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Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney NSW 1235

Lodged online via: www.aemc.gov.au

Dear John,

Consultation Paper: Establishing values of customer reliability

TransGrid welcomes the opportunity to respond to the AEMC's consultation paper in relation to the Establishing values of customer reliability (VCR) rule change request.

TransGrid is the operator and manager of the high voltage transmission network connecting electricity generators, distributors and major end users in New South Wales and the Australian Capital Territory. TransGrid's network is also interconnected to Queensland and Victoria, and is instrumental to an electricity system that allows for interstate energy trading.

In its 2013 reviews of the national framework for transmission and distribution reliability, the AEMC recommended making the Australian Energy Regulator (AER) responsible for establishing VCRs. The AEMC noted that this would be consistent with its role as the economic regulator, with which the COAG Standing Council on Energy and Resources (now COAG Energy Council) agreed.

Since the 2013 reviews, Australia has experienced a notable change in its focus on the reliability of the energy system. In particular, reliability has become a bigger focus, driven by changing community expectations and choices, advances in renewable energy technologies, retirement of existing and dispatchable generation, and the adjustments required in Australia's economy to meet our international climate change commitments. These changes raise complex issues in relation to the design of the National Energy Market (NEM) and have led to a greater focus on ensuring reliability of supply and where that supply comes from. The establishment of the Energy Security Board, the proposed National Energy Guarantee and the inaugural Integrated System Plan are recent examples of this.

VCR estimates form an important input into reliability standards, economic assessment of optimal levels of reliability and other economic analyses, including those that impact investment decisions and capital work programs. It is also used in network planning assessments, such as the regulatory investment tests. TransGrid has contributed to an industry response through Energy Networks Australia and agrees with the issues raised and recommendations outlined in its submission.

Given the importance and expansive use of VCRs, TransGrid would also like to provide further information relevant to the responsibility of establishing VCRs and the methodology applied.

1. Responsibility for establishing VCRs

TransGrid supports a single national body having the responsibility for establishing, reviewing, updating and publishing a VCR methodology and VCR estimates across the NEM. The development of a consistent and robust VCR methodology is likely to provide stability and predictability of jurisdictional VCR estimates. This will help support and facilitate efficient network planning processes and capital work programs.

TransGrid understands that the AEMC and COAC Energy Council are seeking to assign this role to the AER. We would like to raise several issues which we think need to be addressed if the AER is to be assigned this responsibility in the National Electricity Rules (NER).

a. Separation of roles

VCR estimates underpin a substantial proportion of capital work programs, both augmentation and replacement capital expenditure. As part of its role as economic regulator, the AER is responsible for making network service providers' (NSPs) revenue determinations and monitoring and enforcing compliance with application of the regulatory investment tests by NSPs. Under the rule change, the AER would be reviewing the application of its own VCR estimates. It would be prudent for the AER to ensure transparency and a separation of roles between functions that determine VCR estimates and functions that review these estimates as inputs into a revenue determination process or a regulatory investment test.

b. Expertise in establishing VCR

At present, jurisdictional regulators are responsible for determining NSP reliability standards. The AER itself has no specific expertise in identifying the optimal value of reliability for customers. This issue is further exacerbated by the complexity of the problem being solved, which requires a significant investment in time, research and consideration.

c. VCR and the Reliability Panel

The Reliability Panel has the responsibility and expertise in establishing the level of reliability customers can expect and the level of investment required to deliver on this standard. The AER and the NEM more broadly would benefit from this expertise being utilised in establishing VCR. The benefits include the fact that the Reliability Panel:

- Is already assigned to other matters that are closely related to reliability and is specifically required to have regard to the VCR under the NER. Bringing these roles together would ensure any interaction is sufficiently considered.
- Is made up of a cross section of market institutions and industry players, thus ensuring a balanced view.
- Has demonstrated it has the capability to sufficiently engage expertise and consult widely before coming to conclusions, which is required to solve complex problems.

Given the concerns raised above, TransGrid recommends that the AER receives support from bodies with strong technical and subject matter expertise such as the Australian Energy Market Operator (AEMO) and the Reliability Panel.

2. VCR methodology

Given the importance of VCR estimates, consultation should be extensive and undertaken with all stakeholders who make decision or are impacted by the outcome of decisions where VCR is used; in particular: retail customers of all sizes, AEMO, the Reliability Panel, the jurisdictional network regulators responsible for setting reliability standards, and network service providers. The AEMC should consider a rule requirement that the development of the VCR methodology includes direct engagement of all types users of VCRs, and not only retail customers as suggested in the indicative drafting proposed for 8.12 (b) (iii).

The VCR methodology must provide a robust and comprehensive reflection of the different jurisdictions, customer types (by size and activities undertaken) and duration and frequency of an electricity outage. The drafting of the VCR methodology under the NER should reflect this, as well as ensure that the methodology is fit for purpose. The VCR methodology must contain an appropriate methodology for properly understanding and reflecting the value customers ascribe to the effect of low probability and high impact events, which was not reflected in AEMO's VCR Review in 2014. During the development of a new reliability standard recently in NSW, TransGrid received independent economic advice that without this, VCR estimates are likely to be understated.[1] The AEMC should consider additional drafting to address this in 8.12 (c) of the proposed new clause.

3. VCR periodic reviews and timing

The 31 December 2019 deadline for the AER to complete the initial VCR methodology appears acceptable. Given the extensive impact of changes to VCRs on long term network planning and network capital work programs, certainty on the publication date of the first estimates of VCRs is essential. As such, TransGrid suggests the AER confirms upfront that it is committed and able to deliver the initial VCR methodology by the 31 December 2019 deadline.

Changes to VCR estimates can have significant impacts on current capital work programs underway, both with regulatory revenue determinations and regulatory investment tests. TransGrid recommends transitional arrangements are provided to help NSPs manage these changes.

4. VCR annual adjustments and timing

Investment decisions and network planning processes are dependent on robust VCRs as inputs to models. Regulatory investment tests for networks are a complex process, which take a significant amount of time and expense. Stability, certainty and consistency of VCR estimates is crucial for this process to run efficiently. Annual adjustments of VCRs should not be required under the NER unless these are limited to escalations factors already included in the VCR methodology.

It is important that VCR estimates are relatively stable over a reasonable timeframe. Any changes to VCR estimates should provide an adjustment period to reduce the impact on investment decision modelling underway. The Reliability Panel sets its reliability standard and settings for NEM two years ahead. The AEMC should consider a similar arrangement for reviews of the VCR.

TransGrid appreciates the opportunity to comment on the AEMC's consultation paper report on the 'Establishing values of customer reliability' rule change request. If you would like to discuss this submission, please contact Rebecca El-Khoury, Regulatory Analyst on 02 9284 3299.

Yours faithfully

Caroline Taylor

Caroline Taylor
Acting Executive Manager, Regulation

[1] Houston Kemp 2016, *CBD and Inner Metro VCR estimates - A final report for TransGrid on research, methodology and results*, 28 July, Sydney, available at: https://www.ipart.nsw.gov.au/files/sharedassets/website/shared-files/investigation-section-12-publications-electricity-transmission-reliability-standards/consultant-report-transgrid-vcr-estimates-july-2016.pdf