

20 September 2024

Ms Stephanie Jolly
Executive General Manager
Australian Energy Regulator
Brisbane Qld 4003

By email submission: RITguidelines@aer.gov.au

Dear Ms. Jolly,

2024 Review of the cost benefit analysis and regulatory investment test guidelines – draft amendments

The Australian Energy Market Operator (AEMO) welcomes the opportunity to comment on the AER's draft amendments to the cost benefit analysis (CBA) and regulatory investment test (RIT) application guidelines.

AEMO supports the review of the CBA and RIT guidelines and acknowledges the significant amount of work undertaken by market bodies and the Commonwealth to date to implement the recommendations of the Transmission Planning and Investment Review.

AEMO is broadly supportive of the proposed approach in the draft guidelines to require AEMO and RIT proponents to consider changes in Australia's greenhouse gas emissions in the ISP and RIT and the approach reflects the process undertaken by AEMO in the 2024 Integrated System Plan (ISP).

AEMO has some suggestions relating to the proposed approach for treating external funding contributions to RIT projects in the economic assessment process and would prefer that the CBA and RIT guidelines take a consistent approach for wealth transfers regardless of whether the benefit is through direct funding or concessional finance.

We have suggested some minor clarifications and edits to the draft amendments in the guidelines related to social licence and community engagement.

Please see Appendix 1 below for more detailed comments on each subject covered in the draft amendments.

If you would like to discuss anything further, please contact Paddy Costigan, Acting Group Manager – Reform Development & Insights (paddy.costigan@aemo.com.au).

Yours sincerely,



Violette Mouchaileh
Executive General Manager – Reform Delivery

APPENDIX 1: AEMO'S VIEWS AND INSIGHTS ON EACH SUBJECT IN THE DRAFT GUIDELINES

1. Changes in Australia's greenhouse emissions as a market benefit

AEMO welcomes changes to include reductions in Australia's greenhouse gas emissions as a class of market benefit for the purposes of the ISP and the RIT. In preparing the ISP, AEMO must calculate this class of market benefit (unless these benefits are not material) in assessing the investment option that maximises the economic benefit to meet the identified need. AEMO agrees with the position in the draft guidelines that the VER should be used as an input to the evaluation of market benefits post-market modelling, rather than as an additional cost that informs the dispatch of fossil-fuel generation in the market modelling. AEMO also agrees that the discount rate applied to the VER should be consistent with that applied to other project costs and benefits.

AEMO agrees with the position in the draft guidelines that the following emissions scope, where material, must be considered in the cost benefit analysis for the ISP and RIT:

- direct emissions from generation in the NEM, and
- direct emissions other than from generation e.g. sulphur hexafluoride.

The AER's explanatory statement to the draft amendments explains that in addition to the requirement to include direct emissions, 'we encourage AEMO and businesses to include any other scopes that are material and relevant'. AEMO considers that the explanatory statement provides a good description of the scopes of emissions relevant to the NEM, and including this additional detail in the CBA and RIT guidelines themselves would improve clarity for RIT proponents and others.

2. Sharing concessional finance benefits with consumers

The AEMC's final determination on *Sharing concessional finance benefits with consumers*¹ recommended that the CBA and RIT Guidelines be updated to:

- Explain the treatment of concessional finance in the economic assessment process, and
- Provide guidance on the level of funding certainty required before concessional financing can be used to support a project option in the economic assessment process.

The draft amendments to the CBA and RIT Guidelines state that "*funds that move between Participants count as a wealth transfer and do not affect the calculation of costs or market benefits*".

The draft amendments also contemplate two situations whereby a party other than a Participant (Other Party) provide project funding for a credible option:

1. An Other Party (e.g. a jurisdictional government) provides direct funding to a RIT-T proponent for a project option. This should be accounted for as a reduction in project costs to the RIT-T proponent and therefore an increase in the net economic benefit of that option.
2. An Other Party (e.g. a government funding agency) provides concessional finance to a RIT-T proponent where the interest on the funds is at a below market rate. The draft guidelines state that "*where any*

¹ <https://www.aemc.gov.au/rule-changes/sharing-concessional-finance-benefits-consumers>

benefit from the concessional finance will be shared with consumers, the present value of the benefit share with consumers should be accounted for as a reduction in cost to the RIT-T proponent”.

The first example aligns with the wealth transfer requirements. However, in the second example, it is unclear to AEMO why the proportion of the benefit share, and this proportion only, should be accounted for as a reduced cost to the project. The proportion of benefits that flows to consumers is clearly a wealth transfer between the RIT-T proponent and consumers, both Participants under the NER. It is also unclear why the total benefits of the concessional finance arrangement are not accounted for as a reduction in cost to the RIT-T proponent considering that it is a financial benefit from an Other Party to a Participant.

AEMO considers that the proposed treatment of concessional finance conflicts with the requirements to treat funds that move between Participants as a wealth transfer. CBA and RIT Guidelines should take a consistent approach to how financial benefits from an Other Party to a Participant are treated in the economic assessment process. The draft guidelines require the benefit of concessional finance to be observed by consumers in order for it to be accounted for as a reduction in project cost whereas there is no requirement for the benefit of direct funding to be observed by consumers in order for it to be accounted for as a reduction in project cost. Regardless of whether the reduction in cost to the RIT-T proponent is a result of direct funding, or concessional finance, it should be accounted for in the same way in the economic assessment process.

Also, the draft amendments to the CBA Guidelines focus solely on the treatment of concessional finance in the RIT-T assessment. AEMO requests that the language be broadened so that the proposed treatment of concessional finance is applicable at the ISP and/or RIT stages.

AEMO supports the approach taken in the draft guidelines regarding the level of funding certainty required before including concessional finance in the economic assessment process, particularly that proponents are required to undertake sensitivity analysis commensurate with the probability that the agreement is executable for the project in future.

3. Social licence

AEMO welcomes the draft amendments to the CBA and RIT Guidelines to provide clarity to RIT proponents on how and to what extent community engagement should be undertaken and how social licence factors should be incorporated in the identification of credible options.

AEMO suggests that for consistency, the CBA and RIT guidelines utilise the definition of social licence used by the Department of Climate Change, Energy, the Environment and Water in the *National Guidelines on Community Engagement and Benefits for Electricity Transmission Projects*² (see table of proposed edits below).

Also, in addition to references to ‘the community’, AEMO suggests that the CBA and RIT guidelines call out landholders and Traditional Owners as groups with their own distinct engagement considerations.

In the interests of clarity of wording, AEMO requests that the AER considers the following specific edits to the proposed amendments to the CBA guidelines (pages 60-61):

Current drafting	AEMO preferred wording
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² energy.gov.au/sites/default/files/2024-07/national-guidelines-community-engagement-benefits-electricity-transmission-projects.pdf

<p>“Social licence is linked to general awareness and acceptance of a project within its community and is directly linked to a project’s credibility.”</p>	<p>“Social licence is continued support and acceptance from a community that will be affected by an organisation, its activities or projects. For a transmission infrastructure development to be successful, social licence is crucial.”</p>
<p>“a RIT proponent would be expected to not rule out an option as non-credible simply due to low community support during the early stages of the project.”</p>	<p>“RIT-T proponents should not rule out a credible option during early project stages and/or the engagement process solely due to lack or loss of community support.”</p>
<p>“Given the expectation of planned and strategic engagement with identified communities of relevance, identified credible options should always be feasible and not be deemed no longer credible due to a loss or lack of social licence.”</p>	<p>“Proponents should continue to engage closely and meaningfully with key groups – such as local landholders, councils, businesses, Traditional Owners, community groups and members – to understand perspectives and address concerns, while also sharing key option information and its potential broader benefits.</p> <p>This is particularly important in early project stages, where establishing knowledge of local culture, customs and ways of living can help to ensure further engagement is culturally safe, respectful and, considers competing asks or commitments on time.”</p>
<p>“It may be the case that an option that requires more significant community engagement will have a later delivery date than other options. As with identification, the implementation of a project and its delivery timeline should be informed to some extent by community support and opposition.”</p>	<p>“Some options may also require more community engagement than others, and this may in turn lead to a later delivery date.”</p>
<p>“If the most likely timeline, with community support, would not deliver in time to meet the need of the system, the option may not be credible on that basis.”</p>	<p>“However, if an option’s likely delivery timeline, regardless of the reason, exceeds what is needed to support broader system security and reliability, this may mean it is no longer considered credible.”</p>

4. Improving the workability of the feedback loop

AEMO supports the proposed amendments to the CBA and RIT Guidelines that give effect to the AEMC’s final rule on *Improving the workability of the feedback loop*³.

5. Early works contingent project application before completion of a RIT-T

AEMO expects that the final amendments to the CBA and RIT guidelines will reflect the AEMC’s final rule on *Bringing early works forward to improve transmission planning*⁴ regarding the treatment of early works costs in the RIT-T and/or ISP. That is, TNSPs and AEMO are required to exclude any early works costs that cannot be sold or utilised on another project from a RIT-T and feedback loop assessment.

³ <https://www.aemc.gov.au/rule-changes/improving-workability-feedback-loop>

⁴ <https://www.aemc.gov.au/rule-changes/bringing-early-works-forward-improve-transmission-planning>

The final rule on *Bringing early works forward to improve transmission planning* also amends the NER to include principles that the AER must have regard to when assessing an early works CPA. AEMO suggest that the AER review the final dot point in **Explanatory box 3 Early works versus preparatory activities** (pg. 43) for accuracy in light of the new NER principles (text copied below).

“Specifically, for us to be satisfied that an activity is to be characterised as early works, a RIT-T proponent is required to demonstrate or evidence:

- *that the activity is not a preparatory activity for the purposes of clause 5.10.2 of the NER;*
- *that undertaking the activity will improve the accuracy of cost estimates, and/or ensure that a project can be delivered within the time frames specified by the most recent ISP;*
- *how undertaking that activity will not preclude, impede or hamper proceeding with alternative options, in the event an alternative option is deemed to be the preferred option.”*