# SUBMISSION

## SUPPLEMENTARY SUBMISSION - AER ISP GUIDELINES | JAN 2020

EUAA Energy Users Association of Australia

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**Introduction**

This supplementary submission provides additional comment on the issues we raised in our original submission. In particular it draws on the just released AER decision on EnergyConnect's RIT-T application[1].

Our original submission made two main categories of recommendations - that the AER Guideline be more prescriptive than discretionary, at least for the 2022 ISP, and that the AER retain some form of its current role under 5.16.6 to review the cost benefit analysis. On the latter, we suggested that given the proposed rule changes involve deletion of the AER's RIT-T role under 5.16.6, that this benefits assessment role could be incorporated into an expanded contingent project assessment.

The EnergyConnect report has provided strong evidence supporting our position. In the proposed new actionable ISP rules that remove 5.16.6, consumers will not get this type of report. All we will see is the proponent network's assessment of the net market benefits – in this case a net benefit of $924m based on a capex assumption of $1.53b. We will not see the AER's assessment that the benefits are at most ~$269m and could be negative and this is on the basis of a network proposed cost of $1.53b that is based on a 1-15% of the scope being defined and a possible range of $1.07 – 2.23b.

The foundation of the new rules is the assumption that the consultation process on the ISP will provide sufficient opportunity for stakeholders to provide input into the debate on assumptions and modelling methodology. On this basis it is proposed that disputes can only be raised on matters of process, and only after the final ISP is published.

We think that is a flawed foundation. There is ~42MW data on the AEMO ISP website that consumers are invited to make submissions on by 21st February. While networks do undertake extensive consultation, consumers simply do not have the resources or detailed knowledge to be able to undertake the appropriate level of due diligence. Given this information asymmetry we have relied on the AER to provide this with its 5.16.6 RIT-T reports. These are gone under the new rules.

Now the ESB consultation document on the rules says that (p.7):

> "Where new information becomes available, AEMO may publish an update to the ISP that highlights the new information and the impact on the ISP development path."

[1] AER "Decision – South Australian Energy Transformation" https://www.aer.gov.au/system/files/AER%20-%20Determination%20-%20SAET%20RIT-T%20-%2024%20January%202020.pdf

referring to the proposed 5.22.12. However, it is unclear where that new information would have come from, if EnergyConnect were to be subject to the new rules. This is because there would be no AER RIT-T report to show that there is a material change in EnergyConnect's benefits. All consumers and AEMO would have to make an assessment would be Electranet's analysis showing $926m net benefits. All the AER is left to do is determine the efficient level of capex to go into the RAB, irrespective of whether it considers there are net benefits.

**What the AER concluded in the Energy Connect RIT-T report**

*Assessment of net market benefits*

There has been widespread reporting that the AER's 5.16.6 report "approved" EnergyConnect so that it is a project that should proceed. We think this is a misreading of what the AER actually did.

The AER was presented with a submission from Electranet[2] that indicated EnergyConnect was the preferred option and that it had:

> "net market benefits of approximately $900 million over 21 years (in present value terms)"

Electranet sought:

> "…a determination from the AER pursuant to clause 5.16.6 that the preferred option identified in the SA Energy Transformation PACR satisfies the requirements of the RIT-T."

It is worth quoting at some length the AER's report (pp5-6):

> "For the AER to make a determination that the preferred option satisfies the RIT-T, the preferred option must be the credible option that maximises the net economic benefit to all those who produce, consume and transport electricity in the National Electricity Market (NEM). In undertaking this assessment, we have had regard to:
>
> - the reasonableness of the methodology, inputs, assumptions; and
> - ensuring the modelling does not contain material errors.
>
> If there are no errors in the net benefit calculations, the methodologies are sound, and the inputs and assumptions that affect the ranking of options are reasonable, then we consider the credible option identified as the preferred option satisfies the RIT-T. In applying this approach in our review, we identified a number of critical assumptions and inputs that were material to the estimated benefits of the preferred option.
>
> These critical inputs and assumptions relate to:
>
> - South Australian gas plant usage and retirements;
> - system security requirements, including the impact of system security obligations on the preferred option, the role of pumped hydro in addressing these requirements and the impact on the ranking of the credible options."

The AER's analysis concluded that:

- Electranet had made flawed assumptions on SA gas plant minimum capacity factors that reduced the project NPV from $924m to ~$269m
- The remaining ~$269m of benefits are heavily reliant on AEMO requirements for system security

[2] Electranet letter to the AER 11th April 2019 https://www.aer.gov.au/system/files/ElectraNet%20-%20Letter%20to%20AER%20-%20Request%20for%20AER%20determination%20-%2011%20April%202019.pdf

The latter refers to an AEMO requirement for having two units operating to provide FCAS in the rare case of an unplanned double circuit Heywood outage. In examining this assumption, the AER found that (p.8):

> "We consider that ElectraNet's adoption of this assumption in the SAET RIT- T is reasonable. However, the SAET RIT-T goes further than the 2018 ISP and assumes that only gas plant in SA can satisfy AEMO's two unit constraint. AEMO did not specify in the 2018 ISP that the two unit constraint must be met by gas. Pumped hydro is another source of synchronous generation that could have been considered by ElectraNet. AEMO has subsequently advised the AER that a pumped hydro facility may be able to replace one gas generation unit for system security purposes, but that pumped hydro would not be able to satisfy the two unit constraint at all times unless paired with other synchronous generation (which in SA must be gas).
>
> Based on this advice, we have not considered pumped hydro to be a complete substitute for gas generation in satisfying the two unit constraint. However, we have considered how pumped hydro's contribution to satisfying the two unit constraint would have affected gas generation costs."

The AER's conclusion on the system security issue was (p.7):

> "In examining the additional modelling results, we found that the overall benefit of the preferred option becomes negative if these system security assumptions are relaxed."

*Assessment of capital costs*

The AER assessment simply accepted the Electanet estimate of capex of $1.53b. However, it did note (pp.10-11):

> "ElectraNet's SAET RIT-T indicates that the estimated costs of the preferred option are subject to a high degree of uncertainty. We also understand that there is the potential for updated proposed costs in a contingent project application to diverge from the estimated costs in the SAET RIT-T.
> …
> "While our decision on this 5.16.6 application is that the preferred option satisfies the RIT-T, our assessment is that the costs and benefits of the preferred option may be more finely balanced than [Electranet] suggests. On this basis, any significant changes to the costs of the preferred option could have a material impact on the outcome of the RIT-T."

The AER continued (pp. 79-80):

> "Given the preliminary nature of the estimated costs, ElectraNet has identified the investment as being in line with a Class 4 estimate under the AACE International Recommended Practice and Estimate Classification. This implies that only 1 to 15 per cent of the scope of the project has been defined.
>
> ElectraNet stated that the accuracy range for this estimate is -15 to -30 per cent on the low side and +20 to +50 per cent on the high side. This would mean that the investment cost could reasonably be in the range of $1.07 billion and $2.23 billion."

So, the assessment of the net market benefits is based on a very preliminary view of capital costs.

**Our comments on the AER conclusions**

Rather than the AER approving EnergyConnect to proceed, all the AER has done is fulfil a legal obligation to examine a cost benefit analysis at a particular point in time. That examination has suggested that the large benefits

the proponents of EnergyConnect claim may be illusory. That examination has highlighted that the cost estimates are very preliminary and could increase to over $2b which would wipe out any NPV benefits even if the system security assumptions underpinning the remaining $269m NPV are supportable.

We would appreciate Electranet and AEMO explaining:

- the section in the 2020 ISP where the 2-unit requirement is justified and if so why at least some of it cannot be provided by pumped hydro
- how that requirement interacts with the 2020 Power System Frequency Risk Review, which must be completed by June 2020?

**Next Steps**

Electranet and Transgrid will now prepare their contingent project application seeking a level of capex for the project that will go into the networks RAB. Our understanding is that there is no requirement for the proponents to do another cost benefit analysis and the AER has no power to do so – it has done that at the RIT-T review stage. Its contingent project role is simply to assess the efficient level of capex, independently of whether that capex, if used in the RIT-T cost benefit analysis, would have resulted in negative net benefits in the central case.

It is our understanding is that:

- Electranet and Transgrid are not required to undertake any further consumer engagement following the AER report
- The AER will seek submissions on the contingent project application but the AER is only able to act on submissions relating to the efficient level of capital costs in the RAB
- So even if, say, capex goes above a level that means the $269m NPV reduces significantly or even goes negative, consumers have no avenues to force further consultation or review.

We do not think this process and outcome meets the NEO.

Please contact me if you would like to discuss this submission further.

Sincerely,

Andrew Richards
Chief Executive Officer