

## **AER TRANSGRID'S HUMELINK – STAGE 2 (DELIVERY) CONTINGENT PROJECT APPLICATION**

**3 APRIL 2024**

The Energy Users' Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing, building materials and food processing industries. Combined our members employ over 1 million Australians, pay billions in energy bills every year and in many cases are exposed to the fluctuations and challenges of international trade.

Thank you for the opportunity to make a submission on Transgrid's HumeLink – Stage 2 (Delivery) Contingent Project Application (CPA).

The EUAA accepts the need for Transgrid's HumeLink project and its designation as a priority transmission infrastructure project by the Federal government, especially given its strong relationship with the Snowy 2.0 project.

The EUAA understands that transmission companies are designated under the National Energy Law (NEL) and National Energy Rules (NER) as the entity responsible, not just to finance, build, operate and maintain a functional and reliable transmission network, but also to undertake the risks involved in the financing, building, owning and operation of transmission infrastructure.

At the time NSW Electricity Networks purchased the 99-year lease for Transgrid in December 2015, the planning for the transition of the national electricity transmission infrastructure to enable a 100% renewable generation system was well underway, with the 2015 National Transmission Network Development Plan<sup>1</sup> (final report released November 2015), flagging that major inter- regional and intra- regional transmission upgrades would be required. These major transmission upgrades were then formalised in the 2018 Integrated System Plan<sup>2</sup> (ISP). Both final reports had publicly available drafts available through AEMO's website, 6 months or more in advance of the final reports being published.

Given the scale of what was required to transition the NEM was well known almost 10 years ago it is reasonable to believe that Transgrid (and other transmission network service providers) had (or should have had) a clear understanding of the full range of risks and costs involved and made decisions to invest in these entities on that basis. Given this, the EUAA does not accept Transgrid's proposals that effectively transfers the financing and construction risks to consumers.

Transgrid's current proposal in the HumeLink CPA does this through requests by Transgrid for the removal of the Capital Expenditure Sharing Scheme (CESS) and through commencing depreciation "as incurred" rather than the traditional "as commissioned". In addition to this, Transgrid is proposing to move away from a fixed price Engineer,

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<sup>1</sup> [2015-ntndp\\_final.pdf \(aemo.com.au\)](#)

<sup>2</sup> [integrated-system-plan-2018\\_final.pdf \(aemo.com.au\)](#)

Procure, Construct (EPC) contract to a more “flexible” Design and Construct (D&C) arrangement whereby costs and risks are distributed in a different manner. While Transgrid claim this will deliver a lower cost for consumers, it is the initial “headline” cost saving that is referenced, not the final cost that consumers end up paying. We will rely heavily on the AER to make an assessment on the validity of the Transgrid claim and encourage both the AER and Transgrid to continue to engage with consumers to assist them in their understanding of this revised contracting approach.

By transferring the risks to consumers through the removal of CESS and what is in effect a form of accelerated depreciation, consumers are being asked to fund projects before the realisation of consumer benefits, and consumers will bear the full cost of expenditure over-runs. We are concerned that the proposed D&C arrangements may amplify this risk.

The traditional “as commissioned” depreciation model encourages transmission networks to manage projects to be delivered on-schedule, which is a significant requirement for HumeLink, while the CESS is designed to encourage transmission operators to manage projects to be delivered on-budget (EUAA points out that under CESS, consumers pay for 70% of a project’ over-expenditure in any case). Consumers have no ability to ensure a transmission project is delivered on-time and on-budget and therefore has no ability to manage these risks.

While we recognise that transmission projects are unlikely to be delivered on-budget, due to the current global economic conditions and the current global competition for resources to complete transmission projects and that this may also create project delays, it is EUAA’s position that transmission companies (perhaps with government support) are still best placed to manage the risks of budget overruns and timeline delays, not consumers. This position is consistent with both the NEL and NER.

The EUAA welcomes Transgrid’s efforts to reduce project costs through bundling its transmission projects together under the Powering Tomorrow Today (PTT) and are prepared to accept that the revised D&C approach is intended to deliver a better outcome for consumers (although we await AER guidance to validate the approach).

However, the EUAA and other stakeholders are forced to take Transgrid’s word on the savings, specifically:

- EUAA has no doubt that bundling long lead-time equipment orders for ISP projects through PTT has resulted in savings, however EUAA has no way of fact checking the \$85 million figure placed on these savings by Transgrid;
- Likewise, EUAA agrees that savings will be made through performing Project Energy Connect (PEC) enhancement works which will see the Gugaa integration works included in HumeLink and the transmission line from Dinawan to Wagga Wagga constructed at 500kV instead of the PEC plan 330kV, however EUAA has no way of fact checking the claimed \$90 million and \$697 savings respectively from these two projects;
- Transgrid also claim a \$237 million saving from appointing design and construction (D&C) contractors through an Incentivised Target Cost D&C contract rather than the traditional D&C contract. This is even more surprising when other transmission network service providers are continuing with traditional D&C contracts and claiming that they are the most efficient and cost-effective approach to contracting. Again, EUAA has no way to fact check this claim by Transgrid.

EUAA recommends that the AER needs to confirm the counterfactuals as presented by Transgrid and provide stakeholders and consumers assurances that the approaches detailed by Transgrid (and outlined above) will deliver

a better outcome for all stakeholders and consumers and is indeed the best approach for HumeLink and other ISP projects delivered by them.

Without AER's assurances, the EUAA has no way of determining that Transgrid's claimed savings figures are correct, and specifically that the ITC D&C approach is better than a traditional D&C approach, recognising that Transgrid has already entered into two ITC D&C contracts for HumeLink and that these are unlikely to change for this project.

The EUAA does not support Transgrid's HumeLink CPA proposal to remove the Capital Expenditure Sharing Scheme (CESS) and accelerate depreciation of the asset through an "as incurred" depreciation model rather than the traditional "as commissioned" approach. The EUAA has arrived at this position by reason of:

- CESS
  - Transgrid's HumeLink CPA argues that the application of the CESS introduces an asymmetric risk for Transgrid due to the higher likelihood of overspend.
  - Transgrid's HumeLink CPA also argues that no CESS is better for consumers, however the EUAA understands that this is only true in the highly unlikely event of an underspend.
  - Transgrid argues that equity injection from its investors is questionable with the CESS in place. The EUAA counters that Transgrid has one of the highest debt to equity ratios of the NEM's network service providers, and well above the recommended 60:40 debt to equity ratio. As willing investors in the transition of our energy system, equity participants are acknowledging the challenges, risks and rewards of doing so. We have to assume that they were also very aware of the regulatory environment they were investing in and as such, risks such as these would have been contemplated as part of their decision to participate in 2015 (or continue to participate).
  - As such, the EUAA rejects Transgrid's position on the CESS and strongly supports the inclusion of CESS in the revenue determination.
  
- Financeability:
  - The EUAA has been vocal in its opposition to accelerated depreciation of new electricity network assets, however recognises the AEMC's recent draft determination on this matter.
  - The EUAA maintains that accelerated depreciation unfairly transfers costs (and risk) to consumers before the realisation of the consumer benefits (i.e. future reduced costs) are realised.
  - The EUAA rejects energy networks shifting risk to consumers when their businesses have been established to bear those risks. We also assume that through the process of due diligence that equity investors fully understood the risks, costs and benefits of investing (or continuing to be an investor) in the transition of the Australian energy system.

We have made no secret of our opposition to the removal of the CESS and inclusion of accelerated depreciation and are disappointed that Transgrid has requested both mechanisms to transfer financing and project risks away from itself. Having heard Transgrid's arguments for both, and Transgrid having heard our arguments against these approaches, we would have thought a reasonable compromise would be for Transgrid to request one approach or the other. The EUAA has been a long-standing member of the Transgrid Advisory Council (TAC) and remain committed to working with Transgrid but it seems that progressively there is very little scope for collaboration or consideration of consumer preferences.

In addition to the above commentary, we find it difficult to understand how Transgrid can justify a \$33 million cost in raising equity against a \$30 million cost to raise debt, given equity raising is effectively an “internal” process. This \$33 million cost of raising equity is even more extraordinary when considering that debt will make up a higher proportion of total project financing than equity. At a minimum, we would expect the costs to be proportional to the financing amount raised through debt and equity, in reality we would expect that \$1 raised through equity to be far cheaper than \$1 raised through debt. We request that the AER perform a forensic examination of these financing costs with our comments in-mind.

The EUAA believes that there are alternative solutions that Transgrid, and potentially governments, have not thoroughly explored that would assist in managing the alleged risk asymmetry and financeability issues. For example, if private equity refuses to come to the party then governments could take a short-term equity position in projects (i.e. via Rewiring the Nation) to act as a consumer risk shock-absorber. Once many of the early stage risks dissipate and when consumer net benefits are closer to realisation, this government equity can be withdrawn to be replaced by a combination of debt and owner’s equity. We have made this and other suggestions in previous submissions and are disappointed that we find ourselves the position that we were so concerned about; consumers bearing the brunt of the costs and risks during a time when project cost and risks are rising dramatically.

Additionally, a major purpose of the HumeLink Stage 1 CPA (CPA1) for early works was to get a better cost estimate that would reduce the risk of overspend (we would argue this should be a minimum AACE Class 3 cost estimate, preferably Class 2 per our CPA1 submission<sup>3</sup>). It was on this basis that we provided our qualified support. It now appears that Transgrid’s insistence on removing the CESS and accelerating depreciation suggests that the \$350 million CPA1 works (which consumers are already paying for) has not placed Transgrid or consumers in a better place than had the CPA1 works not proceeded.

The EUAA will consider future early works proposals very carefully before providing our support, to ensure that proposed early works achieve a better cost estimate than would otherwise have been the case. A better cost estimate will allow transmission companies to be better placed to manage the risks that the NEL and NER require of them, and ensure overspend risks are better mitigated.

Once again, as a long-standing member of the TAC, we remain committed to working with Transgrid to find equitable solutions to the issues that confront all of us as we move towards a net zero energy system.

Do not hesitate to be in contact should you have any questions.



Andrew Richards  
Chief Executive Officer

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<sup>3</sup> [https://www.aer.gov.au/system/files/EUAA%20Humelink%20CPA%20submission\\_0.pdf](https://www.aer.gov.au/system/files/EUAA%20Humelink%20CPA%20submission_0.pdf)