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Submission to the Converting the Integrated System Plan into Action: Draft Rule

AGL Energy Limited (AGL) is one of Australia's leading integrated energy companies and the largest ASX listed owner, operator, and developer of renewable generation. Our diverse power generation portfolio includes base, peaking and intermediate generation plants, spread across traditional thermal generation as well as renewable sources. AGL is also a significant retailer of energy and provides energy solutions to over 3.7 million customers in New South Wales, Victoria, Queensland, Western Australia, and South Australia. In addition, we continue to be an aggregator and developer of Demand Response and Distributed Energy Resource solutions including the deployment of Virtual Power Plants.

AGL appreciates the opportunity to comment on the Energy Security Board's (**ESB**) Draft Rule to Converting the Integrated System Plan (**ISP**) into Action (**Draft Rule**). We understand the purpose of this Draft Rule consultation document is to outline the proposed amendments to the National Electricity Rules (**NER**) to give effect to the ISP and its supporting regulatory processes, including two mandatory Guidelines¹.

AGL is broadly supportive of a number of the key recommended draft rules, including the legislative basis to implementation the ISP, the overarching governance framework, including Guidelines, ISP identification, power system needs criteria and report publication obligations, and the proposed stakeholder engagement process. There are, however, a range of issues in the Draft Rule which we believe require further consideration or clarification, including a few that AGL raised in our response to the Consultation Paper². We encourage the ESB to review these issues, set out below, prior to publication of the final ISP rule.

- **Definition of 'Actionable ISP Project'** – AGL understands these projects are those that address an identified need and comprise part of an 'optimal development path'. While AGL agrees that these conditions form part of a suitable test criteria, we note that there is no assigned expiry date which determines when an Actionable ISP Project ceases to remain 'actionable'. Therefore, under the proposed Draft Rule, any project that is identified by an ISP final report, could in theory, remain an Actionable ISP Project in perpetuity, irrespective of future power system requirements.

¹ This refers to the two mandatory Guidelines to be developed and enforced by the Australian Energy Regulator (AER), namely the Cost Benefit Analysis guideline and the Forecasting Best Practice guideline.

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<http://www.coagenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/AGL%20Response%20to%20Consultation%20Paper%20on%20Actionable%20ISP.pdf>

AGL recommends distinguishing between proposed priority and longer-term projects. Only those projects that are identified as clearly requiring investigation (and potential action pending a Regulatory Investment Test for Transmission (RIT-T)) within the intervening two-year period between ISP final reports should be labelled as an 'Actionable ISP Project'.

We believe that all other possible projects with a medium or longer time horizon are likely to be speculative and therefore subject to the changing needs of the power system. While these projects may be recognised as potentially necessary in an ISP report, they should not be afforded access to the ISP framework (and streamlined RIT-T regime) until they are evidenced by AEMO as immediate, cost efficient and necessary. We encourage the ESB and AEMO to review this defined term to ensure it is fit for purpose. AGL accepts that a possible longer-term project may become a priority project in a subsequent ISP report, and at that stage it would be suitable to reclassify it as an Actionable ISP Project.

- **Public Policy** – We welcome the ESBs position to limit AEMO's ability to only incorporate public policy commitments where a clear articulation of its impact on the power system and robust implementation arrangements by Government are published. However, to ensure that the power systems needs are adequately considered, and the most credible optimal development path is selected, AGL believes this public policy assessment would be more beneficial as a two-way loop.

AGL suggests a formal advisory obligation be placed on AEMO to provide regular updates to Governments on forecasted operational changes in the NEM. This could include changing market trends, operational system needs and other technical energy system updates that may alter public policy decision making and optimal development path section. Implementing this requirement will ensure that the ISP and public policy development cycles remain closely aligned, informed by each other.

- **Updates to the ISP** – AGL notes that the Draft Rules provides AEMO with full discretion on whether to issue an updated ISP, where new information materially alters the outcome of a "RIT-T that is either commenced or due to commence prior to the publication of the next ISP"³. While AGL supports this approach, in the instance where AEMO does not republish the ISP, this should not prevent the use of updated information in a RIT-T.

AGL also believe there is value in a short AEMO publication (for example, an infographic or factsheet etc.) to capture changes to key market inputs/trends, ISP modelling and/or optimal paths assessment. We recommend these are published at least annually between ISP final reports, or more frequently if necessary, at the discretion of AEMO. This information can alter generation investment decisions, and therefore increasing reporting transparency on these developments will

³ Energy Security Board; Converting the Integrated System Plan into Action – Consultation on Draft ISP Rule (November 2019); page 13

be important inputs into financial assessments for transmission and generation. AGL recommend the ESB and AEMO to consider how best to bring this valuable information to market.

- **Development of the Optimal Path** – While AGL is cautiously supportive of this approach, we do not support the Draft Rule to allow the path to only have a “positive net benefit for the most likely scenario”⁴ instead of the highest positive net benefit. AGL points to the purpose and objectives of the ISP, that is to identify cost efficient transmission investments that are compatible with the National Electricity Objective (NEO). We therefore believe that AEMO should be obligated to demonstrate the economic credibility of its optimal development path and to ensure that any Actionable ISP Project recommended stands up on its own merits as the best option available under the central case. Retaining the existing net benefits test in the Draft Rule would unnecessarily expose greater capital risk to consumers.

In identifying the best option under a system-wide assessment, AGL encourages AEMO to use sensitivity testing across a range of scenarios to determine whether a project could proceed with, and in the absence of, other related projects. However, once identified as an Actionable ISP Project, its RIT-T assessment should not rely on the probability (and benefits) of other related projects progressing. Doing so could increase the risk of underutilised or stranded transmission assets to the detriment of consumers.

- **Regulatory safeguards and broader governance decisions** – In the response to the Consultation Paper, AGL called for further clarity on what governance processes would exist to test and/or verify AEMO’s methodology and findings/recommendations in the final ISP report. AGL notes that this issue was also raised by stakeholders at the ESB’s public forum on 5 December 2019.

While AGL recognises that a series of stakeholder consultation feedback loops have been added to each ISP development process step, no opportunity or regulatory safeguard exists in the Draft Rules to review the decisions taken by AEMO in a final ISP document. Further, an obligation on AEMO to publish its decision and rationale in response to stakeholder feedback has not been included.

Noting the long term significance that the ISP will have on future transmission investments, AGL remains of the view that these additional levels of consumer protection and clear transparent decision making, are necessary in the ISP Framework to scrutinise and reaffirm the accuracy of the details⁵ (and proposed direction of transmission investment) presented in the final ISP report.

⁴ Energy Security Board; Converting the Integrated System Plan into Action – Consultation on Draft ISP Rule (November 2019); page 11

⁵ And the economic and financial credibility of the optimal path. While AGL acknowledges that AEMO is bound to follow the Guidelines when developing the ISP report, there may still be a revenue gap for new investments. Economic credibility could be demonstrated by publishing an expected rate of return or net present values for new builds.

In addition, AGL queries whether investment decisions made under the ISP Framework, would meet the NEO, noting that public policy on key issues such as emissions policy is not covered by the NEO. Therefore, this may limit the degree and pace at which the energy market can transition under the ISP. We encourage the ESB to determine if there is a risk, and if so, how best to align the NEO and the ISP Framework to ensure that the NEM continues its progress towards a decentralised market underpinned by clean technology.

AGL supports the creation of an independent ISP Panel (the Panel) to advise AEMO in the preparation of ISP documents. We encourage the ESB and the AER to provide further clarity in the AER Guidelines on key governance and membership details associated with its creation, including number of panellists, responsibilities, and length of appointment. In our view, the panel should be run under similar terms to the Reliability Panel, and membership of this group should comprise a range of industry, government, consumer representatives, and the AER.

With respect to the role of the Panel, AGL suggests two broader functions are necessary:

1. its 'advisory services' role under the Draft Rule should be expanded to a 'peer review function with recommendations'. It should report to AEMO on the draft and final ISP reports and AEMO should publish these recommendations and AEMO's response on its website to maintain clear transparency and decision-making; and
 2. the Panel should provide a report to the AER following each deliverable above on whether it believes AEMO and the draft/final ISP report remained consistent with the AER Guidelines.
- **Timely Review of the ISP Framework** - AGL recommends that a broader governance review of the ISP Framework be included in the final ISP Rules to examine if the role, objectives and governance framework have delivered against their intent. We note that other major energy reforms, such as the Power of Choice, have been subject to reviews 3-5 years post implementation.

AGL expects that the ISP framework and associated streamlined RIT-T process will deliver significant transmission investment across the NEM. Building at speed will be beneficial as the energy market continues to transition, however an emphasis on capital efficiency, revenue adequacy and consumer risk must not be lost.

- **Role of the AER** – Under the Draft Rules, AGL understands that the primary role of the AER with respect to the ISP framework is the development and enforcement of the Guidelines. Specifically, it will set out the process and technical steps for AEMO and Transmission Network Service Providers to following when developing the ISP report and RIT-T. However, outside of these procedural activities, the AER does not appear to have an economic regulatory function.

We do not support this draft decision and believe that this will increase the risk to consumers from unsatisfactory transmission investments. While we agree that AEMO is a technical expert with respect to the planning, development and operation of the NEM, it is not an economic regulator. The AER was specifically established as an independent authority at arm's length from the market operator with the appropriate economic expertise, skills, and resources to suitably assess the rigour of long-term transmission investment decisions. In line with this market design, AGL strongly believes that the AER should have a larger role in assessing project selection during the ISP development process. We agree, if correctly done, no role for the AER in assessing streamlined ISP RIT-T's is necessary.

AGL suggests the AER be required to assess (but not necessarily approve) ISP project selection (i.e. those projects with Actionable ISP Project status) at the Draft ISP stage. This will:

- provide a suitable level of economic rigour to the optimal development plan whilst allowing AEMO sufficient time to amend (if and as necessary) its modelling; and
 - minimise both consumer investment risks and stakeholder concerns about the removal of the AER post RIT-T approval obligation.
- **Disputes Resolution mechanism** – the Draft Report states that AGL was supportive of the ESB's decision to limit disputes to matters of process⁶. However, this was not our view.

In our response to the Consultation Paper, we stated the proposed ISP disputes resolution process was unworkable because it would only permit procedural disputes to be raised and resolved in practice. We therefore recommended the ESB review its proposal to ensure that a fair, equitable and fit for purpose regime was developed that allowed stakeholders to raise significant issues of substance related to, for example the ISP methodology, calculations or project selection.

AGL welcomes the ESB's reassurance that a proper consultative process will be managed at each stage of the ISP development process. AGL agrees that this will resolve many of the issues that could be raised by stakeholders and therefore minimise use of the ISP disputes resolution process. However, we believe this will only occur if there is a mandatory and transparent feedback loop, with AEMO responses to issues raised published on its website.

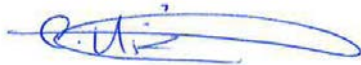
Notwithstanding, a disputes resolution mechanism to address procedural and technical matters of substance is necessary. Per our suggestion to the Consultation Paper, we believe that the ESB should consider limiting access to Industry Associations or disputes with support from multiple industry stakeholders. This will provide industry with comfort that a formal disputes path exists, but also ensures the mechanism cannot be abused or used to unnecessarily derail an ISP process.

⁶ Energy Security Board; Converting the Integrated System Plan into Action – Consultation on Draft ISP Rule (November 2019); page 13

Where AEMO receives a legitimate dispute, it should consult with industry and publish a statement on its website justifying its final position. A similar process could then be implemented by the AER under its escalated disputes resolution mechanism.

If you have any queries about this submission, please contact Dan Mascarenhas on (03) 8633 7880 or DMascare@agl.com.au.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Dan Mascarenhas', with a long horizontal flourish extending to the right.

Con Hristodoulidis

A/g General Manager Energy Markets Regulation