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14 September 2020

Ms Clare Savage  
Chair  
Australian Energy Regulator  
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By email: Clare.Savage@aer.gov.au  
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Copy to:

Audrey Zibelman, Chief Executive Officer, Australian Energy Market Operator (AEMO)  
James Hay, Deputy Secretary Energy Climate Change, Sustainability & Waste, Department of  
Planning, Industry & Environment

Dear Clare

### **HumeLink project – staging of the Contingent Project Application process**

Further to my letter of 4 August 2020, I am writing to update you on our proposed approach for progressing HumeLink<sup>1</sup> through the Regulatory Investment Test for Transmission (RIT-T) and the contingent project application (CPA) processes, following our recent discussions with the Australian Energy Market Operator (AEMO) and Australian Energy Regulator (AER) staff. This includes refinements to our understanding of the practical application of the AEMO's "feedback loop" under clause 5.16A.5 of the new Integrated System Plan (ISP) National Electricity Rules (Rules).

As you may be aware, we are currently in the process of agreeing underwriting support for HumeLink with the NSW Government. We want to ensure an efficient regulatory process given that HumeLink will be one of the first projects considered under the new ISP Rules.

### **Proposed regulatory process**

Our revised understanding of the regulatory process for HumeLink following recent discussions with AEMO and AER staff is as follows:

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<sup>1</sup> The reinforcement of the southern transmission network

1. We can elect for Humelink to proceed under rule 5.16A<sup>2</sup> pursuant to clause 11.126.5<sup>3</sup>, which provides that an **existing** RIT-T proponent may either continue to apply former rule 5.16<sup>4</sup> or new rule 5.16A to an actionable ISP Project.,
2. If TransGrid makes this election, it can apply rule 5.16A, and in particular clause 5.16A.4, to the publication of a Project Assessment Conclusions Report (**PACR**). Our understanding is that TransGrid would not be **required** to issue a new PADR under paragraphs (c) to (h) of rule 5.16A.4.
3. We also understand that the PACR would not have to consider Humelink (or any other options) for project staging. Rather, staging relates to the CPA process with the AER under clause 6A.8<sup>5</sup> as discussed further in steps 4 to 10 below. This is notwithstanding that:
  - (a) the Humelink PADR does not identify Humelink (or any other options) as a staged project, and
  - (b) HumeLink is not a staged project in the 2020 ISP.
4. Prior to lodging a CPA under rule 6A.8, we must obtain AEMO's written confirmation in respect of the project under clause 5.16A.5(b) of the Rules (**Feedback Loop**) that:
  - (a) the preferred option addresses the relevant identified need, and aligns with the optimal development path, in the most recent ISP; and
  - (b) the cost of the preferred option does not change the status of the project as part of the optimal development path.
5. AEMO's Feedback Loop would be required for CPA1 and may be required for CPA2 depending on the updated cost of the Project and whether there have been any material changes.
6. For CPA1, involving the RIT-T process and early works / planning stage of the project, the Feedback Loop will involve us seeking AEMO's written confirmation that:
  - (a) the preferred HumeLink option (i.e. the full project and related costs) addresses the relevant identified need, and aligns with the optimal development path, in the most recent ISP. The application will include details of the CPA staging and the costs of the works proposed under CPA1 and AEMO will include in its confirmation an acknowledgement of the intended sequencing of works and its expectation, in the circumstances of the Staged CPA Process, that should CPA2 reveal that the total costs of the project exceed those considered in the AEMO Feedback Loop for CPA1, then AEMO would need to consider the updated project in a further Feedback Loop before a CPA2 is lodged; and
  - (b) the overall cost of the preferred HumeLink option, as identified in the PACR, and the costs of the works proposed under CPA1, do not change the status of the project as part of the optimal development path but noting that the AER will only be approving a portion of the costs and we will return through the AEMO Feedback Loop, if necessary, in respect of CPA2 for the fully scoped and costed project.
7. Subject to AEMO's written confirmation, we can submit CPA1 to the AER under clause 6A.8.A1(b) of the Rules for the AER's determination under clause 6A.8.2(e) for CPA1 (assuming the CPA1 costs exceed the threshold set out in clause 6A.8.1(b)(2)(iii) of the Rules). CPA1 will only be for a determination to reopen the AER's 2018-23 revenue determination for TransGrid in relation to the CPA1 costs such that references in clause 6A.8 to the actionable ISP project and contingent project

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<sup>2</sup> This clause applies a modified RIT-T process to actionable ISP Projects.

<sup>3</sup> This clause applies to existing actionable ISP projects prior to the clause 5.16.6 stage.

<sup>4</sup> This is the existing clause which sets out the process applicable where the actionable ISP Project is a proposed contingent project in the proponent's revenue determination.

<sup>5</sup> This clause sets out the process for contingent projects, including new arrangements for actionable ISP projects considered under clause 5.16A.

will be read as a reference to that part of Humelink comprising the works covered by CPA1. Given the nature of the CPA1 activities (being one off activities), we are likely to propose that the CPA1 costs comprise actual and expected capital costs to be added to the regulatory asset base

8. If our understanding is correct then, in accordance with clause 6A.8.2 of the Rules, the AER would make a determination within 40 business days but with the ability to extend the timing for another 60 business days in complex cases. Given the tight timeframes and the lack of precedent with the ISP Rules, we understand the AER would be willing to receive information and briefings in advance of the formal CPA1 application with a view to putting the AER in a position to make a determination as soon as reasonably possible. The provision of advance information and engagement by TransGrid will be a key driver for the AER being able to make its determination quickly.
9. Subject to TransGrid fully scoping and costing the project and confirming the net benefits following the approval by the AER of CPA1, TransGrid may then need to seek AEMO's confirmation under the AEMO Feedback Loop for the full Project costs if they increase from CPA1, being the final forecast capex for construction and commissioning works for HumeLink and the costs approved in CPA1. This would ensure AEMO can reconsider the full updated costs of the project and whether the project continues to meet the identified need and remains part of the optimal development path, having regard to the total cost of the project. For this process, we would rely on the PACR but use the fully detailed costs arising from the work done under CPA1. That is, absent a material change in circumstances, we would not be required to issue a new PACR or undertake further market modelling. However, we and the NSW Government are aware that the CPA Staged Process introduces a risk that circumstances may change between CPA1 and CPA2 such that the preferred Humelink option in the PACR may not meet this second confirmation under the Feedback Loop and therefore we may need to reapply the full RIT-T unless the AER determines otherwise.
10. Subject to AEMO's further written confirmation where required, we could then submit CPA2 to the AER under clause 6A.8.A1(b) of the Rules for the remainder of the project costs assuming that the CPA2 costs exceeds the threshold set out in clause 6A.8.1(b)(2)(iii) of the Rules and the aggregate costs under CPA1 and CPA2 do not exceed the project costs considered by AEMO under the relevant Feedback Loop.

### **Implications for the Regulatory Asset Base (RAB)**

As noted above, there is a risk that the project does not proceed to either CPA2 or construction following CPA2 approval. In these circumstances, we seek the AER's confirmation that the CPA1 costs included in the RAB will not be treated differently to where the project had proceeded to completion. For example, the CPA1 costs in the RAB should not be subject to any additional future disallowance risk merely because those costs did not ultimately lead to the construction of specific assets providing prescribed transmission services.

### **Confirmation of AER proposed process and AER Guidance Note**

The Staged CPA Process has significant impacts on how we will proceed with HumeLink and the timing of the project. Accordingly, we are seeking the AER's advice and input on our understanding of the process, as set out in steps 1 to 10 above, on how HumeLink should proceed as staged CPAs under the new ISP Rules.

As noted in our previous letter, a Guidance Note on the HumeLink RIT-T, issued by the AER, would be of great assistance and value to stakeholder engagement through the remainder of the RIT-T consultation and CPA processes.

I would appreciate a meeting with you to discuss this matter and look forward to hearing from you soon.

Yours sincerely

A handwritten signature in black ink that reads "Paul Italiano". The signature is written in a cursive style with a large initial 'P'.

Paul Italiano

**Chief Executive Officer**