

# Submission on the Review of the cost benefit analysis guidelines and RIT application guidelines

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## About the Public Interest Advocacy Centre

The Public Interest Advocacy Centre (PIAC) is leading social justice law and policy centres. Established in 1982, we are an independent, non-profit organisation that works with individuals and communities who are marginalised and facing disadvantage.

PIAC builds a fairer, stronger society by helping to change laws, policies and practices that cause injustice and inequality. Our work combines:

- legal advice and representation, specialising in test cases and strategic casework;
- research, analysis and policy development; and
- advocacy for systems change and public interest outcomes.

## Energy and Water Consumers' Advocacy Program

The Energy and Water Consumers' Advocacy Program works for better regulatory and policy outcomes so people's needs are met by clean, resilient and efficient energy and water systems. We ensure consumer protections and assistance limit disadvantage, and people can make meaningful choices in effective markets without experiencing detriment if they cannot participate. PIAC receives input from a community-based reference group whose members include:

- Affiliated Residential Park Residents Association NSW;
- Anglicare;
- Combined Pensioners and Superannuants Association of NSW;
- Energy and Water Ombudsman NSW;
- Ethnic Communities Council NSW;
- Financial Counsellors Association of NSW;
- NSW Council of Social Service;
- Physical Disability Council of NSW;
- St Vincent de Paul Society of NSW;
- Salvation Army;
- Tenants Union NSW; and
- The Sydney Alliance.

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## 1. Introduction

PIAC welcomes the opportunity to respond to the Australian Energy Regulator's (AER) Review of the cost benefit analysis guidelines and RIT application guidelines consultation paper (the paper).

The Regulatory Investment Tests (RIT) for transmission and distribution are not fit for purpose. Increased rigour in the investment test process is needed to enable meaningful protection for consumers. Consumers currently bear significant risks and costs in the event of material changes in network infrastructure project costs (MCC) but have no way of managing them.

A means to enable meaningful comparison between network and non-network options is also required in order to facilitate selection of the most efficient solutions. Non-network options have a much lower degree of uncertainty concerning cost estimates than network options. As the cost uncertainty for network options is heavily skewed towards cost increases,<sup>1</sup> and this is not well captured by the RITs, the options assessment process is inefficiently biased towards network solutions, with material impacts on consumers.

In this submission we support a number of the proposals in the paper that address these concerns, as well as making some further recommendations.

## 2. Reopening triggers

PIAC supports the proposal for clearly defined, transparent reopening triggers. We also support these taking the form of boundary conditions set in the final RIT report stage.

Given that consumers and other stakeholders are impacted by the risks and costs of MCCs, there should also be clear spaces for input on determining the reopening triggers for stakeholders beyond the project proponents.

This could be done by introducing rigorous processes for stakeholder engagement by the project proponent. It would require the addition of a new test in the final RIT stage where the AER confirms the proponent has sought and used input from key stakeholders, including consumers, on the selection and levels of the boundary conditions.

Alternatively, the proponent could nominate reopening triggers to the AER, and the AER could seek stakeholder input, supporting, contesting or recommending alterations, before confirming the reopening triggers in its approval of the RIT.

To enhance the robustness of the regulatory oversight of MCCs, any stakeholder should have the capacity to alert the AER to the occurrence of an MCC. This should trigger a determination from the AER upholding the assertion or not. The project proponent has a vested interest in the project proceeding and should not be the sole party that can initiate an investigation into whether or not an MCC has occurred.

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<sup>1</sup> AEMO, [Draft 2023 Transmission Expansion Options Report](#). 2 May 2023. Page 25.

### **3. Standardisation of the cost estimate classification system**

PIAC supports the prescription that all RIT applications should use the Association for the Advancement of Cost Engineering (AACE) international cost estimate classification system.

This should include the addition of risk allowances set according to the maturity level of the project.<sup>2</sup> We reiterate our recommendation for an increase in the risk allowances to reflect historical experiences of cost inflation between early-stage planning and project delivery. Risk allowances should also be scaled according to the size of projects, again reflecting the historical experience of larger projects seeing proportionally larger divergences between estimates and final costs than smaller projects.<sup>3</sup>

The inclusion of risk allowances to improve the accuracy of early estimates relative to current standards will go some way to levelling the playing field between network and non-network options.

### **4. Mandating sensitivity analyses**

PIAC supports the proposal for a binding obligation on RIT proponents to conduct sensitivity analyses on the estimated costs of credible options.

The AER should stipulate what mandatory sensitivity analyses should be included, and these should be based on the issues that have caused substantial cost blowouts in recent years: changes in routes, labour supply issues, international supply chain-impacted inputs, and social licence issues.

We recommend that the prescribed sensitivity analyses are not exhaustive, and proponents are encouraged to include sensitivity analyses beyond those stipulated as mandatory in the guidelines.

### **5. Requiring proponents to set out their cost estimation methodology**

PIAC supports the proposal to require project proponents to set out their cost estimation methodology, including key inputs and assumptions. However, while the added transparency is a positive, it is meaningless without being accompanied by powers for the regulator to assess the credibility of the cost estimations.

As a minimum, any cost passed through to consumers in toto, such as those associated with acquiring social licence for a project, should have substantive, rather than merely process-based oversight from the AER. This will go some way to addressing the inefficiencies and inequities caused by consumers bearing these risks and costs, but having no channel by which to manage them.

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<sup>2</sup> As cited in AEMO's [Draft 2023 Transmission Expansion Options Report](#), page 25.

<sup>3</sup> PIAC [Submission to the Draft 2023 Transmission Expansion Options Report](#). 31 May 2023.

## 6. Early works

PIAC supports the proposal for the AER to provide guidance on what activities are covered by the term early works. We recommend the AER also assess what proportion of activities conducted as part of early works by a proponent fall reasonably within the guidelines, and whether the associated costs are reasonable.

We appreciate there is a net reduction in overall project costs from effective and extensive early works. However, the fact that the costs of early works are passed on entirely may incentivise project proponents to shift costs forward to early works in a way that is not efficient. This inefficiency is borne of consumers having no capacity to protect themselves against increases in the costs of early works.

An alternative to the arrangement and provision of guidance would be to place the onus on project proponents to provide evidence that activities undertaken as part of early works reduced overall costs for the project. There would still be a need for the AER to assess these claims before costs were passed through to consumers, but it would be a more difficult task. There would also be greater uncertainty for the project proponent regarding what proportion of early works costs would be approved. Overall, under this approach we would expect the volume of early works to fall as proponents avoided the risk of being left with part of the costs, leading to higher overall project costs.

Regardless of the approach taken, the addition of guidance about what activities can be included in early works will not be a sufficient, efficient remedy without a role for the AER substantively assessing the claims made about the activities completed as part of early works and the costs of those activities. The proposal aims to “provide clarity with the flexibility for RIT proponents to determine which activities are consistent with the definition of early works on a project basis”<sup>4</sup>. In order to manage the exposure of consumers, the ultimate determiner of which activities are consistent with the definition must be the AER.

## Continued engagement

We welcome the opportunity to meet with AEMO and other stakeholders to discuss these issues in more depth. Please contact Michael Lynch at [mlynch@piac.asn.au](mailto:mlynch@piac.asn.au) regarding any further follow up.

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<sup>4</sup> AER, Review of the cost benefit analysis guidelines and RIT application guidelines Consultation Paper, May 2023, page 21.