

12 February 2021

Energy Security Board

By email: info@esb.org.au

Re: Spark response to Consultation Paper on interim Renewable Energy Zone (REZ) framework

Spark Infrastructure provides long-term capital to support investment in a reliable and affordable low emission energy system. We currently have interests in \$18 billion of electricity infrastructure assets, delivering energy to more than 5 million customers across the National Electricity Market (**NEM**). These interests include a 15% interest in TransGrid; a 49% interest in SA Power Networks; a 49% interest in both CitiPower and Powercor; and 100% ownership of the Bomen Solar Farm in NSW.

We are pleased to have the opportunity to contribute to the ESB's Consultation paper on the interim REZ framework (**Stage 2 paper**). Against a backdrop of increased uncertainty and risk for investors, now is the time to ensure that Australian regulation is best set up to facilitate efficient and timely investment in our energy network. Spark Infrastructure supports the recommendations to establish a REZ framework to assist with efficient and effective connection to, and use of, the electricity grid.

If designed correctly, the development of REZs should improve the coordination of transmission and generation investment as the power system transitions away from coal-fired generation. Importantly, REZs should also lower overall system costs in the long-term interests of electricity consumers, by averting future congestion in the network and allowing for timely, coordinated investment.

We support:

- The proposals to improve co-ordination of connections, including an auction to allocate rights to capped capacity for foundation members. This has the potential to reduce the cost of connection for all generators and increase the certainty that capacity will be available both in the REZ and on the shared transmission network.
- The role of the REZ coordinator to manage the auction process, select tenderers, manage auction proceeds and to provide information to transmission planners. This will improve the information available on current and future needs of connecting generators.
- Support the system strength being managed on a REZ basis to ensure the service received by connecting generators is consistent with rights.

However, we recommend further consideration of the following:

- The interim arrangements should not assume a transition to financial rights and could be used to gain valuable information about the practical and commercial operation of access models.
- Connection access protection is more likely to result in investment in REZs than financial protection because it enables practical and commercial issues to be resolved with certainty.
- Interaction with state-based initiatives to support local policy objectives and sharing of experience to inform the ongoing development of the REZ framework and access models.

The REZ framework is a transitional arrangement and should not constrain future options.

The Stage 2 paper is very clear that improving access and co-ordination for REZs does not resolve broader access and congestion issues on the shared transmission system. This is a critical issue for the

interim arrangements and developing a longer-term solution to the access issues facing generators in the NEM is important.

As stated in our previous submissions to the Coordination of Generation and Transmission Investment (COGATI) review, we are skeptical that the benefits of a locational marginal pricing (LMP) and financial transmission rights (FTR) regime will be effective or warrant the additional complexity.¹

Spark Infrastructure considers that further evidence is required to demonstrate that:

- The signals to improve the efficient locational decisions are greater than the signals that currently exist in the MLF scheme and risk of curtailment.
- That dispatch will be more efficient than the current arrangements and not just result in an alternative floor price being established.
- The FTRs will provide certainty and value over and above that currently available through commercial contracts.
- That the cost of establishing and purchasing FTRs will be offset by reductions in costs elsewhere e.g., cost of capital.

There remain questions regarding the extent to which firm access will resolve issues that arise due to lack of capacity and system strength. Nevertheless, we consider that adopting a financial access protection model as an interim arrangement in REZs is unlikely to be valuable or effective but also limits the opportunity to gain experience with connection access protection models that could better inform future decisions.

Connection access protection models are more likely to result in real-life investment.

The access model chosen is critical to the success of the REZ framework. It is important for generators to be able to specify, value and enforce the access rights over time to be able to commit to a project and investment.

We consider that only the connection access protection model can address all the challenges outlined for development of REZs. This model will:

- Ensure that generators can understand, specify, value, and enforce the service and rights being purchased, increasing the certainty and value to generators so that they can make commercial and practical decisions to invest.
- Provide more robust, reliable, and tangible information on demand requirements and congestion to be relied on in planning and regulatory processes. This will be more likely to deliver the required capacity and system strength, in both the REZ and shared transmission system, needed to underpin the contracted rights. This information will also assist staging and integration with state-based initiatives.
- Enable a 'second wave' of future generators to connect and benefit from the planning, coordination, primary access rights and potentially trading of access rights in a secondary market, available to foundation generators.

We do not support an interim REZ financial access protection model or the options that are predicated upon a future transition towards a FTR regime. This includes the 'REZ as a region' model and the 'early allocation of financial transmission rights'. As indicated above, we consider that cost-benefit proposal for LMP and FTRs has not yet been satisfied as it assumes that the cost of capital to generators will reduce

¹ Spark Infrastructure, Submission to COGATI discussion papers, 8 November 2019

because of the availability of FTRs which is not a widely agreed conclusion or supported by the AEMC survey of investors and follow up work.

We look forward to engaging further with the ESB and energy market bodies regarding longer-term transmission and access reform arrangements.

A national REZ framework will need to be compatible with jurisdictional arrangements.

The ESB has acknowledged in the Stage 2 paper that jurisdictional governments in New South Wales, Victoria and Queensland are pursuing REZ arrangements in parallel with the national process. For example, the NSW government recently implemented legislation to support the delivery of its Infrastructure Road Map.² This legislation includes broad powers related to REZ development, including allowing for the Minister to direct that network infrastructure be developed as well as to implement bespoke access, and setting costs and enabling cost recovery overseen by a state government-selected regulator.

It is vital that a national REZ framework be sufficiently compatible with the jurisdictional arrangements that are being formulated in each State. For example, the rules should not be overly prescriptive with regard to the establishment of a REZ coordinator, allowing for State Governments to identify their own where desired. However, the REZ framework should ensure that there is clarity and certainty about the role of existing TNSPs, system planners and the REZ coordinator.

Similarly, the mechanism by which the REZ coordinator leads certain aspects of REZ delivery (e.g., consultation with local communities and generator proponents) should be flexible and principles based. Otherwise, there is the risk that State Governments may increasingly opt out of the national framework to design market mechanisms suitable to their own requirements and objectives.

Please find attached a summary of our responses to the consultation questions. I would be happy to discuss these matters further and can be contacted on 0421057821.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Sally McMahon".

Sally McMahon

Head of Economic Regulation and Energy Policy

² NSW Government, Electricity Infrastructure Investment Act 2020 No 44, 10 December 2020.

Appendix 1 – Summary of questions in Stage 2 paper

No.	Issue	Response
Question 1	Are REZs an appropriate interim solution to the challenges associated with open access?	Yes. It is sensible to establish the REZ framework in advance of addressing broader transmission access issues. However, the interim framework should not limit future access options for the shared transmission networks or undermine jurisdictional arrangements.
Question 2	What are the likely consequences of a framework that addresses these challenges on a localised rather than a system wide basis?	<p>Developing an access framework on a localised, rather than system-wide basis, increases the opportunities for perverse locational incentives to arise.</p> <p>For example, a generator may seek to locate between a REZ reference node and the regional reference node, in order to take advantage of the available transmission capacity that is servicing the REZ. This could cause congestion issues for those generators within the REZ and would undermine the effectiveness of the broader framework.</p> <p>Under a connection access model, the impact on the transfer capacity and system strength in a REZ must be considered when assessing the connection requirements of another generator within or outside the REZ.</p>
Question 3	Do stakeholders agree with the proposed objectives for a regulated REZ development model?	<p>It is not clear what decisions the three objectives will guide.</p> <p>The ISP objectives will guide the selection of REZ projects, and the RIT-T and AER revenue determination objectives and processes will ensure that they are delivered at the lowest cost.</p> <p>If the objectives are to guide the selection of foundation generators and participants in the auction, then the objectives might be better focussed on ensuring financial viability, technical capability, and sustainable service provision. These might be more consistent with requirements of market participants and licensees.</p> <p>If the objectives are to guide decisions about the design of the auction system, then the objectives should focus more on ensuring an efficient market process.</p> <p>The current objectives as presented are more likely to confuse rather than clarify the development model.</p>
Question 4	Are there alternative, preferable options for deciding which generators become part of the REZ?	<p>There are existing relevant examples of market participation and licensing requirements as well as the operation of markets that could be referred to.</p> <p>It is not clear why the geographic location of REZ participants (prior to investment) is relevant or how that would be assessed.</p>
Question 5	Which party is best placed to perform the role of REZ coordinator where the REZ is being developed in accordance with the regulatory framework? Should the decision	It is vital that a national REZ framework be sufficiently compatible with the jurisdictional arrangements that are being formulated in each State. It is therefore appropriate that State Governments are able to nominate the REZ coordinator and take in to account the

	regarding the identity of the REZ coordinator lie with the State government?	planning arrangements and other candidate entities within the state.
Question 6	Are the functions to be undertaken by the REZ coordinator in the regulated model appropriate?	Yes
Question 7	What, if any, qualification criteria should the REZ coordinator apply to prospective REZ participants?	See response to question 3 and 4.
Question 8	What objective or objectives should the REZ coordinator should seek to achieve when selecting successful tenderer?	The REZ coordinator should seek to achieve the nominated capacity for the REZ at the least cost over time.
Question 9	Should the Rules establish a framework to ensure that the REZ delivers an optimal supply mix?	No, high level objectives, including the NEO/NGO, and existing planning entity requirements, should be sufficient for REZ coordinators.
Question 10	Should REZ developments be subject to a requirement that they may only proceed if a certain proportion of the planned capacity of the preceding REZ stage is subscribed?	No, this is too prescriptive and does not allow for changes in technology, supply, or demand.
Question 11	Should the REZ coordinator return any surplus auction proceeds to customers in the form of a reduction in TUOS charges?	Yes, this would be an efficient way of ensuring all customers benefit from additional funds received from the auction of capacity rights that customers pay for through TUOS.
Question 12	Should the ESB consider REZ models that allow for speculative investment that departs from the ISP, in order to reallocate risk away from customers, such as the one put forward by the Public Interest Advocacy Centre (PIAC)?	<p>It is unclear whether the PIAC REZ model is being proposed instead of, or in addition to, the ESB's interim REZ framework.</p> <p>Our understanding is that the ESB REZ framework is to apply to regulated transmission assets. In this case, the only difference between it and the PIAC model is who determines the value to generators – the government or regulator under the PIAC model or the market (or auction) under the ESB's REZ Framework. We consider the auction process is more likely to result in efficient market outcomes.</p> <p>In any event, it is unclear whether this model is technically, operationally, or legally possible. This should be investigated and resolved prior to this model continuing to be proposed as an option. Even if technically and operationally possible to 'reserve' capacity for the provision of unregulated TUOS services. The proposal is unlikely to be compliant with ring-fencing obligations and the RORI.</p>
Question 13	How should pre-existing developments be treated within a REZ framework? At what stage of development should a project be considered a pre-existing development?	Pre-existing generators should be allocated capacity rights consistent with the existing requirements.

Question 14	Should the interim REZ framework contemplate brownfields developments? If so, should developers have the ability to influence the location and configuration of the REZ transmission assets within a brownfields REZ?	<p>Yes, this is worth considering further.</p> <p>The role of the REZ coordinator could benefit brownfields investment and improve the likelihood that those generators have access, and more certain MLFs and system strength.</p>
Question 15	Are the evaluation criteria set out in the introduction to Chapter 5 appropriate?	<p>We also suggest that the following objectives are taken into account when designing an access regime:</p> <ul style="list-style-type: none"> • The extent to which the model enables the service being purchased to be specified and assured sufficiently to enable confidence in purchasing it. • Sufficient capacity and system strength to provide the contracted rights. • The access model should facilitate subsequent waves of generators to be supported under the same scheme and model. • The access model should not be costly to establish and implement or introduce additional complexity and uncertainty. • The interim access model should not limit future options.
Question 16	Which option for access within a REZ is preferable?	<p>The connection access protection model is the only model that enables the transfer capacity and rights to be sufficiently well specified to be purchased and contractually able to be enforced:</p> <ul style="list-style-type: none"> • Generators are more able to assess the practical and commercial issues to support investment. • The information on demand, service and value is more reliable and tangible to support planning and regulatory processes and decisions about staging. • Does not prevent future generators from connecting and enables a 'second wave' of generators to benefit from the role of REZ coordinator and access rights as foundation generators enjoyed. • Physical access rights can be traded in a secondary market. <p>Financial access protection is difficult to specify and value and less likely to be relied on in planning and regulatory processes. The scheme is complex and costly to establish and maintain. It also limits future options (in the REZ and the shared system) as transitioning from a financial to a physical access model is more difficult.</p> <p>The connection protection access model should be no more costly than a financial protection access model and is likely to be more highly valued by generators so that costs can be recovered, and surplus funds returned to consumers.</p>

Question 17	Are there alternative options that the ESB should consider?	There may also be benefits from trialling different approaches to gain better information about the commercial and practical issues associated with different access models. Therefore, a further option could include the REZ coordinator, seeking interest from potential foundation generators on the preferred access model for a particular REZ development.
Question 18	Are there potential improvements to the options that the ESB should consider?	Enable secondary trading of physical access rights. The REZ coordinator could also co-ordinate the connection of future generators to minimise connection costs and ensure the connection access model is maintained.
Question 19	If the ESB were to adopt one of the access options outlined in this chapter, would it be necessary to restrict connections outside of REZs?	The potential for new connections outside the REZ and the impact should be considered when identifying and developing the REZ.
Question 20	If the ESB were to adopt the financial access protection model, should it also adopt measures to avoid winner takes all outcomes?	This issue would be addressed under the connection access model.
Question 21	If the ESB were to adopt the financial access protection model, should subsequent connecting generators be required to provide compensation that reflects the regional reference price?	This issue would be addressed under the connection access model.
Question 22	If the ESB were to adopt the financial access protection model, how should financial compensation be allocated between REZ generators? Is generator availability an appropriate metric?	This issue would not arise under the connection access model.