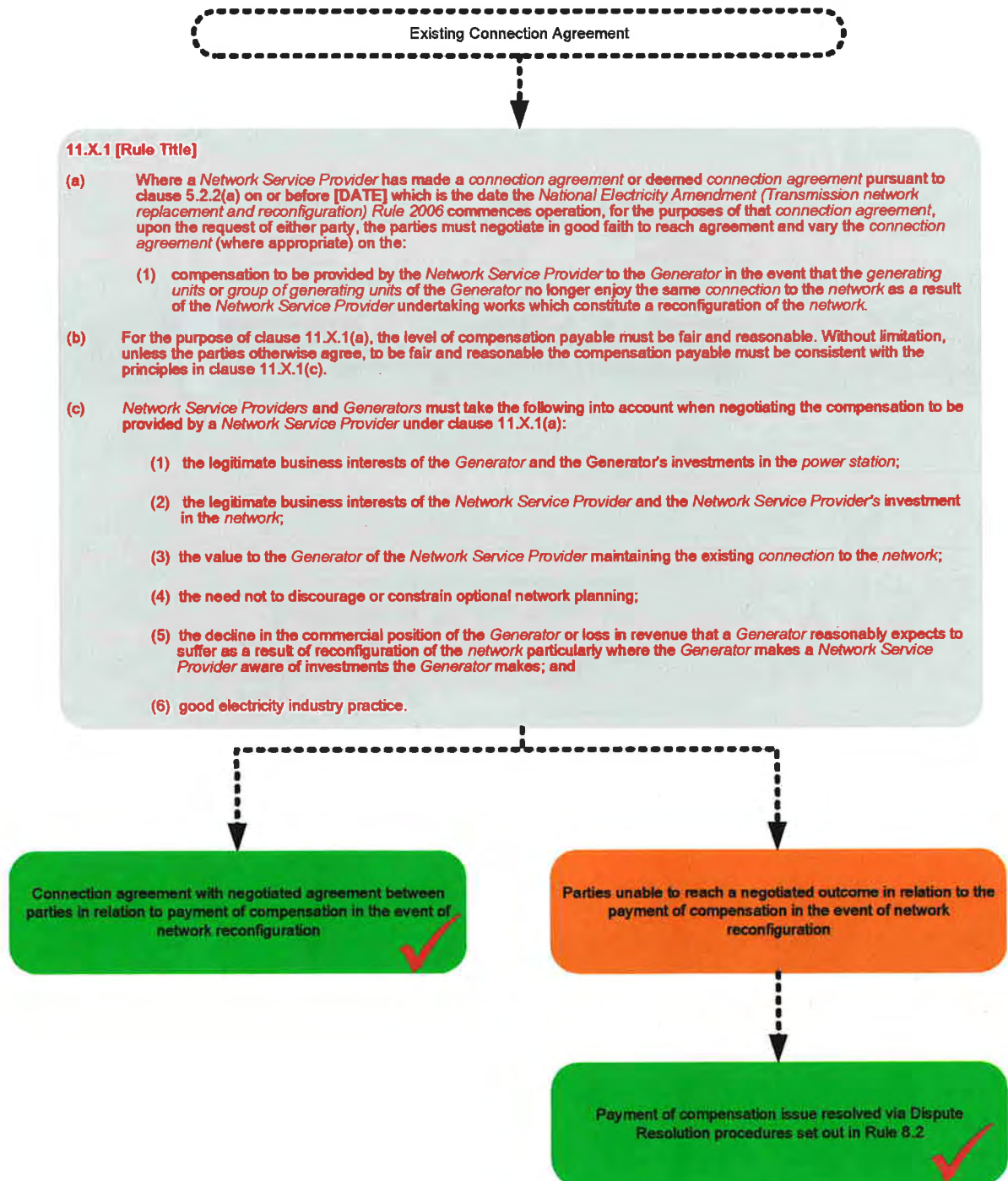
A further clause would need to be interpreted which set out the following:

Network Service Providers and *Generators* must take the following into account when negotiating the compensation to be provided by *Network Service Providers* under clause 5.4A(h)(3):

- (1) the legitimate business interests of the *Generator* and the *Generator's* investments in the *power station*;
- (2) the legitimate business interests of the *Network Service Provider* and the *Network Service Provider's* investment in the *network*;
- (3) the value to the *Generator* of the *Network Service Provider* maintaining the existing *connection* to the *Network*;
- (4) the need not to discourage or constrain optional network planning;
- (5) the decline in the commercial position of the *Generator* or loss in revenue that a *Generator* reasonably expects to suffer as a result of reconfiguration of the *network* particularly where the *Generator* makes a *network service provider* aware of investments the *Generator* makes; and
- (6) good electricity industry practice.

Attachment B - How connection agreements can be used to effectively provide compensation in the event of network reconfiguration

(A) For existing connection agreements



(B) For connection agreements made after final rule determination

