

15 May 2009

Dr John Tamblyn  
Chairman  
Australian Energy Market Commission  
PO BOX A2449  
SYDNEY SOUTH NSW 1235

By e-mail: [submissions@aemc.gov.au](mailto:submissions@aemc.gov.au)

Dear Dr Tamblyn

### **AEMO Response to the Draft Rule Determination for the Regulatory Investment Test for Transmission**

AEMO appreciates the opportunity to respond to the AEMC's Draft Rule Determination on the development of the Regulatory Investment Test for Transmission (RIT-T). This response is being submitted by the Australian Energy Market Operator (Transitional) Ltd (AEMOT) on behalf of Australian Energy Market Operator Limited (AEMO). Any reference in this letter to either AEMO or AEMOT should be taken as a reference to the entity that will exist from 1 July 2009, which will be the Australian Energy Market Operator.

Developing an appropriate economic framework for the evaluation of investment in services is an integral part of the regulatory contract between Network Service Providers and Network Users. As the National Transmission Planner and Victorian Shared Transmission Network Service Provider, AEMO has an interest in ensuring that the tools used to deliver this contract meet the National Electricity Objective (NEO).

AEMO believes that the RIT-T represents a step forward over the regulatory test. In particular, the amalgamation of the Regulatory Test's limbs should support more efficient service provision while the improved consultation process may provide demand side and generation alternatives with improved information enhancing their ability to compete to deliver the markets needs.

There are, however, a number of matters that are integral to the efficient and effective operation of the regulatory framework that are not addressed as part of this National Electricity Rule (NER) change package, or which are still in progress and cannot be addressed at this stage. These include:

- the National Transmission Planning arrangements
- congestion management arrangements;
- nationally consistent reliability standards;
- augmentations for new and existing network connections;

- the impact of climate change policies on the market; and
- the distribution planning framework.

Without these, all the benefits of the RIT-T may not be realised. The development of the RIT-T therefore needs to be considered in the context of that broader framework and be integrated with other relevant NER provisions. AEMO is looking forward to working with the AEMC to identify how the regulatory framework can be improved to integrate these matters to best meet the NEO.

This submission focuses on three issues that AEMO believes can be addressed by the AEMC at this time. These are:

- The RIT-T and Cost Allocation
- Amalgamation of the Limbs; and
- Transmission and Distribution Planning

### **The RIT-T and Cost Allocation**

#### *Prescribed Services and the Regulatory test*

The regulatory test has, historically, played an important role in determining cost allocation for services provided by TNSPs and provided a link between what is now covered in Chapters 5 and 6A of the NER. An investment that satisfied the regulatory test enabled a TNSP to justify spreading the cost of the investment across all network users through use of system charges. Since 2002 amendments to the NER have made this link more tenuous and it was finally removed with the introduction of Chapter 6A in 2006.

The proposed Rule changes clearly exclude both negotiated services and funded augmentations from the RIT-T process through exclusions set out in proposed 5.6.5C(d) and 5.6.5C(a)(11). The changes do not, however, make it clear whether augmentations over the cost threshold which are intended to provide prescribed services and hence have their costs recovered from customers should pass the RIT-T

Since there is no competitive restraint on the costs that are passed onto electricity consumers for regulated services, it is essential that some economic rigour be applied to investments that are to provide prescribed services. Therefore, AEMO recommends that the AEMC amends the proposed changes to make it clear that an option which is to have its costs recovered from customers as prescribed services must have satisfied the provisions of 5.6.5B subject to any exemptions in 5.6.5C. This would also ensure that the RIT-T is applied to decisions to convert assets from negotiated services to prescribed services.

#### *Funded Augmentations and Negotiated Services*

AEMC's Chapter 6A determination of 2006 used the terms 'funded augmentation' and 'negotiated transmission services' interchangeably. However, the references to 'funded augmentations' and 'negotiated transmission services' throughout the NER treat them differently. AEMO considers that at some point the AEMC should clarify the definition and treatment of these services.

The proposed changes also leave open the present arrangements whereby an investment to supply negotiated services does not require any scrutiny or public consultation. Augmentations to the shared network can have complex effects on secure transfer limits. Any potential detriments to transmission network users should be identified and any potential material inter-network impacts considered to augmentations whether they are considered funded augmentations or augmentations to supply negotiated services. As an interim step, AEMO considers that the changes should be amended to ensure that the provisions of 5.6.6 B should also apply to negotiated services.

### *References to services*

In line with the aforementioned links, AEMO believes that the terminology in the regulatory test to 'assets' and 'transmission investment' should be reviewed and in many places should be replaced with references to 'services' and 'options (network and non-network)' in line with the competitive neutrality principles underlying the RIT-T. This would enable services provided by network assets to be compared equally with non-network alternatives.

### **Amalgamation of the Limbs**

AEMO supports the amalgamation of the two limbs of the Regulatory Test and the proposed framework which encourages all benefits to be identified and quantified in an assessment. The effects of this change are expected to deliver efficiencies through better selection of alternatives and the valuation of strategic benefits. Conceptually, this approach may assist in the prioritisation of investments and the better valuation of attributes such as longevity, diversity and other benefits that are potentially overlooked.

The proposed drafting of Rule 5.6.5B(7) however, reintroduces a different treatment between reliability augmentations and market benefits. The addition of this clause unnecessarily introduces the distinction as Rules 5.6.5B(5) and 5.6.5B(6) only require TNSPs to quantify material matters and to undertake analysis that is commensurate with the decision being made. AEMO therefore recommends that Rule 5.6.5B(7) be deleted to reinforce the 'single limb' intention of this Draft Rule package.

### **Transmission and Distribution Planning**

AEMO is concerned with the proposed separation of the economic test to be applied to transmission and distribution services. The network planning and expansion framework for either transmission or distribution networks should serve to optimise the overall investment and operation of the combined systems to address a common need. In a number of cases transmission and sub-transmission (distribution) alternatives will be separate credible options and in other cases a credible option will include complementary work in both transmission and sub-transmission.

The current drafting provides a different test for investment to address needs in either or both the distribution and transmission networks. To provide for the efficient development of the total network, it is essential that the core of the test applying to each is the same.

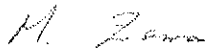
AEMO recognises that the planning and investment decision making processes for distribution networks are currently the subject of another AEMC review. It also recognises that Distribution

Network Service Providers would have difficulties and costs with applying the specific form of the RIT-T to their investments.

However the proposed changes, as currently drafted, risk inefficient outcomes and raise practical problems until the review is complete and the tests for transmission and distribution investment, if different, are closely matched. AEMO considers that this needs to be addressed as soon as practicable.

If you wish to discuss any of these matters raised in our submission, please do not hesitate to contact me on (03) 9648 8501.

Yours sincerely

A handwritten signature in black ink, appearing to read "M. Zema".

MATT ZEMA  
Managing Director and  
Chief Executive Officer  
AEMOT Ltd