

24 November 2016

ABN: 96 603 931 326

Suite 2, Level 14, 1 Castlereagh Street
Sydney NSW 2000

National Electricity Amendment (Replacement expenditure planning arrangements) Rule 2016

Submission to consultation paper

Introduction

Energy Consumers Australia thanks the Australian Energy Market Commission (AEMC) for the opportunity to provide comment on the consultation paper, *National Electricity Amendment (Replacement expenditure planning arrangements) Rule 2016* (the Consultation Paper). The rule change proposal was submitted by the Australian Energy Regulator (AER).

Energy Consumers Australia supports the proposed rule change. Energy Consumers Australia is always mindful of imposing new regulatory obligations on market participants, including network service providers (NSPs). However, in light of the rapid technological advancement and market transformation that increasingly characterises electricity supply in the National Electricity Market (NEM), Energy Consumers Australia submits that it is appropriate to increase the transparency of NSP planning related to asset replacement expenditure (replex). The change would bring replex planning requirements in line with those that apply to network augmentation expenditure, or new build (augex). Such a requirement will help ensure that investment in electricity networks is efficient and that the expenditure that must be recovered from consumers is no more than is necessary. Such a focus on costs to consumers is essential, given the large contribution of increases in network costs to the doubling of electricity prices in recent years. Following those increases, consumers are telling ECA that they are less positive about the value that energy services represent than all other services about which they were surveyed.¹

The changing electricity landscape

According to the AER's rule change proposal (the proposal), many of the components of the current electricity transmission and distribution network planning and expansion frameworks originate from reviews by the AEMC in 2008 and 2009.² At that time,

¹ ECA, *Energy Consumer Sentiment Survey Findings: National*, July 2016, 4. Available at: www.energyconsumersaustralia.com.au/research/energy-consumer-sentiment-survey-findings

² AER, *Request for Rule Change – Replacement expenditure planning arrangements*, 30 June 2016, 4. Available at: www.aemc.gov.au/Rule-Changes/Replacement-Expenditure-Planning-Arrangements

electricity peak demand was forecast to continue increase in line with the historical trend. Accordingly, as outlined in the proposal, the planning frameworks focus:

primarily on network augmentation, which relates essentially to demand driven investment. This is because, at the time the frameworks were conceived, it was not considered that there would likely be viable alternatives to like-for-like replacement [when certain assets reached the end of their lives].³

However, in recent years the electricity demand and supply landscape in the NEM has changed dramatically. The most recent forecasts from the Australian Energy Market Operator (AEMO) predicts that there will be no increase in peak demand over the next 20 years.⁴

These changes to demand forecasts have had a dramatic impact on the type of expenditures that electricity networks are including in their five-yearly revenue proposals. According to the AER, the capital expenditure (capex) forecasts contained in recent revenue proposals contain 30-50% of total capex for repex, compared to 15-30% for augex.⁵ Transmission networks provide even more striking examples, with 90% of the forecast capex in Powerlink's recent regulatory proposal being for repex and only 1% for augex.⁶ AEMO outlined an expectation in its 2015 *National Transmission Network Development Plan* that over the next 20 years, transmission NSPs will focus on repex, rather than augex, replicating the Powerlink experience.⁷

In addition, technological advancements in a variety of areas mean that there is a greater potential for the use of energy storage and distributed generation to provide viable network alternatives to the sole use of poles and wires (so called non-wires solutions, the use of which by some overseas NSPs overseas is extensive⁸). The AER has commenced work to improve the demand management incentive schemes and innovation allowance scheme that seek to promote such options.⁹ Finally, as summarised by the AEMC, the AER submits that:

in a low electricity demand growth environment, there is a stronger economic case for the use of non-network solutions as investment in long-life network assets can be deferred until there is a more certain need, reducing the risk of stranded assets.¹⁰

³ Ibid

⁴ AEMO, *National electricity forecasting report for the National Electricity Market*, June 2016, 3. Available at: www.aemo.com.au/Electricity/National-Electricity-Market-NEM/Planning-and-forecasting/National-Electricity-Forecasting-Report

⁵ AER, as above n 1, 6.

⁶ Ibid.

⁷ AEMO, *2015 National Transmission Network Development Plan*, 11, cited in *ibid*.

⁸ For example, Portland General Electric (California, USA) undertook a comprehensive 2016 evaluation of demand, supply and storage options, using a sophisticated methodology, which ran to 776 pages (Portland General Electric, *2016 Integrated Resource Plan*, November 2015, available at: www.portlandgeneral.com/our-company/energy-strategy/resource-planning/integrated-resource-planning).

⁹ See www.aer.gov.au/networks-pipelines/guidelines-schemes-models-reviews/demand-management-incentive-scheme-and-innovation-allowance-mechanism/initiation

¹⁰ AEMC, *Consultation paper: National Electricity Amendment (Replacement expenditure planning arrangements) Rule 2016*, 7. Available at URL in n 1.

Energy Consumers Australia generally agrees with the AER's characterisation of the current energy environment. Accordingly, Energy Consumers Australia agrees that the current regulatory framework is in need of updating to bring the requirements for NSPs to explore all viable options to meet augmented network requirements to also apply to programs to renew aging parts of the network.

The proposed rule change

On Energy Consumers Australia's reading, there are two key aspects to the proposed rule change. The first element is that a requirement be introduced for NSPs to include planned asset retirements, and options to address network limitations arising from these retirements, in the annual planning reports they currently publish under the National Electricity Rules.

The second component of the proposal is that the regulatory investment tests (RIT) be applied to replex, rather than just augex (as is currently the case). The same threshold for the application of the RIT would apply (\$5 million for distribution NSPs and \$6 million for transmission NSPs). NSPs could apply for exemptions to the requirement to undertake a RIT where they have determined 'on reasonable grounds'¹¹ that a like-for-like replacement is the only option. Interested parties would be able to appeal that decision by the NSP.

The two elements are, unsurprisingly, closely related. The former seeks to provide greater transparency over network planning to stakeholders, especially those who could potentially provide non-network solutions to looming supply constraints. The latter relates to the selection of a preferred option to replace an aging network asset with the option that delivers the required service at the lowest cost to consumers.

Energy Consumers Australia supports these objectives. Increasing the transparency and inclusiveness of network planning will help ensure that network services are delivered as efficiently as possible, a key pre-condition for the promotion of the long term interest of consumers. When imposing new requirements on network businesses, Energy Consumers Australia is always mindful of the risk of imposing unnecessary costs on NSPs and encourages the AEMC to fully examine these costs, to give stakeholders confidence that they do not outweigh the benefits of imposing the new requirement.

Ideally, the NEM's framework of incentive-based regulation would give consumers confidence that NSPs internal business planning processes would mean that only those investments required to deliver the necessary service level proceed. However, there is currently significant uncertainty about the future of the electricity service markets in the NEM, including the infrastructure that will be required to meet consumers' energy needs.

Accordingly, Energy Consumers Australia supports the proposed rule change. ECA believes that the AER's proposal provides an appropriate balance between increasing the rigour of NSP planning processes and not placing an undue burden on those businesses. Energy Consumers Australia, therefore, recommends that the AEMC makes the proposed rule.

¹¹ Ibid, 11.