



APA submission

NSW Electricity Roadmap

Part 5 Network Infrastructure Paper

November 2021



Mr James Hay
Deputy Secretary, Energy, Climate Change and Sustainability
NSW Department of Planning, Industry and Environment

Lodged online

15 November 2021

RE: APA Submission to the Network Infrastructure (Part 5) Policy Paper

Dear Mr Hay,

Thank you for the opportunity to comment on the Network Infrastructure Projects (Part 5 of the Electricity Infrastructure Investment Act) Policy Paper (Policy Paper). We appreciate the NSW Government's ongoing engagement in relation to the design of its Electricity Infrastructure Roadmap (the Roadmap).

APA is an ASX listed owner, operator, and developer of energy infrastructure assets across Australia. Through a diverse portfolio of assets, we provide energy to customers in every state and territory on mainland Australia. As well as an extensive network of natural gas pipelines, we own or have interests in gas storage and generation facilities, electricity transmission networks, and over \$750 million in renewable generation.

We support the NSW Government's Roadmap and are actively involved in the energy transition taking place across Australia. We have recent experience developing and connecting renewable generation assets to the national electricity grid. Our ownership and operation of electricity transmission assets means we support the introduction of contestability and are well placed to help facilitate the timely development of network infrastructure within renewable energy zones (REZs).

Our submission below provides views on the issues raised in the Policy Paper, including the importance of regulatory certainty in driving the most efficient outcomes for NSW consumers.

If you wish to discuss our submission in further detail, please contact John Skinner on [REDACTED]

Regards,



Peter Bolding
General Manager
Economic Regulation & Policy

1 Executive Summary

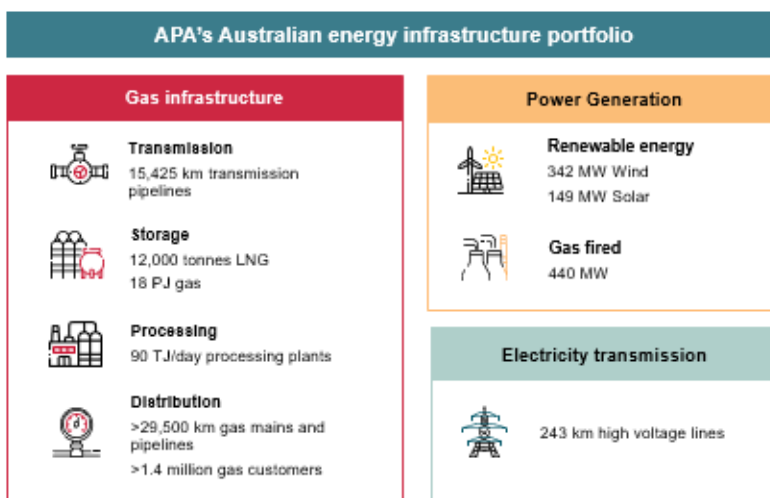
Key points

- Contestability in the provision of network infrastructure will help improve the timeliness and efficiency of investment.
- Consumer interests will be protected if REZ network infrastructure projects are delivered by qualified service providers with strong balance sheets and a track record of delivering large scale linear energy infrastructure projects.
- Where a contestable process has been undertaken to determine the cost of undertaking a project, the Regulator should be required to accept those costs as being prudent and efficient by virtue of having been identified through a competitive process.
- Providing the Regulator with the ability to conduct a building block assessment of network operator costs increases regulatory uncertainty and will result in bids higher than would otherwise be the case. This reduces the likelihood of competitive processes revealing efficient costs.

APA is a leading Australian Securities Exchange (ASX) listed energy infrastructure business. Consistent with our purpose to strengthen communities through responsible energy, our diverse portfolio of energy infrastructure delivers energy to customers in every state and territory on mainland Australia.

Our 15,000 kilometres of natural gas pipelines connect sources of supply and markets across mainland Australia. We operate and maintain networks connecting 1.4 million Australian homes and businesses to the benefits of natural gas. And we own or have interests in gas storage facilities, gas-fired power stations.

Our investments include over \$750 million in renewable generation, making APA the 8th largest renewables investor in Australia. Our high voltage electricity transmission connects Victoria with South Australia and New South Wales with Queensland.



APA is supporting the transition to a lower carbon future. Our ambition is to achieve net zero operations emissions by 2050. Through our Pathfinder Program, we are investigating how hydrogen and other technologies such as batteries and microgrids, can support a lower carbon future.

We support the NSW Government's Electricity Infrastructure Roadmap. With the retirement of aging coal power stations over the next 15 years we recognise the importance of the Roadmap in supporting investment in energy infrastructure and enhancing energy security and reliability in NSW. With an intended network capacity of 12 gigawatts across five REZs, the timely delivery of new transmission infrastructure is essential to ensure the new generation capacity can be connected to customers.

APA has significant, first-hand experience planning, constructing, and operating linear infrastructure and renewable energy generation. We support contestability in the provision of network infrastructure. Competition helps drive innovation, improved service delivery, and better outcomes for customers.

Importantly, where a contestable process has been undertaken to determine the cost of undertaking a project, the Regulator should be required to accept those costs as being prudent and efficient by virtue of having been identified through a competitive process.

Our submission to the Policy Paper is structured as follows:

- PART A contains the key issues we wish to raise in response to the Policy Paper
- PART B contains answers to the questions for stakeholders.

2 PART A – Key issues

2.1 Contestability driving efficient outcomes

Concerns about the timely delivery of key electricity transmission infrastructure have been well ventilated. Introducing contestability will enable businesses like APA to leverage their financial strength and expertise to help deliver the infrastructure necessary within the NSW REZs.

APA welcomes the possibility of competition to help drive efficient outcomes for NSW consumers.¹ Businesses like APA wish to invest in long term energy projects that support the transition to net zero.

Contestability is the best way that governments can choose to promote the timely delivery of transmission infrastructure and attract the lowest cost of capital to projects. While the price at which projects are offered is an important consideration, the lowest cost projects may in fact have the highest risk of delivery. This is because the low-cost projects may make unrealistic assumptions and be more susceptible to factors such as construction delays.

For the necessary investment to be forthcoming, rates of return must compensate for the risks involved. The fact that TransGrid was unable to fund the NSW-SA interconnector without support from the Clean Energy Finance Corporation demonstrates that there may be issues with the way greenfield projects are funded.

2.2 Eligibility criteria to carry out a REZ network infrastructure project

The Policy Paper is seeking views on the eligibility criteria that should apply to carry out a REZ infrastructure project.

We understand that even though a network operator other than TransGrid can develop, build, own and finance new network infrastructure, responsibility for transmission system operation will remain with TransGrid as the primary Transmission Network Service Provider (TNSP) in NSW.

In its recent rule change proposal, TransGrid raised concerns about its ability to finance the NSW-SA interconnector under national regulatory settings.² Although the AEMC did not approve TransGrid's rule change request, there are significant issues in relation to the funding of major transmission projects by incumbents.

In our view, consumer interests will be protected if network infrastructure projects delivered as part of the Roadmap are offered by qualified infrastructure owner and operators with strong balance sheets and a track record of delivering large scale energy infrastructure projects.

¹ NSW Government, *Network Infrastructure Policy Paper*, October 2021, pvi

² AEMC, *Participant Derogation – Financability of ISP Projects (TransGrid) rule change*, April 2021

There are obvious advantages with this approach:

- There is strong competition for participation by both equity and debt providers in large scale energy infrastructure projects. These proponents understand that successful on time delivery of projects is a fundamental precursor for the long-term success of their investment.
- Projects are more likely to be delivered in a timely fashion and operated prudently if proponents have recent experience delivering large scale linear infrastructure.

In our view, the NSW Government should consider the sort of eligibility criteria that would be used to assess a distribution or transmission licence under Schedule 2 of the *Electricity Supply Act*. That is, prospective network owners should be required to satisfy:

- **Technical criteria** – bid proponents should have relevant experience constructing, owning, maintaining, and operating electricity infrastructure
- **Prudential criteria** – bid proponents should have a suitable credit rating and be required to demonstrate their ability to access capital

The importance of getting the eligibility criteria right is demonstrated through Central Ranges Gas Network tender process which is presented in the Policy Paper as a model that could be used within the NSW Roadmap framework.³

In 2003, the successful tender to supply gas to the Central Ranges region of NSW was made by the Europacific Consortium, which consisted of Europacific Corporate Advisory, Country Energy, Colonial First State and Jasdell.⁴ The Central Ranges Pipeline and Central Ranges Gas Network were constructed in 2006, and the competitive tender process undertaken in 2003 was used to determine the reference tariffs which would apply on the pipelines.

Unfortunately, the consortium encountered financial difficulties and APA subsequently purchased both the Central Ranges Pipeline and Central Ranges Gas Network in 2008.

The Central Ranges process demonstrates the importance of eligibility criteria that ensure experienced infrastructure providers deliver the necessary infrastructure in the NSW REZs. Failure to attract the right parties could have severe consequences for the timely delivery of REZ infrastructure in NSW.

³ NSW Government, *Network Infrastructure Policy Paper*, October 2021, p30

⁴ ACCC / IPART Joint Media Release, Final Decision Media Release, 8 December 2005

2.3 Transmission efficiency test and the Regulator's determination

As the Policy Paper points out, the enactment of the *Electricity Infrastructure Investment Act 2020* (the EII Act) provides the opportunity to consider which elements of the national framework should apply to network infrastructure projects constructed as part of the Roadmap.⁵

APA operates in many contestable markets and frequently participates in competitive tender processes. These processes help drive innovation, improved service delivery, and better outcomes for customers. Any tariffs set through the tender process therefore reflect the competitive tension arising from the tender process and are the product of a competitive market.

For these reasons, we agree with the view set out in the policy paper that where a contestable process has been undertaken to determine the market price of undertaking a project, that the Regulator should be required to accept those costs as being prudent and efficient by virtue of having been identified through a competitive process.⁶

It is important to recognise that many factors influence the price point at which bids are submitted, including a proponent's valuation of risk, and assumptions regarding the scope for future load growth and contract renewal. This is where the risk of future regulation becomes relevant, as regulatory uncertainty will affect the price at which capital can be sourced (the cost of capital) which is ultimately factored into the final price of any competitive bid.

To ensure that the Roadmap achieves the objective of delivering network infrastructure as efficiently as possible, the NSW regulations should stipulate that the role of the Regulator is to ensure that the market price put forward by the network operator is consistent with those in the successful bid for the planned life of the asset.

This approach has several advantages:

- Greater certainty for consumers given that the outcome of a competitive process drives long term revenues.
- Tender processes with long term revenue certainty will generate the most competitive price outcomes.
- There will be significantly less regulatory burden for all parties involved, given that the Regulator will not be undertaking a full building block assessment for transmission infrastructure constructed under the NSW Roadmap.

⁵ NSW Government, *Network Infrastructure Policy Paper*, October 2021, p29

⁶ NSW Government, *Network Infrastructure Policy Paper*, October 2021, p33

- Revenues and obligations will initially be established via contractual arrangements, with the Regulator ensuring only contractual amounts are charged.

Providing the Regulator with the ability to conduct a building block assessment of network operator costs is inconsistent with many of the NSW Government's objectives under the NSW Roadmap:

- Competitive tender processes will be undermined and regulatory risk for investors will increase. This will result in bids higher than would otherwise be the case and reduces the likelihood of competitive processes revealing efficient costs.
- There will be greater uncertainty for consumers and investors.
- Regulatory burden on all parties increases given the effort involved in undertaking a full building block assessment.

There may be circumstances in which the Regulator should undertake a building block assessment of proposed costs (for example, if a competitive process was not utilised to determine efficient costs). In this situation, we agree that Regulator scrutiny of costs will help provide customers with confidence that they are not paying too much for their energy supply.

2.4 Preparatory activities

APA has a strong track record of delivering large linear infrastructure projects. We generally plan and deliver the assets we own and operate, and currently have more than \$1.5 billion of investments under development.

Our experienced, in-house team has the following capabilities:

- Land access, easement corridor acquisition and maintenance and environmental approvals
- Landholder, community and stakeholder engagement
- Cultural heritage and native title
- Local, state and federal government liaison
- Project management, scheduling and project timeline determination

Under the EII Act, the Infrastructure Planner, rather than a network operator, will conduct preparatory activities and development works for REZ network infrastructure projects.⁷ While this approach may be appropriate in circumstances where time does not permit the outsourcing of these functions, it may not leverage the significant

⁷ NSW Government, *Network Infrastructure Policy Paper*, October 2021, p17; EII Act s. 63

expertise that exists within proponents like APA. We therefore support EnergyCo, as Infrastructure Planner, including these aspects within the scope of the bid tender when appropriate. This will help drive innovation and better service delivery.

When preparatory activities are undertaken by EnergyCo, the NSW Government intends that the cost of conducting the preparatory activities and development works will be recovered from the network operator selected to carry out the REZ network infrastructure project.⁸ APA is comfortable with this arrangement, provided it is known at the time of bidding for a network project.

2.5 Incentives to drive the timely delivery of infrastructure

The regulatory framework for electricity networks contains a number of incentive schemes that are designed to improve the efficiency or service performance of networks. For example:

- The Service Target Performance Incentive Scheme (STPIS) is designed to provide incentives for the service provider to maintain and improve its reliability (as measured by customer outages) and service performance (measured through call centre telephone answering metrics).
- The Efficiency Benefits Sharing Scheme (EBSS) and Capital Expenditure Sharing Scheme (CESS) are designed to incentivise a service provider to improve its operating and capital expenditure efficiency. Any efficiency gains are ultimately shared with customers.

These incentive schemes exist because electricity distribution and transmission networks are natural monopolies. One of the objectives of the regulatory frameworks, including the incentive schemes, is to replicate the workings of a competitive market and place those competitive pressures on service providers.

If network infrastructure is being provided through a competitive tender process, by firms operating in a competitive market, it is not clear why formal incentive schemes are needed. Market forces will ensure that bids are competitive and that network services are delivered as efficiently as possible into the future.

If the NSW Government wishes to ensure that network infrastructure projects are delivered on a timely basis and generators are connected as quickly as possible, we support performance levels being established within the terms and conditions of the resulting contract, rather than through a formal incentive scheme.

⁸ NSW Government, *Network Infrastructure Policy Paper*, October 2021, p18

3 PART B – Responses to questions for stakeholders

Number	Question	Response
1	Do you agree with the proposed guiding principles? Are there additional principles that should be considered?	<p>Yes, we agree with the proposed guiding principles. However, we consider that an additional principle, enhance competition should be included to reflect the increased efficiency that will result from the introduction of contestability:</p> <ul style="list-style-type: none"> • Timely implementation • Maintain existing roles in reliability and system security • Consumer interests • Address key risks and barriers to network investment • Legislative consistency • Facilitate appropriate cost and risk sharing arrangements • Regulatory efficiency • Enhance competition
2	What are your views on the proposed approach to defining classes of network infrastructure?	Yes, we agree with the proposed classes of network infrastructure as they are based on well understood descriptions from the national framework:
3	Are there any risks to the effective delivery of a REZ if the necessary system strength services are not included as a class of network asset under the EII Act?	No response.
4	Does the proposed method appropriately balance the transparency of costs recovered through the Scheme Financial Vehicle against the certainty needed to conduct preparatory activities and development works to deliver timely REZs?	<p>See section 2.4 of this submission.</p> <p>When preparatory activities are undertaken by EnergyCo, the NSW Government intends that the cost of conducting the preparatory activities and development works will be recovered from the network operator selected to carry out the REZ network infrastructure project. APA is comfortable with this arrangement, provided it is known at the time of bidding for a network project.</p>
5	What information relating to network options do LTES Agreement and access rights tender participants require to provide sufficient	The network options will need to be identified with enough specificity to allow tender participants to participate in the bid processes. The information required will include:

Number	Question	Response
	certainty and confidence to participate in the bid processes?	<ul style="list-style-type: none"> Geographic location of distribution and transmission assets, including feeders, substations, and other assets Maximum and minimum capacity for the network <p>As outlined in Box 3, it is important that technical specifications only vary to the extent required to efficiently respond to different generation technology within a REZ.</p>
6	What eligibility criteria should apply for Network Operators that may be authorised to carry out a REZ network infrastructure project?	<p>See section 2.2 of this submission.</p> <p>In our view, the NSW Government should consider the sort of eligibility criteria that would be used to assess a distribution or transmission licence under Schedule 2 of the Electricity Supply Act. That is, prospective operators should be required to satisfy:</p> <ul style="list-style-type: none"> Technical criteria - bid proponents should have relevant experience constructing, owning, and operating electricity infrastructure Prudential criteria – bid proponents should have a suitable credit rating and be required to demonstrate their ability to access capital
7	What factors should be considered by the Consumer Trustee in recommending that the Minister direct, and by the Minister in directing, a Network Operator to carry out a REZ network infrastructure project under the EII Act?	<p>There should be very few circumstances in which the Minister directs a network operator to carry out a REZ network infrastructure project. We support contractual obligations, arising from contestable tender processes, establishing obligations to carry out an infrastructure project. For this reason, the minister should only direct in circumstances where:</p> <ul style="list-style-type: none"> A contestable process did not identify a party willing to undertake the network project and Contractual obligations were not successful in having the required infrastructure built.
8	How can consumer and stakeholder input be considered in the TET and revenue determination processes?	<p>Consistent with best practice consultation approaches, we expect that the Regulator (expected to be the AER) can seek stakeholder input as part of the TET and revenue determination processes.</p>
9	Is clarification required with regard to the principles to be taken into account by the Regulator and the objects of the Act, and are there any additional principles that should be considered by the Regulator?	<p>There are a number of principles the Regulator is to take into account in exercising its functions under section 37 of the EII Act:</p> <ol style="list-style-type: none"> A Network Operator is entitled to recover the prudent, efficient and reasonable costs incurred by the Network Operator for carrying out the infrastructure project. Incentives should be given to Network Operators to promote economic efficiency.



Number	Question	Response
		<p>c) A Network Operator is entitled to revenue for the ongoing ownership, control and operation of an infrastructure project that is commensurate with the regulatory and commercial risks to the Network Operator.</p> <p>d) A Network Operator is entitled to be informed of material issues being considered by the Regulator under this Division.</p> <p>e) Other principles prescribed by the regulations.</p> <p>In our view, it should be clarified in the regulations that where a contestable process has been undertaken to determine the prudent and efficient market price of undertaking a project, that the Regulator should be required to accept those costs as being prudent and efficient by virtue of having been identified through a competitive process (see section 2.2 of this submission). The Regulator's role will be to ensure that the network operator's revenue is consistent with contractual arrangements.</p>
10	What views do you have on these elements and is there any other guidance that should be included in the TET guidelines to be developed by the Regulator?	<p>The Regulator will apply the Transmission Efficiency Test (TET) to assess capital costs for the development and construction of a REZ network infrastructure project once a Network Operator has been authorised by the Consumer Trustee.</p> <p>The Regulator may develop an overarching guideline to cover both the TET and revenue determination process to be followed under the EII Act and also refer to other guidelines if relevant. Some of the elements these guidelines could cover include:</p> <ul style="list-style-type: none"> a) timeframes for undertaking the determination, including public consultation b) requirements on the Network Operator to provide information to the Regulator c) how the Regulator will consider information provided by a Network Operator d) the process and approach by which the Regulator will undertake a cost assessment e) how the Regulator will make a revenue determination if the Network Operator is selected through a contestable process, and f) how the Regulator will treat confidential or sensitive information (including information provided during any contestable process if applicable). <p>We propose that the TET be 'light touch'. If the NSW Government intends to drive efficient outcomes and reveal the efficient cost of projects through contestable processes, allowing the Regulator to open the outcomes of those processes will lead to higher bids in the first place.</p>
11	Should financeability concerns be addressed in the NSW framework?	No, we do not think financeability concerns should be separately addressed in the NSW framework.



Number	Question	Response
		If EnergyCo intends to drive efficient outcomes via contestability, this will reveal whether privately funded network operators are able to deliver the projects taking into account the risk and expected returns of the project.
12	What views do you have on these elements and is there any other guidance that should be included in the guidelines regarding the revenue determination to be developed by the Regulator?	See section 2.3 of this submission. We agree with the view set out in the policy paper that where a contestable process has been undertaken to determine the cost of undertaking a project, that the Regulator should be required to accept those costs as being prudent and efficient by virtue of having been identified through a competitive process. The Regulator's role will be to ensure that the network operator's revenue is consistent with contractual arrangements, rather than determining prudence and efficiency.
13	Are there any elements of the AER's approach to assessing and setting regulated revenue requirements that should be modified or added to when considering the framework that will be applied under the EII Act in New South Wales?	See response to question 12 and section 2.3 of this submission.
14	What do you think about an incentive scheme to ensure the availability of projects and the timely connection of generators to a REZ by Network Operators? How could that be designed?	See section 2.4. If the NSW wishes to ensure that network infrastructure projects are delivered on a timely basis, generators are connected as quickly as possible, and the reliability of the transmission infrastructure is maintained, we support arrangements being established under contract, rather than through a formal incentive scheme.
15	Do you agree there should be limited circumstances under which the Consumer Trustee directs the Regulator to review and remake a revenue determination outside of the five-yearly cycle?	Agree. There should be very limited circumstances under which the Consumer Trustee can direct the AER to remake a revenue determination outside of the five-yearly cycle. Any scope to reopen revenue determinations will increase the perceived risk, and hence cost, of projects.
16	Do you agree with the proposed circumstances under which the Regulator may adjust a revenue determination during the five-yearly cycle?	Where revenues have been determined through a competitive process, revenue adjustments should not be necessary. Any scope to reopen revenue determinations will increase the perceived risk, and hence cost, of projects.



Number	Question	Response
17	Is there a need to clarify the process for transitioning of assets between the NSW and national frameworks?	Agree. Transitioning assets between the NSW and national framework should only be at the election of the network operator.
18	Is there a need to clarify the circumstances under which a transfer of network infrastructure from a Network Operator to another person may occur under the EII Act?	We think it unlikely that network operators will need to rely on the regulations in these circumstances, and therefore do not think this is necessary.



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