Inertia Shortfall Event 2023

Cost Pass through Application

2 FEBRUARY 2023

ElectraNet

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Executive summary

This document sets out ElectraNet's cost pass through application under clause 6A.7.3 of the National Electricity Rules (Rules). This relates to an *inertia shortfall event* which occurred on 20 December 2023 when AEMO gave ElectraNet notice of an inertia shortfall pursuant to clause 5.20B.3 of the Rules. That event will materially decrease ElectraNet's likely cost of providing inertia network services relative to their likely level before the event.

Inertia is transferable across interconnectors. With the Heywood interconnector intact, there is sufficient inertia available to South Australia. However, when South Australia is separated from the rest of the NEM, inertia must be provided from within the State.

The Rules require that AEMO must periodically determine and publish the inertia requirements for inertia subnetworks, relevantly the South Australian region.[1] As the Inertia Service Provider in South Australia, ElectraNet must use its reasonable endeavours to provide the level of inertia AEMO determines is necessary by the date it has specified.[2]

If AEMO assesses that there is, or is likely to be, an inertia shortfall in South Australia, it must give ElectraNet a notice of that assessment.[3]

In December 2021[4], AEMO declared an inertia shortfall equivalent to 360 MW of Fast Frequency Response (FFR) from 1 July 2023 until the expected completion of Project EnergyConnect. The Australian Energy Regulator (AER) subsequently approved a network support allowance of $8.15m ($FY23) per annum in 2023-24 and 2024-25 to fund the provision of this service.

In December 2023 AEMO gave ElectraNet notice that it had revised the inertia shortfall for 2024-25. Whereas the shortfall had been the equivalent of 360MW of raise FFR, it has now been revised downwards by approximately 86% to 50 MW raise FFR. In large part the revision is due to the establishment of a 1 second Frequency Control Ancillary Services market.

This revision is likely to constitute a *negative pass through event* as described in clause 6A.7.3(f) of the Rules. As such, ElectraNet is required to report the event to the AER within 90 business days along with the likely cost reduction and other details.

Upon receipt of the above report, the AER would consider the matter and, presumably, determine a negative pass through amount that would be used to reduce ElectraNet's future revenue. The AER also has the ability to impose a negative pass through amount if the negative pass through event is not reported.

ElectraNet has not yet set transmission charges for 2024-25. This must be done on or before 15 March 2024. Therefore, there is an opportunity to amend ElectraNet's network support pass through allowance *before* transmission charges are set. One way or another, customers will be reimbursed for the difference in the network support allowance and the actual cost of providing inertia network services in 2024-25 through the network support pass through mechanism. However, this takes two years.

Having regard to the current climate of high electricity prices ElectraNet considers it appropriate to move quickly and reduce the 2024-25 network support pass through allowance that would otherwise be included in 2024-25 transmission charges. This avoids charging customers for a service now considered unnecessary in the first place, rather than to charge now and reimburse later.

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1 Clause 5.20B.2(a) and (c).

2 Clause 5.20B.4(a) and (c).

3 Clause 5.20B.3(c).

4 AEMO, 2021 System Security Reports, 17 December 2021.

Therefore, ElectraNet proposes that the AER determines a negative pass through amount of $6.15m ($FY23) in response to the above negative pass through event in time for ElectraNet to reflect that change in transmission charges for 2024-25.

In doing this, ElectraNet notes that this is an estimate of the likely cost of providing inertia network services in 2024-25 and that, under clause 6A.7.2 of the Rules, customers will be 'trued up' for the actual cost through the network support pass through process. As noted above, the effect of this proposal is simply to avoid collecting revenue to fund services that AEMO has now determined to be surplus to its requirements.

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1. Introduction

ElectraNet is the Jurisdictional Planning Body for South Australia and, as such, is the *Inertia Service Provider* for the South Australian Inertia sub-network.[5]

In this capacity, ElectraNet must use reasonable endeavours to provide the level of inertia services necessary to meet inertia shortfalls identified by the Australian Energy Market Operator (AEMO).

On 20 December 2023 AEMO issued a notice to ElectraNet in which it declared an inertia shortfall for 2024-25. This replaced an earlier notice and had the effect of reducing the inertia shortfall for 2024-25 from 360 MW raise FFR to 50 MW raise FFR. That notice is attachment 1 to this pass through application.

In the circumstances, AEMO's declaration of a reduced inertia shortfall is negative pass through event within the meaning of the National Electricity Rules (Rules) (chapter 10). Clause 6A.7.3(f) requires ElectraNet to submit a written statement to the AER specifying certain details of this event.

This document contains the above statement and is also ElectraNet's pass through application in respect of the negative change event. In particular, ElectraNet proposes that the AER determine a pass through amount of $6.15 ($FY'23). That determination will reduce the existing network support payment allowance from $8.15m ($FY'23) to $2.0m ($FY'23), which is our current forecast of the likely cost of that contract, noting that negotiations are still ongoing.

This is an estimate of the amount ElectraNet is likely to save as a result of AEMO's revised inertia shortfall. Under clause 6A.7.2 of the Rules, customers will be 'trued up' for the actual cost through the network support pass through process.

ElectraNet has not yet set transmission charges for 2024-25. This must be done on or before 15 March 2024. Therefore, there is an opportunity to amend ElectraNet's network support pass through allowance *before* transmission charges are set. One way or another, customers will be reimbursed for the difference in the network support allowance and the actual cost of providing inertia network services in 2024-25 through the network support pass through mechanism. However, this takes two years.

Having regard to the current climate of high electricity prices ElectraNet considers it appropriate to move quickly and lower the 2024-25 network support pass through allowance in the 2024-25 transmission charges based on the above forecast rather than to delay while contract negotiations are completed. This avoids charging customers for a service now considered unnecessary in the first place, rather than to charge now and reimburse later.

This document is structured as follows:

- Chapter 2 describes the applicable regulatory requirements
- Chapter 3 is ElectraNet's written statement in relation to the negative change event as required by clause 6A.7.3(f)
- Chapter 4 provides information in support of ElectraNet's pass through application.

[5] Clause 5.20B.4

2. Regulatory Requirements

This chapter summarises the following aspects of the Rules in turn:

- ElectraNet's obligations for the procurement of inertia network services in response to a shortfall declared by AEMO, which are contained in clause 5.20B.4 of the Rules.
- The regulatory requirements applicable to cost pass through, which are contained in clause 6A.7.3 of the Rules
- The network support pass through mechanism, which is contained in clause 6A.7.2
- Aspects of transmission pricing regulation, which is in part J of chapter 6A.

2.1. Procurement of Inertia Network Services

ElectraNet is the responsible Inertia Service Provider in South Australia. Therefore, in response to a notice issued by AEMO to address an inertia shortfall declared in South Australia under clause 5.20B.4 it must:

- use reasonable endeavours to make the inertia network services available by the date specified in AEMO's notice;
- make a range and level of inertia network services available to address the inertia shortfall such that the relevant inertia network services when enabled are continuously available, taking into account planned outages and the risk of unplanned outages;
- ensure relevant inertia network services are qualifying services when enabled;
- maintain the availability of those inertia network services until the obligation ceases as specified by AEMO;
- make available the least cost option or combination of options that will satisfy its obligation within the time referred to in AEMO's notice, for so long as the obligation to make the inertia network services available continues;
- prepare and publish relevant information to enable the development of non-network options;
- provide information in its Transmission Annual Planning Report about activities undertaken to satisfy its obligation to make inertia network services available, any inertia support activities undertaken, and any proposed network investment for these purposes; and
- meet relevant information and approval requirements under clauses 5.20B.5 and 5.20B.6.

A notice of this kind was issued on 20 December 2023 (attachment 1). This replaced a previous notice in which the declared shortfall mas materially larger.

2.2. Cost pass through

Clause 6A.7.3 of the Rules deals with cost pass through. In broad terms it establishes a mechanism by which an existing revenue determination can be adjusted under certain circumstances.

2.2.1. Pass through event

There are six types of *pass through event*, one of which is an *inertia shortfall event*. This is defined in Chapter 10 (Glossary) of the Rules as:

> *A Transmission Network Service Provider is required to make inertia network services available …or to cease making inertia network services available under clause 5.20B.4 as a consequence of an assessment by AEMO under clause 5.20B.3(d) that an inertia shortfall in the inertia sub-network has ceased and:*
>
> *(a) the Transmission Network Service Provider is required to …cease providing, inertia network services during the course of a regulatory control period; and*
>
> *(b) … ceasing to make inertia network services available …materially decreases the Transmission Network Service Provider's costs of providing prescribed transmission services.*

On 20 December 2023 AEMO gave ElectraNet notice that the inertia shortfall in South Australia in 2024-25 is 50 MW raise FFR. This is an *inertia shortfall event* because, by reason of that decision, ElectraNet is required to make *inertia network services* available.

2.2.2. Negative change event

Pass through events can be either positive or negative. A negative change event is defined in Chapter 10 (Glossary) of the Rules as:

> *a pass through event which entails the Transmission Network Service Provider incurring materially lower costs in providing prescribed transmission services than it would have incurred but for that event.*

In this context a cost change is material if it exceeds 1% of the Maximum Allowable Revenue for the relevant regulatory year, which was $411m ($FY23, smoothed) in the final determination PTRM. Therefore, the Materiality threshold for this application is $4.11m ($FY23).

The *inertia shortfall event* described above is a *negative change event* because the reduction from 360 MW raise FFR to 50 MW raise FFR is likely to lead ElectraNet to incur materially lower costs than would have otherwise been incurred.

2.2.3. Information requirements applicable to negative change event

Clause 6A.7.3(f) of the Rules provides that a Transmission Network Service Provider must submit a written statement to the AER within 90 business days of a negative change event occurring.

The statement must include:

1. the details of the negative change event concerned;
2. the date the negative change event occurred;
3. the costs in the provision of prescribed transmission services that the Transmission Network Service Provider has saved and is likely to save as a result of the negative change event until:

i. unless sub paragraph(ii) applies – the end of the regulatory control period in which the negative change event occurred; or

ii. if the transmission determination for the regulatory control period following that in which the negative change event occurred does not make any allowance for the pass through of the cost savings - the end of the regulatory control period following that in which the negative change event occurred;

4. the aggregate amount of those saved costs that the Transmission Network Service Provider proposes should be passed through to Transmission Network Users;

5. the amount of the costs referred to in subparagraph (4) the Transmission Network Service Provider proposes should be passed through to Transmission Network Users in the regulatory year in which, and each regulatory year after that in which, the negative change event occurred; and

6. such other information as may be required pursuant to any relevant regulatory information instrument.

The above statement is provided in chapter 4 of this document.

2.3. Network Support Allowance

The network support pass through mechanism allows a TNSP to 'true up' the difference between its network support payment allowance and the actual cost incurred in providing inertia network services each year.

There is no materiality threshold for a network support pass through and the event is taken to have occurred at the conclusion of each regulatory year.

The mechanism operates as follows:

- The cost of providing relevant services is determined by (in this case) the number and duration of events requiring the service to be dispatched by AEMO during each year; and
- That cost is compared to any pre-existing allowance the AER may have approved previously. Any surplus (or shortfall) incurred is subsequently be refunded to (or recovered from) customers, respectively.

In ElectraNet's current revenue determination the AER established a network support payment allowance to fund the provision of inertia network services. That allowance reflects the 360 MW shortfall declaration in place at the time.

In due course, ElectraNet anticipates making network support pass through applications to 'true up' any difference between the amount provided as a network support payment allowance and the actual cost of providing inertia network services in each relevant year.

Among the relevant factors the AER will be required to take into account, in assessing ElectraNet's future network support pass through applications, is the efficiency of the decisions and actions ElectraNet has made in procuring contracts to provide the inertia network services in question, including whether we failed to take any action that could reasonably be taken to reduce the magnitude of the positive network support event.

It is relevant to consider these matters now in relation to the network support payment allowance against which future 'true ups' will be made. We provide this information in chapter 4.

2.3.1. Transmission pricing

Part J of chapter 6A of the Rules deals with regulation of pricing for prescribed transmission services. It establishes a TNSP's *pricing methodology* as the basis for setting transmission prices.

Clause 6A.24.1 (b) provides that (emphasis added):

> *A pricing methodology is a methodology, formula, process or approach that, when applied by a Transmission Network Service Provider (or a Co-ordinating Network Service Provider on behalf of Transmission Network Service Providers within a region);*
>
> *(1) allocates the **aggregate annual revenue requirement** for prescribed transmission services provided by the Transmission Network Service Provider to each category of prescribed transmission services;*

A TNSP's aggregate annual revenue requirement is defined in clause 6A.22.1. It must be calculated by reference to the *maximum allowed revenue* adjusted in accordance with clause 6A.7. That is, it is adjusted by a pass through amount determined by the AER. Neither the pass through amount nor the aggregate annual revenue requirement can be adjusted by the TNSP without the AER's approval.

At the time of making this application, the approved pass through amount (network support payment allowance) in ElectraNet's approved revenue for 2024-25 is $8.15m ($FY23). ElectraNet has no discretion in this matter.

Pursuant to clause 6A.24.2(c)(1) ElectraNet is required to publish its transmission prices by 15 March each year. ElectraNet has no discretion in this matter.

3. Written statement under clause 6A.7.3(f)

This chapter provides the information required by clause 6A.7.3(f) of the Rules.

3.1. The details of the negative change event concerned

On 20 December 2023 AEMO gave ElectraNet notice of an inertia shortfall in South Australia for 2024-25. That shortfall is the equivalent of 50 MW raise FFR. This declaration replaced AEMO's prior declaration of a shortfall equivalent to 360MW raise FFR. The notice is attachment 1 to this application.

ElectraNet considers that a negative change event, being an inertia shortfall event, occurred on 20 December 2023.

3.2. The date the negative change event occurred

The negative change event occurred on 20 December 2023.

3.3. The costs ElectraNet is likely to save

The costs that are likely to be saved are uncertain for two reasons.

First, ElectraNet is still working through the process of negotiating contracts to provide the relevant services. Under other circumstances ElectraNet would have waited until that process was resolved before reporting the negative pass through event to the AER.

However, ElectraNet is acutely aware of the current cost of living situation and the contribution made by electricity prices. While transmission charges are a small part of most customer's electricity bills, we see no reason to collect money from customers for services they do not need, only to reimburse them in two years' time.

As discussed elsewhere, the narrow opportunity that exists to amend transmission prices to prevent collecting excess revenue. This led ElectraNet to make this application sooner than it might otherwise have done.

Second, the services in question are only required in the event that South Australia is 'islanded' from the National Electricity Market. The cost of providing service depends on whether an islanding event occurs and, if so, its duration. A detailed discussion of this matter is contained in Attachment 4 to ElectraNet's revised Revenue Proposal of December 2022.

Having regard to these two matters, and also the short time available to implement a change in time for 2024-25 transmission pricing, ElectraNet proposes that the AER determine a negative pass through amount based on a reasonable estimate of the likely saving and that the network support pass through process be used to 'true up'.

In proposing this we note that if no pass through amount is determined, the same 'true up' mechanism will ultimately be used to reimburse customers for the excess revenue associated with the reduced shortfall, but this will take two years.

3.4. The amount that should be passed through to users

As discussed above, the amount of saving is not currently certain. ElectraNet proposed that the AER determine a negative pass through amount of $6.15m ($FY23) based on the analysis in chapter 4.

Regardless of the amount, ElectraNet proposes that the full amount should be passed through to transmission network users. In fact, ElectraNet proposes that, rather than being collected and then passed through to customers in subsequent years, this amount should not be collected at all, lower transmission prices in the respective period.

3.5. The appropriate timing

ElectraNet has not yet set transmission charges for 2024-25. This must be done on or before 15 March 2024. Therefore, there is an opportunity to amend ElectraNet's network support pass through allowance *before* transmission charges are set. One way or another, customers will be reimbursed for the difference in the network support allowance and the actual cost of providing inertia network services in 2024-25 through the network support pass through mechanism. However, this takes two years.

Having regard to the current climate of high electricity prices ElectraNet considers it appropriate to move quickly and lower the 2024-25 network support pass through allowance in the 2024-25 transmission charges. This avoids charging customers for a service now considered unnecessary in the first place, rather than to charge now and reimburse later.

Therefore, ElectraNet proposes that the AER determines a negative pass through amount in time for ElectraNet to reflect that change in transmission charges for 2024-25.

In doing this, ElectraNet notes that this is an estimate of the likely cost of providing inertia network services in 2024-25 and that, under clause 6A.7.2 of the Rules, customers will be 'trued up' for the actual cost through the network support pass through process. As noted above, the effect of this proposal is simply to avoid collecting revenue to fund services that AEMO has now determined to be surplus to its requirements.

3.6. Such other information as may be required pursuant to any relevant regulatory information instrument.

ElectraNet is not aware of any such information.

4. Likely future cost of providing inertia network services

4.1. Efficiency of future costs

In making a pass through determination the AER will consider whether the costs involved are efficiently incurred. In this context the AER considered the contracts through which ElectraNet is likely to acquire the relevant services in its assessment of our proposed Network Support Allowance in our current revenue determination.

As noted above, we are currently part way through renegotiating contracts to reflect the reduced inertia shortfall. The process by which those contracts were established initially was summarised in Attachment 4 to our Revised Revenue Proposal, with supplementary information provided in response to Information Request #27 (ENET0281). Our current intention is to renegotiate those contracts, which is underway. Given that this will draw on procurement processes that were recent and which have been assessed and found effective by the AER, we are confident that the extensions will also be efficient.

4.2. Deriving likely future cost of inertia services

As the AER is aware from information provided in support of our current Revenue Determination, ElectraNet conducted a competitive tender process to procure our existing inertia services contracts. That process is summarised in Attachment 4 to our Revised Revenue Proposal.

Following that process, ElectraNet entered contracts with three providers.

It is apparent from the table that only two of the current providers are capable of providing sufficient FFR capacity to meet the reduced shortfall. Similarly, a review of the offers received previously but not accepted shows that no other single provider is capable of providing sufficient capacity to meet the shortfall.

As noted above, timing is such that ElectraNet is proposing a pass through amount based on its best estimate of the likely saving. Any discrepancy between this and our actual saving will be trued up in due course through the network support pass through process.

At this stage ElectraNet has commenced, but not concluded negotiations Our expectations as to this matter are as follows.

[redacted]

Considering the circumstances described above, and the benefit to customers in an urgent change, our proposed pass through amount is as shown in Table 4.2.

Table 4.2 – Eligible pass through amount

	$m FY23 per final decision PTRM
FY25 MAR	411
1% of MAR	4.11
Network support allowance	8.15
Revised cost expectation	2.0
Likely saving	(6.15)
Eligible pass through amount	(6.15)

ElectraNet