

20 September 2024

Ms Stephanie Jolly
Executive General Manager
Australian Energy Regulator
PO Box 12241
George Street Post Shop
BRISBANE QLD 4003
Electronic Submission – RITguidelines@aer.gov.au

Dear Ms Jolly,

AER Draft decision – Review of the cost benefit analysis guidelines and RIT application guidelines

Energy Networks Australia (ENA) welcomes the opportunity to respond to the AER's Draft decision on its latest review of the cost benefit analysis (CBA) guidelines and Regulatory Investment Test (RIT) application guidelines.

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. This response is on behalf of ENA electricity transmission and distribution members.

Overall, ENA supports the draft amended guidance, and considers that the AER has struck the right balance in providing permissive guidelines that provide clarity but are not overly prescriptive, and therefore provide flexibility for the RIT proponents to adopt the most appropriate approach on a case-by-case basis.

In some areas, ENA considers that the proposed amendments may not fully capture what we understand to be the AER's intent (based on the Explanatory Statement and the AER's presentation at the information sessions). We have highlighted these areas in this submission and have provided a suggested mark-up of the guideline amendments as an attachment.

The key area in which ENA has concerns is with the proposed guidance and expectations in relation to community engagement for non-ISP transmission projects and now also for all RIT-D projects.

It is important that amendments to the CBA and RIT guidelines are fit for purpose and result in outcomes that benefit consumers.

The updated guidance relating to community engagement has its genesis in the *Enhancing community engagement in transmission building* Rule change, which related to community engagement for ISP projects only. The AER is proposing relatively prescriptive guidance on engagement for these ISP projects, including through the development of a stakeholder engagement plan.

The AER also sets out in its Explanatory Statement an expectation that the same type of engagement plan should be considered for all other transmission and distribution projects. While we do not oppose the idea that community engagement might be relevant for some non-ISP projects, the requirement that it be undertaken unless the relevant network service provider (NSP) justifies a decision not to do so is unnecessarily prescriptive.

ENA is not aware of a strong basis for extending the guidance on engagement to replex and minor transmission augmentations, or to distribution projects. NSPs' experience to date with replex and minor augmentation projects across both transmission and distribution is that few submissions are received during the RIT process and, where submissions are received, they are mostly unrelated to the purpose of the RIT. Requiring additional consultation is costly and diverts resources away from projects where engagement is more valuable to consumers and contributes to stakeholder engagement fatigue.

ENA understands from the Explanatory Statement and stakeholder forum that the AER's intention is to provide flexibility on how NSPs engage for these types of projects. ENA suggests that the guidelines be

more explicit in the flexibility that proponents are provided to choose an appropriate level of consumer engagement, and re-thinks the requirement for proponents to state the reasons why they haven't engaged. The focus should be on consulting on the *right* things (ie, projects which may have a material community impact), rather than on everything, to deliver benefits to consumers.

Relatedly, ENA also considers that the low level of consumer engagement around the majority of RIT-Ds and minor RIT-Ts makes a compelling case for the AER to consider raising the RIT thresholds as part of its current thresholds review. This would better align the resources that are involved in RIT assessments (from both NSPs and consumers) with the relative materiality of the investments subject to the RIT.

In finalising the changes to the guidelines, ENA:

- supports consideration of the change in direct emissions from both NEM generation and network investments, where material to the RIT outcome. This addresses ENA's earlier concern that the impact on SF6 emissions should be able to be considered.
 - ENA suggests the guidelines be clear that in considering materiality, focus should be directed toward whether the change in emissions will impact the RIT outcome, consistent with the objective of the RIT being to identify the preferred option, rather than to fully quantify the costs and benefits of the project in question. In this context a qualitative description will often be sufficient to explain when emissions are not material. ENA has provided suggested wording to this effect;
- supports the 'opt in' approach for including the impact of other, indirect emissions, where they are material to the RIT outcome and where there is a robust and proportionate methodology that can be used to quantify this impact;
- generally supports the additional guidance proposed on how social licence should be considered in identifying credible options in the RIT, noting that in practice social licence may not be a material concern for many RIT projects (particularly repex and minor augmentations);
- in relation to concessional finance, suggests the guidelines should be clearer that only information that relates to the appropriate inclusion of the impact of the financing in the RIT assessment should be included.
 - The provision of information 'to reduce the variability of agreements and bring a greater degree of standardisation to the negotiation [...] of these agreements' as well as to provide 'greater transparency around agreements' does not affect how the concessional financing is included in the RIT and so is outside the scope of the RIT guidelines.

Each of the above points is expanded on in our attached submission. In addition, ENA has separately provided a marked-up version of the AER's draft RIT-T guidelines with ENA's suggested amendments, to support the AER in providing clear and precise guidance.

ENA looks forward to engaging with the AER on the further development of its updated guidelines. ENA would be happy to review the final guidelines version prior to publication to ensure clarity, if that would be helpful.

Should you have any queries on this response please feel free to contact Verity Watson, vwatson@energynetworks.com.au.

Yours sincerely,



Dominique van den Berg
Chief Executive Officer

Attachment

Including an emissions reduction benefit in the ISP and RIT

ENA welcomes the guidance provided on the inclusion of changes in greenhouse gas emissions in the ISP and RIT assessments, and in particular the explicit recognition that has been given to the potential importance to the RIT outcomes of changes in direct emissions associated with network infrastructure (in particular sulfur hexafluoride (SF6)).

ENA understands that the AER's intent is to require these direct emissions to be estimated, where they are expected to be material to the outcome of the RIT assessment. ENA considers that the proposed wording of the guidelines could be amended to make it clearer that:

- the consideration of the 'materiality' of direct emissions should be made in relation to whether or not quantifying this benefit category is expected to lead to a change in the outcome of the RIT assessment (ie, it could impact the ranking of the options, or whether the options have a positive or negative market benefit); and
- the consideration of materiality can be made on a qualitative basis, rather than requiring quantification, provided the NSP provides a clear rationale for why benefits are not expected to be material. In this regard ENA considers that the word 'demonstrates' as currently used in the guidelines could be interpreted as requiring quantitative assessment, which would be excessive in this instance, and would be better replaced with 'justified'.

The attached marked-up version of the RIT-T guidelines provides ENA's suggested wording amendments to address these issues.

ENA also supports the AER's proposed 'opt in' approach to the treatment of indirect emissions. As the AER has recognised, this is an evolving field in which methodologies, data sets and experience are being developed. ENA considers that overall the AER has struck the right balance in providing permissive guidelines relating to indirect emissions that are not overly prescriptive, and which will allow proponents to adopt prevailing best practise methodologies and data at the time of the analysis to quantify emissions changes, where they have a material impact on the outcome of the RIT.

ENA understands that the AER's intent is for indirect emissions to only be included at the NSP's discretion, where the NSP considers they could be material to the outcome of the RIT, and where the NSP further considers that appropriate and robust data and methodologies are available to underpin this quantification. ENA has suggested amendments to the proposed guideline wording to make this intent clearer.

Further, ENA notes that the Explanatory Statement includes five 'other scopes of emissions', but the proposed guideline changes currently include only three of these,¹ and omits:

- embodied emissions in assets outside the project, and
- emissions associated with losses (noting that these may already be captured as part of the estimate of changes in direct emissions associated with generation).

ENA suggests the guidelines be amended to be consistent with the indirect emission categories identified in the Explanatory Statement.

Notwithstanding, ENA also notes that where there are embodied emissions in assets outside of the project (eg, a wind farm which is only constructed if the project goes ahead), there are likely to also be offsetting avoided embodied emissions (eg, from other wind farms which would have gone ahead in the absence of the project, as reflected in the RIT base case), and so overall the impact of these indirect emissions may not be material to the RIT outcome.

¹ Draft amendments Explanatory Statement, pp.11-12; draft CBA guidelines, p. 25; draft RIT-T guidelines, p. 38 and draft RIT-D guidelines, p. 37.

In relation to other areas the AER has highlighted in its Explanatory Statement and in the proposed guideline changes, ENA:

- agrees that the inclusion of changes in emissions should be undertaken by estimating the value of the change in emissions at the cost benefit analysis stage, as opposed to including the VER in modelling NEM dispatch outcomes;
- appreciates that the AER has provided proponents with flexibility in how they quantify emissions and is not requiring wholesale market modelling (which is not typically done for RIT-D assessments or for many RIT-T assessments (including repex)). ENA has suggested some changes to the proposed guideline wording to make this intent clearer;
- concurs with the AER's view that the VER may be used concurrently with AEMO's carbon budget modelling for the ISP;
- is comfortable that the guidance is not prescriptive in relation to the use of inputs and assumptions for estimating the changes in this benefit category; and
- is comfortable with the application of the same discount rate for valuing changes in emissions as applied to the other cost and benefit categories.
 - The AER suggests that sensitivity analysis could be conducted adopting a lower discount rate for the market benefit from changes in emissions.² ENA notes that such sensitivity analysis would appropriately be conducted using a lower discount rate (and specifically the 'lower bound' regulated discount rate as set out in the RIT-T/RIT-D instruments) across *all* cost and benefit categories, rather than the emissions benefit category alone. A sensitivity analysis that only varied the discount rate applied to changes in emissions would be difficult to then reconcile with the conclusions drawn from the main RIT analysis.

In response to the AER's request for feedback on its worked examples, ENA considers that the wording for the worked examples relating to changes in direct emissions is clear. ENA also supports the AER in not including worked examples relating to the quantification of indirect emission scopes, as this would be premature at this time, and would be more appropriate in future, once settled methodologies have emerged.

Social licence

Identifying credible options in a RIT assessment

ENA supports the inclusion of social licence considerations in identifying credible options as part of a RIT.

ENA understands the AER's intent that social licence considerations should not rule out an option as being credible per se, as social licence is something that is gained over time, and RIT proponent should consider appropriate engagement and strategies to ensure that there is social licence for the options being considered. However, ENA also understands that the time taken to gain social licence and the associated cost of consumer benefit sharing are factors that the RIT proponent should take into account in considering whether options are credible in RIT assessments.

Where addressing social licence concerns means that an option is not able to be delivered in the timeframe required to meet the identified need under a RIT, ENA understands that the updated guidance means that that option could be considered not to be credible. This is likely to be most relevant where the identified need is a 'reliability corrective action'.

² AER, *Review of the cost benefit analysis guidelines and RIT application guidelines, Draft amendments - explanatory statement*, August 2024. p. 8.

Further, ENA understands that where the option is included in the RIT assessment, the timing assumed can be based on the expected time required to address social licence concerns (with the consequence that the timing of benefits may be delayed compared to other options which do not raise social licence concerns).

The AER's proposed guideline amendments also include a statement that: 'no delays to the most likely timeline should be considered when assessing the credibility of an option'.³ ENA considers this may be a potential source of confusion, as it could be read as if expected delays in project timelines due to the need to gain social licence should not be taken into account when determining if an option is credible. ENA suggests that the statement in the guideline either be removed, or amended to read: 'no further delays to the most likely timeline should be considered when assessing the credibility of an option.'

The AER states in its Explanatory Statement that an option may not be credible if social licence concerns indicate that community concerns can only be addressed at a cost which is significantly higher than other options for similar benefits or lower benefits.⁴ In this case, the AER concludes that:

'this option may not be economically or technically feasible'.⁵

The AER also highlighted this consideration in its Social Licence for Industry Experts stakeholder forum.⁶

ENA notes that this consideration is not currently reflected in the draft guideline amendments relating to credible options and has proposed wording to cover this in the attached guideline mark-up.

As a more general point, the AER's proposed guideline amendments in relation to the consideration of social licence in relation to credible options lean heavily on the linkage with a RIT proponent's community engagement. ENA agrees that for some projects, the assessment of social licence concerns will be informed by the proponent's community engagement strategy from an early stage. However, as discussed further below, community engagement will not always be necessary or proportionate for RIT projects, particularly at an early stage and where the projects relate to brownfield investments or are minor augmentations. In these cases, social licence may not be a substantive issue. However, NSPs may also form a view on the potential for social licence impacts through other avenues, such as strategic land use planning and multi-criteria analysis.

ENA has proposed mark-ups to the guidelines in this area to recognise that community engagement may not always be undertaken, and to highlight the other potential avenues for RIT proponents to gain an understanding of the potential for social licence impacts on options being considered in a RIT. ENA considers that this allows for a more proportionate approach to early engagement in the identification of credible options.

Costs and market benefits associated with social licence

ENA supports the recognition in the guidelines that the costs and benefits associated with gaining social licence should be reflected in RIT assessments.

ENA agrees with the AER that the benefits can be accommodated under the existing RIT benefit categories, and do not require an additional benefit category to be added.

ENA notes that in the amended guidelines the AER refers to the 'efficient' costs of community benefit sharing activities being included (and justified) in RIT assessments. ENA considers that the focus on demonstrating that costs are 'efficient' at the RIT stage is misplaced and does not reflect the standard that is applied to the other costs included in the RIT assessment. The assessment of whether the community benefit sharing costs (as well as the network investment costs themselves) are efficient is the focus of the AER's regulatory determinations and contingent project assessments. The focus in the RIT assessments should instead be on whether the NSP considers those costs to be reasonable (based on the information available at that stage of the RIT), and on the RIT proponent setting out how the community benefit sharing costs have been

³ Draft RIT-T guidelines, p. 20 and draft RIT-D guidelines, p. 16.

⁴ AER, *Review of the cost benefit analysis guidelines and RIT application guidelines, Draft amendments – explanatory statement*, August 2024. p. 16.

⁵ AER, *Review of the cost benefit analysis guidelines and RIT application guidelines, Draft amendments – explanatory statement*, August 2024. p. 16.

⁶ AER, *Social license webinar industry 28 Aug*, 28 August 2024, p. 5.

estimated for the purpose of the RIT assessment. ENA has provided some alternative wording in the attached mark-up addressing this point.

ENA further notes that the worked example on *Community benefit sharing* provided in the amended guidelines⁷ suggests that the same percentage of funding should be allocated to community benefit sharing across all options, despite the discussion in the AER Explanatory Statement stating that early engagement may indicate options may require a different level of community benefit sharing.

ENA considers that if community engagement, or alternative analysis, has indicated that there are different community benefit requirements for each option, then these different costs should be included in the RIT assessment. The purpose of the community engagement is to understand the extent of community benefit costs that may be required, and it seems counter-productive to then not take this information into account in the RIT assessment. ENA has suggested some changes to this worked example to address this point.

Community engagement

ENA has concerns with the proposed guidance and expectations in relation to community engagement for non-ISP transmission projects and now also for all RIT-D projects.

The updated guidance relating to community engagement has its genesis in the *Enhancing community engagement in transmission building* Rule change, which related to community engagement for ISP projects only.

The AER is proposing relatively prescriptive guidance on engagement for these ISP projects, including through the development of a stakeholder engagement plan. ENA and its transmission members recognise the importance of effective community engagement for ISP projects and are actively involved in implementing best practice engagement approaches for these projects. The AER's proposed stakeholder engagement plan for these projects will sit alongside these initiatives, and ENA supports the flexibility proposed by the AER on the form and content of engagement under these plans, and the primary responsibility of the TNSPs in determining the manner of engagement.

The AER has set out in its Explanatory Statement an expectation that the same form of engagement plan should be considered for all other transmission and distribution projects⁸. While we do not oppose the idea that community engagement may be relevant for some non-ISP projects, it will not be relevant for all projects and the requirement that it be undertaken unless the relevant NSP justifies a decision not to do so is unnecessarily prescriptive.

ENA understands that the AER is not intending to be prescriptive in relation to the community engagement requirements for non-ISP RITs. Indeed, the AER recognises elsewhere in its Explanatory Statement that:⁹

'The level of expected engagement may depend on community interest and the impact of the project. Projects to replace existing parts of the network or minor augmentation projects therefore may require lesser engagement, when compared to large RIT projects.'

However, the current proposed amendments do not clearly emphasise this flexibility, and instead set up a presumption that the NSP would provide an engagement plan, unless it explains in the RIT documentation why a plan is not necessary.

Flexibility to engage in a fit-for-purpose manner for different RITs is important, because:

- encouraging consumer engagement across all investments, even those that are minor, can unnecessarily contribute to stakeholder engagement fatigue;

⁷ Example 40 of Appendix A.11 in the draft RIT-T guidelines and example 34 of Appendix A.9 in the draft RIT-D guidelines

⁸ AER, *Review of the cost benefit analysis guidelines and RIT application guidelines, Draft amendments – explanatory statement*, August 2024, p. 19.

⁹ AER, *Review of the cost benefit analysis guidelines and RIT application guidelines, Draft amendments – explanatory statement*, August 2024, p. 17

- consumer engagement is costly and diverts resources away from projects where engagement is more valuable to consumers; and
- for many projects, stakeholders already have other opportunities to engage, ie:
 - through the engagement activities undertaken as part of an NSPs regulatory reset process (including for repex investments);
 - through broader engagement conducted in concert with other government agencies and other utilities (where the projects are associated with new development areas); and
 - in response to the publication of RIT documents on an NSP's website. Currently the degree of stakeholder engagement on these documents is extremely low for the majority of repex and minor augmentations, often with no submissions being received.

While the guidelines provide proponents flexibility to not undertake community engagement, conditional on the proponent explaining why it's not necessary, it would be preferable if expectations around engagement for non-ISP projects were more clearly set out in the guidelines, and if it was brought out more clearly that proponents have flexibility to engage to the level they believe appropriate. ENA has proposed some wording to this effect in the attached mark-up.

ENA considers that the proposed wording and re-emphasise will facilitate the AER's goal of extending community engagement requirements to non-ISP projects in a flexible manner. It will also avoid the inclusion of boilerplate wording in the RIT documents to explain why engagement has not been undertaken, which risks making these documents even longer.

ENA also encourages the AER to consider other options that would extend engagement expectations while also limiting the number of low value and non-controversial RITs captured, such as:

- only applying the presumption of additional engagement to greenfield projects; or
- applying a cost threshold (such as the \$100m threshold applied elsewhere in the guidelines), below which there is no general presumption on additional community engagement.

Finally, ENA notes that the *Stakeholder engagement* example in the RIT-T and RIT-D guidelines appears to reflect intended guidance, as opposed to being a worked example. For clarity and accessibility, we suggest that all the 'requirements' included in this example be reflected in the main body of the document instead.¹⁰

Finally, the worked example proposed for inclusion in the CBA Guidelines on 'Refining a project through community engagement'¹¹ could be interpreted as suggesting that if options are amended following submissions on the PADR, there needs to be 'publication of these changes to the proposed preferred option' ahead of the PACR. ENA understands that this is not the AER's intention, and has proposed wording to clarify this example.

Sharing concessional finance benefits with consumers

ENA supports the AER's proposed amendments to clarify the treatment of the benefits to consumers from concessional finance as part of the RIT assessment.

ENA agrees with the worked example the AER has provided on the treatment of concessional finance,¹² noting that the provided example is only applicable where the concessional finance is debt which is fully passed through to consumers. ENA has identified what appears to be an incorrect value in this example in the CBA guidelines, which is corrected in the included mark-up.

¹⁰ Example 41 in the draft RIT-T guidelines and example 35 in the draft RIT-D guidelines.

¹¹ Example 11 of the draft CBA guidelines.

¹² Example 20 in the draft CBA guidelines; example 22 in the draft RIT-T guidelines and example 19 in the draft RIT-D guidelines.

ENA notes that the consumer benefit from concessional finance will be different where:

- less than 100% of the concessional finance is passed through to consumers. In this case it may also affect the taxable income of the RIT proponent (and therefore the net tax reflected in the building block model); and
- the concessional finance is in the form of equity. In this case the concessional equity finance will lower the taxable income of the RIT proponent (and therefore the net tax reflected in the building block model), which is an additional benefit which should also be included in the impact on consumers.

In relation to the information which a RIT proponent is required to provide in relation to a concessional financing agreement for the purposes of the RIT assessment, ENA supports what it understands to be the AER's intent that proponents are required to 'provide sufficient detail'¹³ to support the basis on which the agreement has been reflected in the RIT.

The AER guidelines should be clear that only information that relates to the appropriate inclusion of the impact of the financing in the RIT assessment should be included in the RIT. The provision of information 'to reduce the variability of agreements and bring a greater degree of standardisation to the negotiation [...] of these agreements'¹⁴ as well as to provide 'greater transparency around agreements'¹⁵ does not affect how the concessional financing is included in the RIT and so is outside the scope of the RIT guidelines.

In particular, for concessional finance agreements that have not been executed, it is not likely to be possible to provide details commensurate with the requirements in NER clauses 6A.3.3 (RIT-T) and 6.2.9 (RIT-D). Further, this detail is also not required for the purpose of explaining how the financing agreement has been reflected in the RIT assessment. Setting out an 'expectation' that the RIT proponent provides this information may cause confusion when compared to the less prescriptive requirement in the amended guidelines that proponents 'provide sufficient detail'.

ENA suggests the AER clarify that the details required at the RIT stage should be sufficient to substantiate how the value of the concessional finance is expected to be shared with consumers and has been reflected in the RIT-T assessment, and to note that these details are separate to the information NSPs must provide under NER clauses 6A.3.3 (RIT-T) and 6.2.9 (RIT-D) once an agreement has been executed.¹⁶ ENA has provided suggested amendments to address this point.

ENA supports the AER's proposed approach to treating agreements that have not yet been executed as a sensitivity in the RIT assessment, to avoid situations in which a RIT needs to be re-applied as a consequence of the concessional financing agreement either subsequently being concluded or not going ahead. ENA understands the guidance to allow the RIT proponent to determine whether the agreement is reflected in the main RIT analysis, or treated as a sensitivity, based on the RIT proponent's view of whether it is likely to be executed, which it would then need to substantiate in the RIT documentation. ENA notes that this sensitivity has currently only been included in the CBA guidelines, and has suggested in the attached mark-up some wording that could be included in the RIT-T and RIT-D guidelines.

Other issues

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

ENA notes that the AEMC has now released its final rule determination on the *Bringing Early Works forward to improve transmission planning* rule change. In this final rule determination, the AEMC has updated its

¹³Draft CBA guidelines, p. 76; draft RIT-T guidelines, p. 59 and draft RIT-D guidelines, p. 54.

¹⁴ AER, *Cost benefit analysis guidelines and RIT application guidelines, Final Amendments, Explanatory Statement*, October 2023, p.14.

¹⁵ AER, *Review of the cost benefit analysis guidelines and RIT application guidelines, Draft amendments – explanatory statement*, August 2024, p. 22.

¹⁶ See the separate document: 'Suggested markup to the guidelines'.

draft position regarding the treatment of sunk costs funded through an early works contingent project application determination.

ENA believes that the AEMC's final rule determination is clear, in that now RIT-T proponents must:

- exclude any incurred early works costs that are sunk (ie, that cannot be sold or utilised on another project), from the costs of that option in the RIT-T assessment; and
- include any incurred early works costs that can be re-sold or utilised on another project, in the costs of that option in the RIT-T assessment.

The AER has 12 months to update and publish its CBA guidelines in line with the AEMC's final rule, and ENA notes that consultation that has been taken to date on this matter will count towards the AER's consultation requirements under the NER.

Given the AER's earlier intention to update its CBA guideline in line with the AEMC's final rule determination as part of this current consultation round, ENA would be happy to review the AER's proposed wording for the final CBA guideline on this point, to act as an additional check on the clarity of the proposed guideline wording.

Finally, ENA also flags that the requirement relating to the treatment of sunk costs in the AER's draft amended guideline has not been included in the list of binding elements on RIT-T proponents in the CBA guidelines.¹⁷ ENA suggests that the updated guidance on incurred early works costs is reflected in the list of binding elements in the CBA guidelines.

Improving the workability of the feedback loop

ENA is comfortable with the draft amended guidelines relating to the workability of the feedback loop.

Inclusion of an appendix summarising binding guidelines

Finally, given the increasing inclusion of binding requirements in the RIT-T and RIT-D Application Guidelines, ENA requests that the AER includes a list of the binding elements in these two guidelines, similar to that currently included in Appendix A to the CBA Guidelines.

ENA notes that the AER did not adopt this suggestion in its previous 2023 guidelines review, on the basis that the number of binding requirements introduced in that review was small.¹⁸ However, ENA considers that the increase in binding requirements proposed in this latest review warrants the inclusion of such an appendix.

Providing a concise list of binding requirements at the end of the guidelines will increase clarity and accessibility, thereby enabling greater compliance and the monitoring of compliance at minimal cost.

¹⁷ Draft CBA guidelines, p. 64.

¹⁸ AER, *Cost benefit analysis guidelines and RIT application guidelines, Final Amendments, Explanatory Statement*, October 2023, p.29.