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The Chairman
Australian Energy Market Commission
Level 16, 1 Margaret Street
SYDNEY NSW 2000

By email to submissions@aemc.gov.au

Dear Chairman,

Scale Efficient Network Extensions – Draft Determination

AGL Energy welcomes the opportunity to comment on the Australian Energy Market Commission's (AEMC) *Draft Rule Determination National Electricity Amendment (Scale Efficient Network Extensions) Rule 2011*.

As the leading investor in renewable energy in Australia, AGL Energy (AGL) is well placed to comment on transmission policy. AGL operates across the supply chain and has investments in coal-fired, gas-fired, renewable and embedded electricity generation. AGL is Australia's largest private owner, operator and developer of renewable generation in Australia with 1,073 MW of renewable capacity (at 30 June 2010). AGL is also a significant retailer of energy with over 3 million electricity and gas customers.

AGL supports implementation of the Draft Rule. The AEMC has done an outstanding job balancing the interests of generators, transmission network service providers, customers and other stakeholders in developing this alternative to the four options presented in the previous Options paper. This submission reflects AGL's further engagement in the SENE concept, and should be considered in conjunction with previous submissions: to the SENE Discussion Paper in May 2010; and to the SENE Options Paper in November 2010.

Principles for transmission policy

AGL contends that transmission policy should be set in a way which ensures economic efficiency (including allocative, dynamic and productive efficiency) is maximised while security of electricity supply is maintained. In a previous submission on the original SENE concept, AGL prepared the following principles. They are considered to be consistent with the objectives of the National Electricity Rules and provide for a competitive market.

1. Transmission policy should deliver efficient transmission prices which incentivise generation proponents, all other things being equal, to locate their investments as close to load centres as possible.

2. Extensions of transmission networks should be financed solely by the benefiting entities. Only where existing infrastructure is upgraded to the benefit of other participants as well as connecting entities can the costs be appropriately shared across all the benefiting parties. Impacts of additional charges on existing generators should be minimised unless those generators are the proponents of the augmentation.

3. The risks and returns of developing infrastructure should be appropriated on the same entities. In other words, policies that ensure economic returns flow to generation proponents and transmission network service providers (TNSPs) for investments made should ensure that the risks of failure are apportioned towards these same entities.

4. Electricity customers should not be required to underwrite the development of transmission services as customers do not receive any share of the profits, should the investments generate economic returns. In other words, policy settings should not privatise profits and socialise losses.

AGL considers that the Draft Rule is consistent with the four principles articulated above. By focusing only on the provision of information to market participants, the Rule ensures that the risks and returns of developing infrastructure remain with those that make the investment decision.

Public policy rationale for Draft Rule

Based upon the principles articulated above, AGL strongly opposed the original proposal related to SENE. In its original form the proposed change would have allowed a regulatory body to determine the creation of new infrastructure. Network providers would have then been able to recover costs from consumers irrespective of whether the infrastructure became fully utilised. In this form, the SENE concept was considered to be conflicting with the near-two decade long reforms to the energy market. Such reliance on central planning introduces an array of risks in the circumstances where no market failure has been evidenced.

The revised Draft Rule overcomes the limitations of the original proposals by focusing only on the public policy rationale for change. It could be argued that the key limitation of the existing regulatory framework (in relation to scale development) is the lack of transparent and comparable information which would allow a SENE to be adequately considered by an investor. The Draft Rule seeks to address this limitation by focusing on ensuring that a transmission network service provider is incentivised to conduct a study into the need for a SENE.

This Draft Rule is not without precedent. The Australian Energy Market Operator already publishes a Statement of Opportunities to provide guidance on demand forecasts and transmission capabilities. The Draft Rule essentially requires a similar publication (albeit where requested by a proponent) by a transmission network service provider with the following key pieces of information:

- the location of the SENE (including its connection point to the present network);
- the configuration of the SENE including its technical specifications; and
- a comparison between the total project expenditure associated with a scenario in which a SENE is constructed and a scenario where a SENE is not constructed.

With this information publicly available, each market participant will then be able to make a decision on whether to invest in the development of the SENE within the existing market and regulatory structure. AGL has consistently argued that where market participants are prepared to financially commit to a likely future generation location, they are free to structure arrangements to adequately extend (or increase the capacity of) transmission to the anticipated region. The open season process provides for these arrangements, and allows those who are most informed, to take on the associated risks of extensions and new build. This conclusively avoids the need for central planning interjection or any abstraction of the energy market reforms.

The gas industry routinely manages the situation that the SENE concept is seeking to address, that is, a large fuel source with a number of users who are competing with each other to get the fuel to a common location. In that industry, participants jointly arrange the construction of necessary facilities to service their needs without recourse to public subsidy or regulatory intervention. The Draft Rule acts to facilitate such joint investment by ensuring the adequate and transparent information is made available.

Recent analytical work in relation to scale developments

The Draft Rule may be criticised by proponents of remote renewable generation clusters. AGL strongly believes that if proponents of remote clusters have more cost effective projects (including transmission connection costs) than resources closer to the existing grid, there is no regulatory impediment related to their financing a connection. The actual impediment is likely to relate to the total project costs of renewable resources being developed today being lower than those of the remote clusters. A study carried out by ROAM Consulting for the Clean Energy Council[1] (of which AGL is a member) suggests that:

- it is possible to arrange a sufficient quantity of wind farms to meet the 20% RET by 2020 with minimal transmission congestion or significant transmission augmentation; and

- highly concentrated wind development with substantial transmission development to allow export of generation to the NEM does not appear to be the lowest cost way of meeting the RET.

This modelling suggests that in an optimised least-cost scenario, the cost of the transmission required to support wind investments to meet the 20% RET is small. In other words, costs to consumers will be lower with the existing regulatory framework than if a more interventionist approach in relation to transmission is adopted.

Conclusion

AGL considers that, given the dynamic nature of the energy market, the competitive market will develop solutions to capture the economies of scale available in connection and extension assets if the savings are significant. AGL sees no reason why the competitive market will not drive efficient outcomes. The distortionary impacts of a regulated approach with the potential for asset stranding must be avoided. As such, AGL strongly supports the AEMC's Draft Rule with its emphasis on information provision.

Should you have any questions in relation to this submission, please contact me at tanelson@agl.com.au or on (02) 9921 2516.

Yours sincerely,

Tim Nelson
Head of Economic Policy and Sustainability

[1] See ROAM Consulting report to Clean Energy Council, *Transmission Congestion and Renewable Generation*, October 2010.