



17 January 2019

The Chairman
Energy Security Board
C/- CoAG Energy Council

Sent by: email to info@esb.org.au

Converting the Integrated System Plan into Action Response to Draft Decision

The Major Energy Users Inc (MEU) welcomes the opportunity to provide its views on the Energy Security Board (ESB) draft decision on converting the Integrated System Plan (ISP) into action. The MEU has been a consistent respondent to the various ESB consultations since its inception on this and other topics.

The MEU and its regional affiliates have been advocating in the interests of energy consumer for over 20 years and it has a high recognition as providing informed comment on energy issues from a consumer viewpoint with various regulators (ACCC, AEMO, AEMC, AER and regional regulators) and with governments.

While the MEU has a number of concerns about the draft decision, it has five over-riding concerns – there is a need for better checks and controls within the ISP process.

1. AEMO is not independent

The proposed approach places a massive reliance on AEMO and its processes. Despite concerns raised in responses to the consultation paper about AEMO, the ESB responded that it considers AEMO, being financially independent, will address the responsibilities placed on it in a manner that will serve the long-term interests of consumers.

The MEU is very concerned about this assessment made by the ESB, in that while the MEU accepts that AEMO is not a financial beneficiary of network augmentation, it should be considered to have an active and positive interest in augmenting the transmission network as AEMO:

8 Harker Street, Healesville, Victoria, 3777

ABN 71 278 859 567

www.meu.asn.au

- J Is the TNSP for Victoria and so has a vested interest in ensuring adequate investment is made in the Victorian transmission network to achieve the reliability of supply it considers is needed. Being the TNSP for Victoria places the AEMO activities central to the needs for SA, NSW and Tasmania which all have connections to the Victorian transmission network (ie Victoria is central to the operations in four of the five regions of the NEM)
- J As the operator of the electricity market, it has an incentive to make the operation of the market as easy for AEMO staff as possible, to minimise loss of supply that impinges on its reputation and to minimise the number of credible contingencies faced by its operations staff
- J Has openly expressed views that despite the significant additional costs that will be incurred by consumers and that the amounts of unserved energy (USE) in each region are consistently well below the Reliability Standard, the
 - o market needs increased reserves of generation in order to achieve a higher reliability of supply than is currently provided,
 - o the transmission network needs to be significantly expanded in order for it to provide the reliability of supply AEMO considers is needed
 - o the Reliability Standard needs to be changed so there is less risk of a loss of supply than currently applies¹.

2. AEMO is overly conservative

In addition to its concerns about its true independence, the MEU reiterates the concerns it has made to AEMO and others about the excessive conservatism that applies to AEMO forecasting such that massive but unnecessary investments have been made in networks in the past based on AEMO conservative forecasts. This conservatism continues, highlighting the risk for consumers that more unnecessary investments might be made.

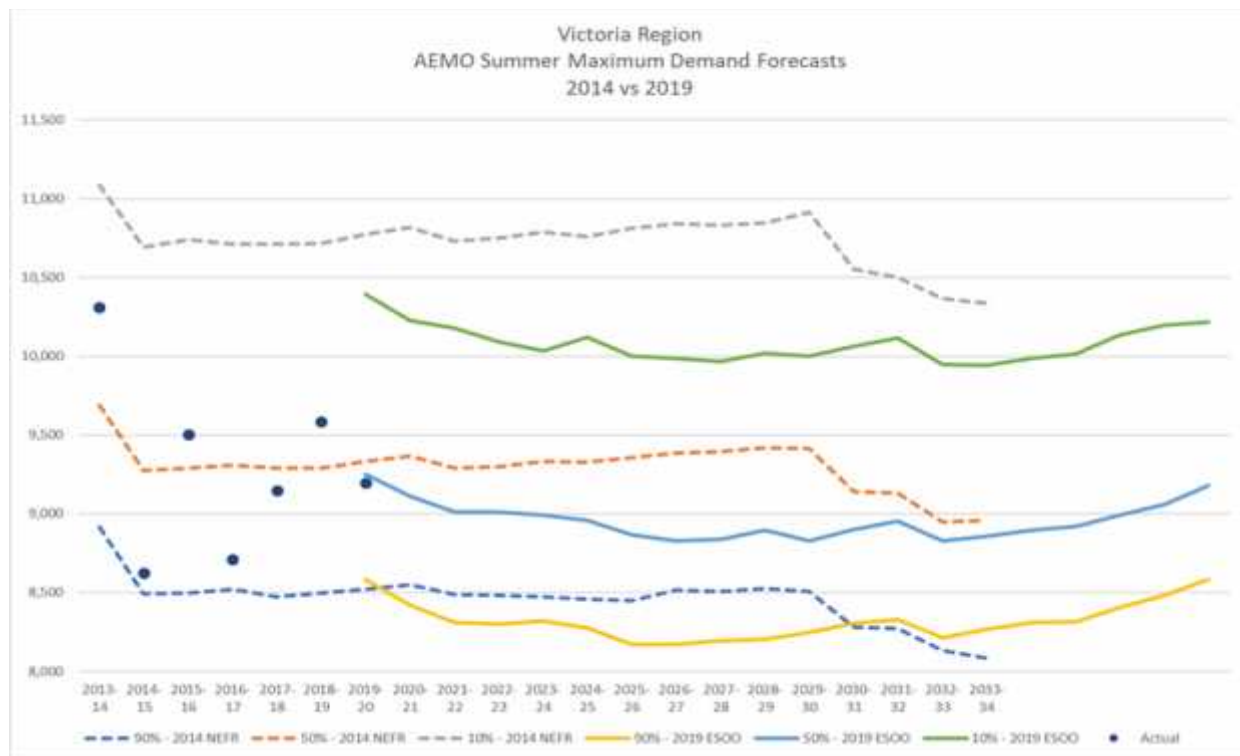
It is with this major concern that the MEU considers that the changes proposed for the planning and implementation of transmission investment under the ISP need to reflect these realities.

The MEU considers that the apparent urgency to build new transmission assets is being used to over-ride the inherent constraints that are built into the current controls that are there to ensure that the long-term interests of consumers are being achieved. If there had been a similar urgency (as is implied by the ISP draft decision) in (say)

¹ The MEU points out that most of the losses in supply that consumers experience is not from lack of wholesale supplies but from failures in the distribution networks. An increase in wholesale supply will have a marginal impact on the overall reliability of supply but will result in considerable cost to consumers

2014 to build new transmission assets, there would have been considerable unnecessary investment that would still be unused at considerable cost to consumers.

For example, the following chart shows the AEMO data for Victoria from its 2019 ESoO superimposed on the data from the 2014 ESoO.



Source: AEMO ESoO 2014, 2019

This chart shows that an ISP generated in 2014 would have required significant augmentation of the transmission network both within Victoria and in the interconnectors it has with SA, NSW and Tasmanian regions just to maintain the Reliability Standard. Fortunately, the current RIT-T process prevented such unnecessary investment but moving to a faster process as implied by the draft decision, could have resulted in considerable harm to consumers through over-investment.

A similar outcome to that for Victoria applies to NSW and in the other regions (SA and Qld) it is not until 2030 and later that the 10PoE trace for 2014 matches the 10PoE trace for 2019. This exemplifies the MEU concern that imposing urgency will lead to over-investment

3. The need for an independent assessment of the AEMO model

The MEU highlights that the modelling carried out by AEMO and the assumptions used in its forecasting are used in the RIT-T assessments generated by all TNSPs. While

this would appear to be sensible, there has never been any ex post review² of a forecast net benefit analysis disclosed by such modelling so there are real concerns about whether modelling carried out under the ISP will in fact deliver the most efficient outcome³.

As the proposed changes detailed in the draft decision embed the AEMO ISP into the requirements for other TNSPs to use the AEMO modelling as the basis for their commitments for ISP augmentations, the MEU considers that the AEMO ISP modelling, especially for the preferred option, must undergo independent testing, preferably under the auspices of the AER.

Additionally, the ISP projects that are implemented should be subjected to an ex post review after (say) five years to test if the actual outcome reflects the modelling that was used to substantiate the project. While the MEU accepts that by this time, the investment will have been made, the ex post review will provide feedback as to whether the assumptions and key inputs used were justified. By carrying out the ex post review of the models and identifying input and assumption errors within them, this will increase the accuracy of the modelling carried out for future projects.

4. The new consultation process

The MEU considers that AEMO must implement a significantly expanded consultation program which not only addresses in detail the key inputs and assumptions used to populate the ISP model, but also include detailed consultation about the various options that have been considered. While the MEU notes that the draft decision does imply there is to be increased consultation, the MEU notes that such consultation **must be open to suggestions from stakeholders for other options as well as about key inputs**. The MEU has noticed a reticence in the past for AEMO and other TNSPs to consider that any views other than their own, have much merit or are worthy of being modelled.

The MEU notes that there is an ability for an aggrieved stakeholder to appeal an ISP decision in relation to the process used for developing the ISP. The MEU considers that appealing after the ISP has been published is likely to create delays so the MEU suggests that the rules explicitly allow for a stakeholder to appeal to the AER **during the ISP development** about concerns of the way AEMO (and other TNSPs) are developing the ISP and any subsequent PADR.

² The MEU is aware that an independent model by Frontier Economics was generated in relation to the proposed Heywood upgrade in 2013 which considered the net benefits forecast by AEMO/ElectraNet were overstated. Unfortunately, the AEMO/ElectraNet forecast net benefits for this upgrade have yet to be realised.

³ The MEU points out that once a commitment is made under a RIT-T process, the augmentation of the transmission network will be added to the Regulatory Asset Base and will remain there, even if the augmentation is later proven to be oversized or even redundant

5. The dispute process

As is stated above, past performance of AEMO has shown there have been significant flaws in its forecasting. In some cases, stakeholders have identified the causes of such flaws and questioned AEMO about them, often with little effect. The disputes process is about ensuring that AEMO does take appropriate notice of stakeholder input yet the limitations in the disputes process included in the draft decision do not address this concern.

This means that the disputes process has to be expanded so that it is clear:

-) that a dispute can be raised at any time during the ISP development
-) how the AER addresses the instance where a stakeholder(s) is of the view that AEMO has not appropriately considered the views of stakeholders during the consultation process⁴? The draft decision states that an appeal can only be about “process” yet if the consultation process is not followed as is intended, the outturn ISP will not reflect the purpose of the consultation that is required by the draft decision⁵.
-) what is the remedy should the AER decide that AEMO has not followed the processes required under the best practice guidelines (cost benefit analysis and forecasting)?

The MEU considers that if there is an instance where stakeholders consider that AEMO has erred, and the AER agrees on the basis of the independent modelling the MEU considers is essential, then AEMO should be required to correct its modelling by implementing an appropriate change to its assumption, even if this delays augmentation of the network.

Other Concerns

There are other concerns the MEU has about the draft decision.

-) The MEU observes that there is a distinct disconnect between the market benefits test used in the RIT-T as the basis for the ISP, the impact of loss of supply (as measured by the amount of unserved energy), credible contingent loss of supply possibilities and the price consumers pay for transmission network services. This trade off – between energy not supplied and price – does not seem to be reflected in the ISP draft rules and the draft decision seems to imply that urgency for new augmentations is paramount delivering increased reliability of supply⁶ regardless of cost.

⁴ The MEU points out that consultation can range from being mere “window dressing” where the entity purports to consult but ignores any input, to where the entity properly incorporates the input provided

⁵ For example, if AEMO decides to input an incorrect assumption into its model but has followed the due “process” in that it has “consulted”, stakeholders will not be able to appeal the issue and so prevent an inappropriate outcome.

⁶ ie a reduction in the Reliability Standard

Because of the very high prices consumers are now having to pay for their electricity supplies, there is a growing view amongst consumers that the current (even a reduced) reliability of supply is preferable to further increases in prices. The MEU considers that the ESB needs to moderate its desire for urgency and time minimisation to reflect this consumer view.

-) The draft decision reflects a two-year timeframe between ISP reviews. While the MEU recognises that the increased consultation and testing for the ISP would reasonably require two years between editions, the MEU recognises that the electricity market is becoming more dynamic with the rate of change being seen (eg building of new network scale generation and storage occurs faster than 2 years and behind the meter generation and storage occurs even faster).

The draft decision does envisage that AEMO might be required to issue updates to a current ISP before the next one is due, but it is not clear that if an update is issued, whether the update will be subject to the same requirements as apply to the scheduled ISP activities. The MEU considers that an update should be required to follow the same process controls, consultation and checks as scheduled ISP development.

-) Once the ISP is issued, other TNSPs must address the augmentation proposed by the ISP and use the preferred ISP option as at least one of the options considered by the TNSP to achieve the desired outcome. The MEU points out that there is no requirement on the TNSP to seek stakeholder input to any of the other options that the TNSP might examine in addition to the ISP preferred option as part of the further development of the augmentation.

As the Project Specification Consultation Report (PSCR) process is now removed from the TNSP for an ISP project, the MEU considers that the TNSP must seek consumer input to selection of any other option that is to be considered in the development of the Project Assessment Draft Report (PADR) process. To rely on stakeholder input after the PADR is released does not allow for the proper investigation and assessment of options other than that developed by AEMO in the ISP process or by the TNSP involved.

-) The MEU is very concerned that the draft rules assume that the 2020 ISP will be deemed to comply with the ISP rules even though the consultation to date for the 2020 ISP has not benefited from the requirements for increased stakeholder involvement or from the consumer advisory panel proposed.

The 2020 ISP proposes some extensive transmission network augmentations, which will result in a massive step increase to the overall transmission Regulated Asset Base by over 20% adding many hundreds of millions of dollars to the annual electricity charges; this at a time when consumers are already paying excessive prices for their electricity.

Because of this massive increase in costs to consumers, the MEU is very concerned that the 2020 ISP might include augmentation of the transmission network that is not justified.

J) The MEU observes that the RIT-T process reflects a market benefits test, yet the draft decision implies that the ISP is intended to provide the best outcome that is in the long-term interests of consumers⁷. The MEU points out that the draft decision imposes a number of elements that might militate against the long-term interest of consumers. For example

- AEMO is given the unilateral flexibility to select as the preferred option, a project that does not deliver the maximum net benefit. The MEU notes above that there should be independent modelling carried out to test the preferred option but if the preferred option is not the option delivering the highest net benefit, then the project options discarded should also be independently tested to support any decision to exclude it
- There needs to be clarity about what generation and other augmentations AEMO is to include in the key inputs for its model. Currently AEMO has flexibility as to what it will assume will be in operation for the majority of the life of the proposed augmentation and when other augmentations (generation and network) will be implemented.
- There is concern that there is an opportunity for double counting of network benefits.

For example, the QNI upgrade, the VNI upgrade HumeLink, EnergyConnect and VNI West might each individually contribute a net market benefit when assessed in isolation. Yet each of the projects might be claiming the same benefits that would otherwise be delivered by one or more of the other projects.

The ISP must assess as a separate activity the combined net benefit of all projects that are included in priority (group 1) projects and near term (group 2) projects to ensure that there is no double counting. As part of this assessment, the deletion of one or more of the projects should be included to test if the inclusion (or deletion) provides an increase in the net benefit

- The draft decision highlights that AEMO is to establish an “ISP Panel” to advise AEMO on ISP issues, the MEU points out that such a panel needs to be structured so that it can provide “fearless” advice and is not constrained by actions of AEMO. The MEU considers that this panel

⁷ The MEU is not aware where it has been proven that a market benefit test is the equivalent to a benefit test which would more in the long-term interests of consumers are required by which is implied by the NEO. The MEU notes a market benefits test allows for the transfer of wealth from consumers to generators – it is not clear that such a transfer of wealth would be in the long-term interests of consumers

and/or members need to be able to appeal to the AER on process issues during the ISP development rather than wait until the ISP report is delivered.

-) While the draft decision highlights that AEMO is to institute an “ISP Panel” of stakeholders, there is no clarity on how the panel members will be selected so that it not only has the ability to provide a meaningful contribution to the process but that its membership will provide critical input to AEMO deliberations for the ISP development
-) It is not clear to the MEU how the process of inclusion of contingent projects is to be addressed. Under the current arrangements a TNSP includes a contingent project in its 5-year determination process. A contingent project must be identified in the TNSP’s application and the triggers for its inclusion in the allowance identified. Under the draft decision, it would seem that if AEMO identifies a new project in the ISP, then this project would automatically be an approved project even if the TNSP had not previously included it as a contingent project during the reset process
-) While the MEU notes that the draft decision excludes commentary on cost allocation⁸, the MEU points out that the Regulatory Investment Test is a market benefits based test rather than a consumer benefits based test even though it will be consumers that will pay for regulated augmentations added to the Asset Bases of the TNSPs. Specifically, any transfer of wealth from consumers to generators that results from an augmentation is excluded from any assessment. The MEU is very concerned that any ISP augmentation will become a direct cost to consumers even where the benefits accrue to generators.

Summary of MEU position

While the MEU is generally supportive of the concept behind the draft decision, it is very concerned that the draft rules proposed by the ESB will result a reduction in the controls inherent in the current RIT-T requirements to ensure that any investment in the shared network delivers the optimum net benefits for the long-term interests of consumers.

The MEU is concerned that, to reflect the urgency of transmission network augmentations, there is now too much flexibility for and reduction of controls on AEMO in the draft rules and that the past performance by AEMO and other TNSPs in augmenting the transmission network has resulted in inefficient investment leading to economic loss for consumers.

Specifically, the MEU is very concerned that the demonstrated conservatism in AEMO forecasts coupled to its stated desire for more generation and transmission network to be provided can result in a transmission network that is oversized for the needs. To

⁸ Pointing out that this is being addressed in part under the AEMC CoGaTI process

overcome this, the MEU suggests that there be implemented a number of improvements to the draft ISP rules including:

-) Greater cognisance needs to be given to the increasing consumer view that they would prefer lower prices rather than increased reliability of supply
-) Independent assessment of modelling used to substantiate an augmentation
-) Vastly improved consultation with stakeholders and specifically consumers
-) The explicit ability for stakeholders to commence an appeal process during the ISP development process
-) The disputes process needs to be clarified
-) The 2020 ISP should not be deemed to comply with the new rules
-) The flexibility allowed for assessing assumptions and key inputs used in the modelling needs to be constrained through the improved consultation process that is being implemented
-) The ISP analysis must include modelling of the multiple projects being proposed to ensure there is duplication of the benefits claimed by different projects

The MEU is happy to discuss the issues further with you if needed or if you feel that any expansion on the above comments is necessary. If so, please contact the undersigned at davidheadberry@bigpond.com or (03) 5962 3225

Yours faithfully



David Headberry
Public Officer