

1 December 2023

Ms Stephanie Jolly
A/Executive General Manager – Consumer, Policy and Markets
Australian Energy Regulator
GPO Box 3131
Canberra, ACT, 2601

Email - [REDACTED]

Dear Stephanie,

AER Directions Paper – Social Licence

Energy Networks Australia (ENA) welcomes the opportunity to make this submission in response to the AER’s Directions Paper on social licence for electricity transmission projects.¹

ENA represents Australia’s electricity transmission and distribution and gas distribution networks. Our members provide more than 16 million electricity and gas connections to almost every home and business across Australia. Our electricity transmission members, the TNSPs, are focused on delivering ISP projects, REZ projects and other major transmission upgrades, which are urgently needed to facilitate the energy transformation that is central to Australia’s carbon reduction commitments.

In this context, TNSPs recognise the need for open and genuine community engagement to build social licence for these important projects. For example, TNSPs are working proactively with Energy Charter, agricultural groups and farmers federations to co-design a range of guidelines to further improve their approach to community engagement. ENA also notes that the AEMC’s recent Rule change² will further support TNSPs building and maintaining social licence, particularly during the planning stage for transmission projects.

Importantly, building and maintaining social licence is part of an ongoing relationship with the communities in which we operate. It occurs before, during and after the development and delivery of projects and needs to be adequately resourced and funded throughout. Within this context, we offer the following comments on the Directions Paper.

Key messages

¹ AER, Directions Paper, Social licence for electricity transmission projects, October 2023.

² AEMC, National Electricity Amendment (Enhancing Community Engagement in Transmission Building) Rule, 9 November 2023.

The AER's Directions Paper is a timely and important contribution to further clarifying how social licence can be supported and advanced by the existing regulatory framework. ENA concurs with many aspects of the Directions Paper and the following AER positions in particular:

- **The paper's focus on actionable ISP projects is appropriate.** ENA supports the Directions Paper's focus on the social licence framework applying to actionable ISP projects, given the scale of these projects, their potential impact on communities, and significance for the energy transition. These larger projects generally involve transmission line works and are more likely to have greater social licence engagement and activity considerations.³
- **Further guidance on engagement is not required.** ENA agrees with the AER that it is not necessary or appropriate to provide further guidance in relation to community engagement⁴ noting also recent separate Rule changes that address this. Instead, it is preferable to allow TNSPs to work with the relevant communities and stakeholders on a case-by-case basis to determine how best to build social licence. For some projects, the social licence costs may be less material and, in these circumstances, the regulatory scrutiny of those costs should be commensurately lower.
- **Flexibility is required on types of social licence activities.** ENA supports the AER's position that it does not intend to be prescriptive on the types of engagement or activities which TNSPs carry out, nor on the types of costs that could be classified as social licence expenditure.⁵ Instead, it is appropriate to consider the reasonableness of the proposed expenditure, having regard to the specific community issues in the context of each project.
- **Cost recovery should be addressed through ex ante allowances.** ENA agrees with the AER's position that social licence cost recovery should be addressed through ex ante allowances provided in revenue determinations or contingent project decisions. ENA notes that this cost recovery approach preserves the incentive properties of the regulatory framework and drives TNSPs to incur the efficient level of expenditure, whether this is below or above the AER's allowance as warranted by the circumstances.
- **Interface with the RIT-T.** ENA agrees with the AER that a TNSP will consider materiality when considering which costs and market benefits relating to social licence should be included in a RIT-T assessment. The purpose of the post-RIT-T engagement is to obtain and maintain social licence for the preferred option, rather than seeking to modify it (as suggested in Deloitte's report).⁶ While some

³ AER, Directions Paper, Social licence for electricity transmission projects, October 2023, footnote 5, page 6.

⁴ Ibid, page 10.

⁵ Ibid, page 10.

⁶ Deloitte, Final Report – Assessment of Social License Costs, 6 March 2023, page 6.

clarification of the treatment of social licence may be warranted in the RIT-T process, ENA agrees with the AER's position that the primary issue relates to cost recovery arrangements.

ENA therefore supports key aspects of the AER's Directions Paper. Specifically, ENA agrees with the AER that efficient social licence expenditure can be promoted through the application of the existing regulatory framework. In addition, the Directions Paper has highlighted some practical considerations that are worth exploring further in the interests of ensuring a fit for purpose framework:

1. **Practicality of the AER's expenditure review process.** ENA's principal query is that the AER's proposed expenditure review process outlined in the Directions Paper may be difficult to apply in practice, and that these inherent limitations should be taken into account in its assessment approach. ENA also queries the practicality and need for both a social licence engagement plan and social licence activity plan for every ISP project.
2. **Application of the AER's 'but for' test.** ENA would be concerned if the AER's 'but for' test is overly quantitative in nature because it may be challenging to apply in practice. A 'reasonableness' test may be a more suitable approach to determine the prudent and efficient level of expenditure.

Each of these matters is discussed in further detail below.

Detailed discussion

1. Practicality of the AER's expenditure review process

As explained in the Deloitte report, the term social licence first emerged more than 20 years ago. In its broadest form, it refers to the need for companies to build trust, legitimacy and credibility with the communities in which they operate.

ENA recognises the challenges in defining social licence and applying economic regulation to it. These difficulties point to the need for a flexible approach to regulation, as noted in the Directions Paper. In summary, there are three practical considerations that ENA would like to raise for the AER's further consideration:

a. Social licence is difficult to measure or observe

For transmission networks, securing and maintaining social licence has become increasingly important given the scale of the actionable ISP projects that are required to meet customers' needs and deliver on Australia's carbon reduction commitments. While 'social licence' can be tested through dialogue with the community and stakeholders, it is not directly observable or measurable. As such, it may be difficult to assess a TNSP's success in securing social licence, or identifying and calibrating the specific actions that are required to secure social licence in relation to a particular project.

b. Benchmarking and competitive procurement

The Directions Paper suggests that the efficiency of social licence expenditure could be demonstrated by "competitive procurement, benchmarking or

another relevant process.”⁷ In general, ENA is supportive of this regulatory approach but notes that it may be difficult to apply to social licence.

ENA considers that social licence expenditure may not be subject to competitive procurement and benchmarking as indicated by the Directions Paper, for the following reasons:

- Social licence expenditure is likely to be project-specific, making it difficult to benchmark different projects with one another; and
- Even if benchmarking were feasible, the delineation issues between social licence activities, ‘early works’ and other engagement activities may make it difficult to establish a consistent definition of ‘social licence’ for benchmarking purposes.
- Social licence engagement is not usually subject to competitive procurement, as TNSPs typically undertake a significant component of engagement in-house. This approach is consistent with building long-term relationships with communities and recognises that TNSPs should be accountable for obtaining and maintaining social licence.

In practice, therefore, benchmarking and competitive procurement may only provide limited guidance regarding the prudence and efficiency of proposed social licence expenditure.

c. Submission of social licence plans may not dovetail with the revenue setting process

The Directions Paper explains that it expects cost recovery for ‘social licence engagement’ to occur during Stage 1 ‘early works’, while ‘social licence activities’ will occur during subsequent stages:⁸

“The Rules allow transmission businesses to recover costs for early works phases of ISP projects. We envisage that at the Stage 1 early works phase, costs related to social licence would primarily relate to engagement expenditure, as there would be little information on which to base an assessment of activity expenditure. However, at later stages it may include both engagement and activity expenditure.”

The Directions Paper appears to envisage that a social licence engagement plan and a social licence activity plan will be submitted sequentially through staged Contingent Project Applications. While this may be the case for some actionable ISP projects, for others an actionable ISP project will be subject to a single revenue setting process. In those cases, the sequential submission of a

⁷ AER, Directions Paper, Social licence for electricity transmission projects, October 2023, pages 30 and 39.

⁸ Ibid, page 18.

social licence engagement plan followed by a social licence activity plan, as envisaged by the Directions Paper, may not be workable in practice.

ENA also notes that a TNSP may want to devolve decisions regarding the preferred social licence activities to a specially convened community group. In these circumstances, the social licence activity plan could not identify the proposed activities, as envisaged by the Directions Paper.

ENA considers that the regulatory framework should facilitate communities making their own decisions on the social licence activities, subject to an agreed budget amount that reflects prudent and efficient expenditure. However, if the regulatory framework required TNSPs to detail the social licence activities in a plan, depending on the scope and staging of contingent project applications (CPA), it may preclude an approach that empowered the community to make its own decisions.

On balance, therefore, ENA queries whether a social licence activities plan will be available at the time of a CPA or is required in all circumstances.

2. Application of the AER's 'but for' test

In relation to cost recovery, the AER explains it will provide an ex-ante allowance in network determinations and contingent project decisions. For social licence activities, the AER proposes to apply a 'but for' test, which the AER explains as follows:⁹

“We do not propose to rule that certain activities should be explicitly allowed or excluded at this time. We intend to use a 'but for' test to review this method and subsequent activities. Under this test we will consider whether the project's objectives cannot be efficiently and prudently met but for the method taken. We do not intend to assess each individual activity, but rather the overall method, package and costs proposed.”

ENA would be concerned if the 'but for' test contemplated by the Directions Paper seeks to apply an overly quantitative approach to assessing the prudence and efficiency of social licence expenditure. As noted earlier, 'social licence' is a concept that relates to 'community acceptance', rather than being an observable or measurable output. As such, linking the proposed engagement plans and activities to an improvement in outcomes would be challenging, with the possible exception of specific improvements such as undergrounding.

TNSPs will need to exercise their own judgement in deciding on the appropriate scope of the engagement and the resulting social licence activities. By the same token, the AER will need to assess the reasonableness of those judgments, having regard to the potential risks to the project. ENA is concerned that the application of a 'but for' test to social licence is unlikely to be practical or produce meaningful outcomes. ENA therefore prefers a more flexible approach based on a 'reasonableness' assessment

⁹ Ibid, page 20.

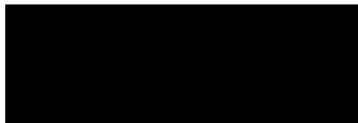
which places the onus on the TNSP to demonstrate that the proposed expenditure is prudent and efficient.

Way forward

ENA supports many aspects of the Directions Paper. In particular, ENA supports the AER's position that the onus should be on each TNSP to show how its proposed social licence expenditure complies with the Rules requirement that the expenditure is prudent and efficient. As explained in this submission, there are some issues arising from the Directions Paper where further clarification would be beneficial to ensure that the AER's proposed approach can be applied in practice.

ENA looks forward to working with the AER as it continues to develop its approach to regulating social licence costs. As a next step, it may be useful to meet to discuss the queries raised in this submission. In the meantime, if you would like to discuss this submission, please contact Verity Watson [REDACTED] in the first instance.

Yours sincerely,



Dominique van den Berg
Chief Executive Officer