

5 May 2011

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

Rule Change Reference Code: ERC0100

Dear Mr Pierce

RE: ERC0100 – Scale Efficient Network Extensions, Draft Determination

Alinta Energy (AE) commend the Australian Energy Market Commission (AEMC) on the work performed to date and is pleased to have the opportunity to provide comment in response to its Draft Rule Determination on the proposed rule change for inclusion of Scale Efficient Network Extensions (SENE) within the National Electricity Rules (NER).

In general, AE support the structure and direction of the AEMCs draft rule and agree its proposal presents a preferred approach when considered alongside the initial rule proposal as submitted by the Ministerial Council on Energy (MCE) and the options presented within the Options Paper.

AE however remain concern in presenting the draft rule determination the AEMC has failed to present appropriate quantitative analysis that adequately addresses the costs and benefits of the proposed rule change. In doing so AE fail to see how the draft determination sufficiently contributes to the National Electricity Objective (NEO) and considers any reasonable doubt regarding its ability to contribute should be the basis for exclusion from the rules. AE subsequently remain opposed to the inclusion of SENE within the rules.

Prior to making its Final Determination AE wish to bring to the attention of the AEMC the following issues and points of interest which we believe require further thinking and analysis.

Trigger for Consideration of SENE and Scope of SENE Design and Costing

AE is of the belief the AEMC has appropriately identified the necessary trigger for consideration of a SENE and those matters for consideration by a TNSP in completing a SENE 'design and costing study'.

Notwithstanding AE's support, AE holds reservations regarding the AEMCs decision not to assign property rights over the outcomes of a study. Failing to do so may diminish the incentives facing an entity to fund the SENE study for the following reasons:

- Confidential Information – limiting the ability of those entities funding a study, and those with registered interest, over access to and sharing of confidential information is likely to deter entities from supplying sufficient information in order to appropriately design and cost a SENE. This is likely to

result in an inferior outcome for those entities interested in the study results or in the worst-case entities opting not to fund a study at all;

- Free Rider Problem – restricting the ability to re-coup the funding costs of a study where parties fail to disclose their interest could expose a funding entity to 'free riders' who look to utilise the outcomes of the study for their own benefit and potentially to the detriment of the funding entity and registered parties;
- Recovery of sunk costs – without the assignment of property rights a funding entity will have limited, or no ability to recover the sunk costs of a study where it decides not to take further action. This may be the case where the outcomes of the study are no longer relevant to the funding entity, however may assist another interested entity in years. This may be the case where a funding entity opts to proceed with a stand alone connection.

AE therefore urges the AEMC to re-consider the assignment of property rights over the design and costing study, providing these rights to the funding entity. This would ensure the funding entity is well placed to manage access to and sharing of confidential information provided as part of the study, as well as enabling the funding entity to recover its costs associated with the study.

Risk Allocation

As stressed in our submission in response to the AEMCs SENE Options Paper and reflected again by the AEMC in its Draft Determination, AE is of the belief that *"efficient investment decisions are more likely to be made where the risk associate with those decisions is allocated efficiently"*. An efficient outcome is considered where the risk is borne by the investor and/or the entity best placed to manage that risk. AE argued within its original submission that placing the burden of managing potential stranded asset risk onto end users was likely to lead to an inefficient outcome.

AE is therefore supportive of the AEMCs decision to allocate this risk away from end users and onto those entities who agree to fund a SENE and the Transmission Network Service Provider (TNSP) responsible for operation of the SENE.

Ownership, Control and Triggering the Build of a SENE

AE support the AEMCs approach for triggering the build of a SENE. Before making a final investment decision a funding entity will be required to take into account a number of variables beyond the scope of the 'design and costing study'. These variables will be specific to each individual entity and include; an assessment of the funding entity's required rate of return and its capacity to manage potential exposure to stranded asset risk in the event forecast generation fails to connect to the SENE.

Whilst it has been noted by the AEMC that a funding entity may influence the design features of the SENE, the AEMC has not indicated the level of influence and who ultimately will make the final decision regarding the design of the SENE. AE recommend the AEMC provide guidance on this level of influence and who is to make the final decision as this potentially departs from the existing planning framework.

Furthermore, AE is concerned the recovery of a revenue stream by a funding entity from those generators who choose to connect to the SENE may be idealistic under the existing framework given the practical

implementation of the revenue requirements and the existing transmission use of system charging regimes. Moreover, AE considers any potential commercial negotiation between a SENE funding entity, SENE builder, SENE operator and connecting generators is likely to present information challenges. A non-TNSP SENE funding entity will only enter into an arrangement to fund a SENE where its cost recovery is considered to be revenue neutral for those expenses beyond its stand alone cost.

Under the existing framework AE considers there to be limited scope for merchant transmission ownership, this is particularly the case in those jurisdictions where a licensed generator is forbidden to hold a transmission licence. AE is not aware of existing registered TNSPs outside of the incumbent jurisdictional and interconnector TNSPs who build, own and operate a transmission network. As a result it can be inferred any commercial negotiation is therefore between a SENE funding entity (other than a TNSP) and a TNSP as builder and operator (and ultimately owner). Generators are therefore at the mercy of jurisdictional TNSPs whom have the necessary skill, knowledge and experience in the development and costing of network assets in order to negotiate a favourable position.

Additionally, where a TNSP is able to earn a non-regulated return on its SENE investment, potentially at a rate that is greater than prescribed under its regulated revenue determination; it subsequently is faced with an incentive to classify the SENE as a non-regulated service ensuring these assets are not included within its regulated asset base. This presents further issues where by generators connecting to a TNSP funded SENE are potentially required to pay higher charges under its connection arrangement. In turn this will result in end users paying higher energy charges as generators attempt to re-coup their costs.

AE maintains the AEMC is required to provide further analysis into the recovery of a revenue stream by non-TNSP and TNSP SENE funding entities prior to making its Final Determination.

Negotiating Connection to the SENE

As part of the AEMCs Transmission Frameworks Review (TFR), AE highlighted in its submission to the Issues Paper *"a lack of clarity and transparency exists within the NER provisions around connections and the allocation of reasonable costs by a TNSP"*.

AE considers this to still be the case under the existing framework. A service classification, be it prescribed, negotiated or non-regulated, given by a TNSP is dependent on the practices specific to that provider. AE argues that whilst the rules provide for the commercial negotiation of a classification between generator and TNSP this rarely occurs in practice where a TNSP is able to exhibit monopoly power over the final outcome.

Moreover, given a TNSPs ability to assess each SENE connection on a case by case basis ensures these restrictions within the existing framework will remain. AE note the service classification is considered out of scope for the purposes of this review and will be covered further as part of the TFR.

Should the AEMC wish to discuss the contents of this submission further please contact James Reynolds on 07 3011 7646 or Lance Brooks on 07 3011 7667.

Yours sincerely

A handwritten signature in black ink, appearing to be "G. Stanford".

for

Gary Stanford
Executive Director Wholesale Energy
Alinta Energy