The Hon Tom Koutsantonis MP
Member for West Torrens

eA153990

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Mr John Pierce
Chairman
Australian Energy Market Commission
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Dear Mr Pierce John

Thank you for the opportunity to comment on the Australian Energy Market Commission's (AEMC) *Transmission Frameworks Review – First Interim Report.*

As indicated in previous South Australian Government submissions to the Transmission Frameworks Review, we consider the issue of generators connecting to the network without facing the true costs of their impact on the wider transmission network needs to be addressed. The development of a framework that provides incentives for generators to locate in uncongested parts of the network is consequently a key concern for consideration under this review.

South Australia therefore welcomes the AEMC's comprehensive work in developing potential mechanisms to improve the current transmission frameworks. Officers have reviewed each of the packages proposed and assessed them against the key South Australian issues. More comprehensive commentary on the First Interim Report from the department is attached.

We consider a regional optional firm access (OFA) model as presented in Package 4 provides the basis to address some of the issues that currently exist. Locational signals for generation will be significantly improved by exposing generators that wish to have firm access rights to the cost of upgrading the network and exposing non-firm generators to the potential to pay higher compensation costs, should either locate in constrained parts of the network.

In terms of the charging approach for the regional OFA model, South Australia considers that deep connection charging would be less complex and more effective in influencing the locational decision of a new generator entrant. South Australia also supports the development of a reimbursement scheme that would require subsequent new generators to rebate a proportion of the original cost to the first mover. South Australia also considers that incumbent generators that choose to have firm access rights should be liable to pay some charge where the underpinning transmission network capacity already exists to support such an application.

South Australia is also supportive of reforms that would improve coordination and transparency in the national planning process. A harmonised national transmission planning regime would reduce costs on market participants and provide greater consistency.

However, we consider that the current arrangements for the Regulatory Investment Test for Transmission (RIT-T) are too time consuming and process driven. While we do not have any issues with the general principal of improving the transparency of the RIT-T, it is important that any additional requirements do not further expand the already onerous and lengthy process.

With regard to connections, it is recognised that the current National Electricity Rule (NER) provisions can result in challenging negotiations for new connections. The ambiguity of the connections provisions will be an area of increasing concern as new and remote generation increases on the transmission system. This is of particular concern to South Australia with increasing levels of geothermal and wind generation in remote areas. We therefore support amendments to the NER to make the connections process clearer and more efficient for all parties.

However, with regard to the more significant connections reforms proposed, South Australia supports the AEMC's second option which proposes enhancements to the negotiating framework that improve the transparency of the connections process and also alleviates any existing information asymmetries.

Finally, South Australia supports allowing third party access to network extensions. Consideration should be given to the rights of incumbent generators in these situations, such as mechanisms to reimburse them for any capital contributions they have made towards the cost of the extension, and to compensate them should they face greater constraints following the connection of the new generator to the extension. South Australia encourages further investigation by the AEMC on these issues.

Should you have any questions in relation to this submission, please contact Rebecca Knights, Director, Energy Markets, Energy Markets and Programs Division on (08) 8204 1715.

Yours Sincerely

Hon Tom Koutsantonis MP
Minister for Mineral Resources and Energy

2 February 2012

Attach: submission from the Department for Manufacturing, Innovation, Trade, Resources and Energy

2010//04175/01
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Government of South Australia
Department for Manufacturing, Innovation, Trade, Resources and Energy

Reference: EPR0019

Department for Manufacturing, Innovation, Trade, Resources and Energy (DMITRE) Submission to the Australian Energy Market Commission's (AEMC) Transmission Frameworks Review – First Interim Report.

The Energy Markets and Programs Division of DMITRE thank you for the opportunity to comment on the Australian Energy Market Commission's (AEMC) *Transmission Frameworks Review – First Interim Report.*

As indicated in our previous submissions to the Transmission Frameworks Review the main area of concern for South Australia is the inefficient locational decisions made by generators which result in congestion on the South Australian transmission network. The development of a framework that provides incentives for generators to locate in uncongested parts of the network is a crucial issue for South Australia.

Energy Markets and Programs Division considers that the current framework does not provide sufficient incentives for generators looking to connect in unconstrained areas of the network. The access regime allows for generators to connect to the network at a chosen location without facing the true costs of their impact on the wider transmission network, for example 'deeper' augmentation costs.

Pathways to Reform

South Australia welcomes the AEMC's comprehensive work in looking at potential mechanisms to improve the current transmission frameworks. We have considered each of the packages proposed in light of the issues that we have raised previously.

We do not support the AEMC's Package 1 which reinforces the current access regime by removing clause 5.4A from the National Electricity Rules (NER) and therefore removes any ability for generators to negotiate firm access with a transmission network service provider (TNSP). Clearly this does not address the issues, such as the lack of locational signals and congestion, which are already evident and likely to increase in impact over time.

While South Australia notes that incorporating a congestion pricing mechanism into the current open access regime, as proposed in Package 2, is likely to correct some of the distortions created by instances of congestion, such as disorderly bidding, we consider that this fails to address the underlying transmission issues that result in congestion in certain parts of the network.

Introduction of a generator reliability standard as proposed in Package 3 would likely improve the effectiveness of locational signals to a degree. However, as it is a mandatory standard with a corresponding generator transmission use of system (TUoS) charge, it lacks the flexibility to enable a generator to determine if it values increased reliability enough to pay an additional cost, and for how much of its capacity. Further there is likely to be significant complexity in determining the costs that are attributable to maintaining load service standards or generator service standards, in a particular zone or region.

South Australia considers that a regional optional firm access model as presented in Package 4 has the potential to address the issues that are created by the current framework. South Australia considers that under a regional optional firm access model, locational signals for generation will be significantly improved. This is because generators purchasing access rights will face the costs of investment in the network to meet the required generation planning standard, which is likely to be higher in areas where the network is already relatively constrained. Further, non-firm generators will face greater exposure to paying compensation to firm generators if they locate in an already constrained part of the network. Importantly, the advantage that this model has over general reliability standards is that generators are able to consider the differing access costs between particular locations, whether to become firm or non-firm and for what proportion of their capacity. This allows a decision to be made that is the most efficient for a particular generator.

The AEMC discusses in its paper the possibility of using either deeper connection charges or a generator TUoS which would reflect the costs associated with the provision of the network capacity underpinning the access rights. South Australia considers that deep connection charging would be more effective in influencing the locational decision of a new generator entrant. Facing the full cost of investing in additional network capacity is likely to present a strong signal against locating in areas where augmentations would be required. Similarly, a signal would exist to connect where (or when) there is spare capacity due to corresponding low charges. This may promote more efficient use of the network and provide a more effective locational signal than any form of generator TUoS.

Deeper connection charges also provide a less complex approach to charging generators for firm access rights. Many of the issues the AEMC raises in regards to using this mechanism for charging are able to be addressed and are certainly no less insurmountable than those associated with forms of a generator TUoS mechanism. As the AEMC notes in appendix D, any first mover disadvantage could be addressed through the development of a reimbursement scheme that would require subsequent new generators to rebate a proportion of the original cost to the first mover.

South Australia considers that the discrimination between incumbent and new entrant generators could also be addressed through the operation of a hybrid generator TUoS and deeper connection charges model. Under such a model incumbent generators that take up the option to have firm access rights would be liable to pay some level of generator TUoS charge where the underpinning transmission network capacity already exists to support such an application. This charge would be in recognition of the generator receiving a new firm access right. Revenue from this charge would be used to offset charges on load in recognition that they have initially funded the infrastructure that is now providing a service to the firm incumbent generator. New generators that take up the option of firm access would face the required deep connection charges or reimbursement payments to a previously connecting generator.

We encourage the Commission to consider the potential impact that accurate locational pricing signals across the market may have on the locational decisions of generators and the subsequent effect this may have on the level of congestion. We consider that maintaining the status quo in this area is unacceptable.

Planning

South Australia is supportive of reforms that improve coordination and transparency in the national planning process, in particular inter-regional planning, and allow opportunities to be identified for a more coordinated approach.

We support an incentive based regulatory and planning regime for transmission networks that incorporates economically derived reliability standards that are deterministically expressed. We also agree with the AEMC that financial incentives are likely to provide the most robust and transparent driver for efficient decision making regarding network investment.

We agree with the AEMC's previous recommendations to the Ministerial Council on Energy (MCE), which promoted a national framework for transmission reliability standards for load. This approach allows states to continue to set the most appropriate standards for their jurisdiction, while allowing greater national transparency and comparability.

South Australia also supports the option to improve the consistency of the Annual Planning Reports (APR's). We consider that transparency could be improved in the planning process, at relatively low cost, by requiring greater consistency in the presentation of TNSPs APRs, making it easier to compare outcomes between individual APRs and the National Transmission Network Development Plan (NTNDP).

While the enhanced coordination of the NTNDP and TNSP's APRs would improve the planning of National Transmission Flow Paths, South Australia considers that the requirement for bilateral endorsement could potentially result in significant delays in the release of the NTNDP and a TNSP's APR in the event that agreement could not be reached.

An alternative may be for endorsement to only be required from the Australian Energy Market Operator (AEMO), in its role as the National Transmission Planner, for a TNSP's APR to ensure that it appropriately reflected the NTNDP. However, South Australia would like to see further detail on how endorsement by AEMO would work in practice, what would occur if endorsement was not provided and how the benefits stated by AEMC would be achieved. At a minimum, clear timeframes and a clear process for handling disagreements should be set so that delays in releasing the APRs do not occur.

South Australia does not have any issues with the general principal of improving the transparency of the Regulatory Investment Test for Transmission (RIT-T). It is important, however, that the AEMC does not consider introducing any additional requirements that would further expand the already onerous and lengthy RIT-T process. Despite AEMO and ElectraNet commencing a Feasibility Study in 2010, the current RIT-T process for an upgrade to the Heywood interconnector is still in the early stages. The Project Specification Consultation Report was released in October 2011 and is only the first stage of the RIT-T process to undertake extensive consultation on the credible options and markets benefits associated with a Heywood upgrade. A Project Assessment Draft Report is still to be released, with a final report to follow. AEMO state that the upgrade to Heywood could be

commissioned by June 2016 (at the earliest), depending on the outcome of the RIT-T. We consider this process to be very time consuming and process driven. This is coupled with the lack of incentives for AEMO and ElectraNet to undertake the review of the Heywood Interconnector in the first place, as noted in our previous submission. We would be concerned if changes were made that further extended this process.

We are also concerned that in some cases modelling has already substituted for planning rather than informing it. The AEMC should consider any impact that proposed changes are likely to have on the already extensive RIT-T process and whether any additional benefits are likely to be material and better inform final decision making.

Connections

South Australia agrees that the current NER provisions regarding connections lack clarity and would result in negotiations for new connections being more challenging than they should. We therefore support general amendments to the NER to make the connections process clearer and more efficient for all parties. These amendments should be made regardless of the final recommendations on the matters raised in Chapters 13 and 14 of the First Interim Report.

Specifically, we support amendments that clarify what each transmission service required to connect to the network involves and these provisions should include the clear boundaries of what is considered a shared transmission service, a connections service and an extensions service. TNSPs obligations regarding connections and the provision of services should be clear and whether the construction of the underlying asset is included in the provision of a service should be unambiguous.

As mentioned in the Directions Paper, the ambiguities related to the connection service will be an area of increasing concern as new and remote generation increases on the transmission system in response to both demand and climate change policies. This is of particular concern to South Australia with geothermal and wind generation opportunities in remote areas.

With regard to the more significant reforms proposed, South Australia supports enhancements to the negotiating framework which improve transparency associated with the connections process and alleviate any information asymmetries that currently exist (Proposal 2 in Chapter 13). We consider it is important to ensure that as much information as possible is provided by TNSPs that would allow greater ability for the connecting parties to forecast potential costs early in the process. It is equally important that TNSPs charges are cost-reflective and that the process that leads to the formulation of these charges is transparent.

Submissions to the AEMC's Directions Paper revealed that generators believe there is little transparency with regard to how TNSPs arrive at the cost and technical design of a connection. While the NER state that TNSPs can charge a 'reasonable cost', there is no direct NER requirement for 'reasonable' to equate to 'efficient'. The measures proposed by the AEMC would be expected to alleviate these concerns.

While South Australia is supportive of measures that increase transparency, we question the proposed requirement which requires TNSPs to publish indicative or

average costs of connection on an annual basis. We consider there is some merit in such a proposal as this increases the information available to prospective connection applicants, however, there are issues with this approach. As the indicative cost required for connection will vary greatly according to the type, size or location of the generator being connected, the published costs of connection may not provide much value to prospective applicants. The AEMC will need to consider these issues, and how the requirement would best be drafted to ensure it provides value to connection applicants, prior to implementing the measure.

South Australia does not agree with the option to regulate the weighted average cost of capital (WACC) that could be applied to all transmission services that are categorised as negotiated transmission services. If a connection service is categorised as a negotiated service and therefore contestable, it seems inconsistent to then apply a regulated WACC to these services. Rather than supporting a regulated WACC to constrain a TNSPs ability to charge for services above an efficient rate of return, it is preferable that the framework is clear on what level of competition is permitted in the provision of these services to ensure that sufficient competition exists, and charges are maintained at an efficient level.

With regard to the other options proposed by the AEMC for amendments to improve the balance in bargaining power between TNSPs and network users, South Australia does not support the proposed amendments to the dispute resolution arrangements nor the categorisation of all transmission services as prescribed services.

As the dispute resolution arrangements have never been invoked, the shortfalls of the process and therefore the exact reason for its under-utilisation are unknown. This suggests that any changes to the framework may be premature and may not increase the usage of the process or result in better connection negotiations. However, this decision should be informed by parties who would access the dispute resolution process. If they provide the AEMC with sufficient evidence that barriers do exist and that these amendments would enable greater utilisation of the dispute resolution process then South Australia would not object to changes being made, providing the benefits of the changes outweigh any costs.

South Australia considers the option to re-categorise all connection-related services as prescribed services would involve the greatest change to current arrangements and it is not evident that amendments to this extent are required at this point.

South Australia supports the AEMC proposal to separate the two parts of the extension service. The separation of the construction of an asset and the subsequent ownership, operation and control of an extension should be allowed to enable a different classification, and form of regulation, to apply to each service. Contestability for the construction of an asset should be supported, as occurs in the distribution network in South Australia. However, we note that an important component of this process is the setting of the design specifications by the owner of the network on which the asset is being constructed. So while any third party may construct the asset, it must meet these design specifications. Clear timeframes must be provided in the NER so that a network owner provides the design specifications in a reasonable time to ensure the connecting party can obtain offers for construction from third parties. Further, to ensure the design specifications aren't set at too higher standard, the network owner's specifications may require regulator approval or a process to handle disputes between the network owner and parties

who are required to meet the design specifications. The ownership, operation and control of an extension should remain the responsibility of registered TNSPs.

With patterns of generation investment changing, and generators locating further from the existing shared network and around common locations, South Australia supports allowing third party access to network extensions. As stated in our submission to the AEMC's Directions Paper, South Australia has experienced a significant increase in wind farm construction since the middle of the last decade. The vast majority of these generators have located in the south-east and mid-north regions of the state. Further extensions of the network to connect generators may not be efficient if existing extension lines are already present in these areas. We therefore consider that relevant amendments to the NER should be made to confirm that third party access to extensions is allowed.

Further, the NER would benefit from greater clarity regarding the rights of incumbent generators in these situations. Firstly, in respect of any capital contributions they have made towards the cost of the extension, South Australia considers a reimbursement scheme could be introduced to repay the incumbent generators. Secondly, as the existing generator may face greater constraints following the connection of the new generator to the extension, we believe they should be able to receive some form of compensation if third party access is allowed. Alternatively, the new generator may be required to fund the necessary amendments to the extension to ensure their access does not constrain the incumbent generator. South Australia encourages further investigation by the AEMC on these issues if third party access to extensions is permitted.

Should you have any questions in relation to this submission, please contact me on (08) 8204 1715.

Yours Sincerely

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