TasNetworks | Powering a Bright Future

Tasmanian Networks Pty Ltd
ABN 24 167 357 299
PO Box 606, Moonah, TAS, 7009

21 March 2025

Mr Arek Gulbenkoglu
General Manager, Network Expenditure
Australian Energy Regulator

By email: aerinquiry@aer.gov.au

Dear Mr Gulbenkoglu,

Re: AER's Capital Expenditure Incentive Guideline Review

TasNetworks welcomes the opportunity to contribute to the Australian Energy Regulator's (AER's) consultation on its review of the Capital Expenditure Incentive Guideline (Guideline). We are pleased that the AER has broadened the scope of the review to consider matters beyond the Australian Energy Market Commission's (AEMC's) amending rule on managing Integrated System Plan (ISP) project uncertainty through targeted ex-post reviews.[1]

As the distribution and transmission network service provider (NSP) in Tasmania, TasNetworks understands the importance of the Guideline and its intent to incentivise NSPs to undertake efficient capital expenditure (capex), as efficient capex benefits both NSPs and consumers.

TasNetworks is currently progressing the North West Transmission Developments (NWTD), which is a component of Project Marinus. The Australian Energy Market Operator's (AEMO's) Final 2024 ISP reconfirmed the actionable status of Project Marinus with no decision rules and the timing of Stage 1 by June 2030 and Stage 2 by June 2032.[2]

Given the size and complexity of the NWTD relative to TasNetworks' existing regulatory asset base (RAB) and our non-ISP capex pipeline (approved as part of our 2024-29 determination[3]), we welcome the proposed amendments to the Guideline to accommodate the AEMC's amending rule ahead of commencing the construction phase of the NWTD in early 2026.

However, we hold several concerns in relation to the Capital Expenditure Sharing Scheme (CESS) and how it currently applies to ISP projects and large non-ISP projects.

In addition to the amendments proposed in the review, we ask the AER to please also consider the following:

- ISP project capex & CESS application timing: separate the application of the CESS for ISP and non-ISP project capex, similar to how the amending rule will separate ex-post reviews for ISP and non-ISP project capex.

[1] Managing ISP project uncertainty through targeted ex post reviews | AEMC
[2] AEMO, 2024 ISP, June 2024, p.62 (in service timing)
[3] TasNetworks - Determination 2024–29 | Australian Energy Regulator (AER)

Tasmanian Networks Pty Ltd
ABN 24 167 357 299
PO Box 606, Moonah, TAS, 7009

- CESS penalty for efficient ISP project overspends: for ISP project capex, if a complete ex-post review (i.e. stages 1 & 2) is triggered and the overspend is deemed to be efficient, the AER should have the ability to amend the CESS outcome and the AER's default position in this instance should be that no CESS penalty is applied.
- CESS flexibility for large non-ISP projects : for large non-ISP projects, the AER should have flexibility in how it applies the CESS and consider the specifics of each project.
- Abandonment of projects & CESS application: NSPs should not receive a CESS bonus for abandoning a project and not spending to its approved allowance.

ISP project capex & CESS application timing

The current application of CESS to ISP projects has the potential to cause unintended impacts to consumer prices. If a NSP delivers an ISP project over multiple regulatory control periods, re-profiles it's capex during delivery but delivers the total project in line with its approved allowance, this could result in higher prices for consumers in the short-term.

Tables 1 and 2 outline the scenario described above. The scenario assumes:

- the NSP delivers the ISP project over FY27 to FY31;
- the NSP's regulatory control periods end FY29, FY34 and FY39; and
- the NSP spends its non-ISP project capex to allowance each year during ISP project delivery.

Table 1: ISP project capex profile and variance

Year	Capex Allowance ($M)	Capex Spend ($M)	Variance ($M)	Cumulative Variance ($M)
FY27	70	50	-20	-20
FY28	300	240	-60	-80
FY29	400	400	0	-80
FY30	540	500	+40	-40
FY31	240	200	+40	0

Table 2: CESS outcomes

Reg Period	Total Bonus (+) or Penalty (-) $M	Annual Bonus (+) or Penalty (-) $M
FY29	N/A	N/A
FY34	+80	+16
FY39	-80	-16

Although the scenario outcome would be largely neutral in the longer term (once the CESS bonus and penalty have both been applied, noting that the timing of the accrual of the financing benefit/cost will mean that the outcome is not completely neutral), it clearly demonstrates that consumers are inadvertently paying more in the short-term.

To avoid this, the AER could separate the application of the CESS for ISP and non-ISP project capex and could undertake an assessment of actual ISP project capex against allowance over multiple regulatory control periods for the purposes of the CESS.

Tasmanian Networks Pty Ltd
ABN 24 167 357 299
PO Box 606, Moonah, TAS, 7009

CESS penalty for efficient ISP project overspends

When applying the Guideline to ISP projects, the current interaction between the CESS and ex-post reviews is not fit for purpose. Large ISP projects are introducing NSPs to an unprecedented set of challenges as the energy transition continues to accelerate.

NSPs have noted that ISP projects can be substantially larger than their business as usual (BAU)/non-ISP project capex and more susceptible to forecasting risk (as noted by Transgrid in its HumeLink Stage 2 contingent project application[4] and Marinus Link in its Stage 1 – Part B revenue proposal[5]). This creates an asymmetric risk towards NSPs due to the higher likelihood of incurring a CESS penalty (relative to a CESS bonus or spending to approved allowance) and also creates the risk of incurring a larger CESS penalty (relative to BAU/non-ISP project capex, where NSPs can reprioritise or defer projects).

As ISP projects are typically required to facilitate government energy policy, making NSPs accept an asymmetric CESS risk in delivering these projects is inconsistent with the objective of the CESS which intends to provide symmetric incentives[6]. However, if NSPs are required to accept this asymmetric risk, then NSPs should not be penalised if an overspend is ultimately deemed efficient via an ex-post review.

Continuing with the status quo is contrary to the National Electricity Objective insofar as it creates a disincentive for NSPs to undertake necessary efficient investment in electricity services when an overspend is driven by something outside of the NSPs control (e.g. forecasting risk). This type of disincentive would not be in the long-term interests of NSPs or consumers.

CESS flexibility for large non-ISP projects

For large non-ISP projects that aren't delivered as part of an NSPs BAU capex program of work, the AER should consider the specifics of a project on a case-by-case basis and be flexible in its application of the CESS.

If the AER took this approach, the onus should be on NSPs to explain the specifics of the project in their contingent project application/revenue proposal and justify why the AER should apply the CESS differently and how it is in the long-term interests of consumers.

A "large" non-ISP project could be defined as both a dollar amount (e.g. $100 million) and a proportionate amount (e.g. percentage of the NSPs BAU capex during a regulatory control period). This would provide appropriate flexibility to account for NSPs with differing scales of operations.

Abandonment of projects & CESS application

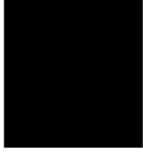
If the total cost incurred by a NSP to the point of project abandonment is lower than the approved project allowance, the NSP should not receive a CESS bonus for not undertaking expenditure.

Providing a bonus in this situation is inconsistent with the intent of the CESS insofar as the underspend is not a result of delivering the project more efficiently than forecast.

[4] HoustonKemp, HumeLink CPA stage 2 - Capital incentives applying to HumeLink, February 2024, section 3.2.
[5] Marinus Link, Attachment 10 - Capital Expenditure Sharing Scheme, December 2024, section 3.
[6] AER, Capital Expenditure Incentive Guideline, April 2023, section 2.1.

Should you wish to discuss any aspects of this submission further, please contact Matthew Clarke at [redacted].

Yours sincerely,



Sandra Thaow
Acting Head of Regulation