Submission to AER

Expenditure Forecast Assessment Guidelines Review: Draft Decision

9 August

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About the Justice and Equity Centre

The Justice and Equity Centre is a leading, independent law and policy centre. Established in 1982 as the Public Interest Advocacy Centre (PIAC), we work with people and communities who are marginalised and facing disadvantage.

The Centre tackles injustice and inequality through:

- legal advice and representation, specialising in test cases and strategic casework;
- research, analysis and policy development; and
- advocacy for systems change to deliver social justice.

Energy and Water Justice

Our Energy and Water Justice work improves regulation and policy so all people can access the sustainable, dependable and affordable energy and water they need. We ensure consumer protections improve equity and limit disadvantage and support communities to play a meaningful role in decision-making. We help to accelerate a transition away from fossil fuels that also improves outcomes for people. We work collaboratively with community and consumer groups across the country, and our work receives input from a community-based reference group whose members include:

- Affiliated Residential Park Residents Association NSW;
- Anglicare;
- Combined Pensioners and Superannuants Association of NSW;
- Energy and Water Ombudsman NSW;
- Ethnic Communities Council NSW;
- Financial Counsellors Association of NSW;
- NSW Council of Social Service;
- Physical Disability Council of NSW;
- St Vincent de Paul Society of NSW;
- Salvation Army;
- Tenants Union NSW; and
- The Sydney Alliance.

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The Justice and Equity Centre office is located on the land of the Gadigal of the Eora Nation.

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1. Introduction

The Justice and Equity Centre (JEC - formerly PIAC) welcomes the opportunity to respond to the Australian Energy Regulator's (AER) Amended National Energy Objectives: The AER Expenditure Forecast Assessment Guidelines Review, Draft Decision (Draft Decision).

The context for this process is the need for AER guidelines to reflect the amendment of the National Electricity Objective (NEO), the National Gas Objective (NGO), and National Electricity Retail Objective (NERO), which now require decision makers to consider achievement of emissions targets when determining the long term interests of consumer of electricity and gas.

The JEC welcomes the introduction of emissions reduction to the amended energy objectives. However, we are concerned the scope of the AER's proposed guidelines falls short of what is required by the amended objective and the Minister's intent in introducing it. As proposed, emissions reduction is only to be considered when approving network expenditure that will reduce emissions. It is not proposed that emission targets will be considered for expenditure that either increases emissions, or maintains network infrastructure that has a role in continued emissions which impact emissions reduction targets.

Ministers objective and intent in amending the energy objectives was to enable a decarbonised, efficient and reliable energy system, as a driver for efforts to achieve net zero by 2050. Market bodies were given direction that the operation and regulation of energy investment and markets should actively contribute to achieving net zero. Accordingly, consideration of achievement of the emission targets at all levels is relevant to the AER's approval of all expenditure. Approving ongoing or new expenditure that does not support emissions reduction, will mean the AER does not achieve its stated objective as outlined in the paper:

> The [AER] exists to ensure energy consumers are better off now and into the future. Consumers are at the heart of our work, and we focus on ensuring a secure, reliable, and affordable energy future for Australia as it transitions to net zero emissions.[1]

Consumers will not be better off where there is imprudent or inefficient investment in networks, which does not contribute to the transition to net zero, or which impedes the efficient achievement of targets.

2. The Ministers intent when amending the national energy objectives

The Ministers' intention in amending the NEO, NGO and NERO were made clear in the 2nd Reading Speeches of the Bill amending the National Electricity Law, National Gas Law, and the National Electricity Retail Law.[2] These intentions are relevant to the interpretation of the directions and powers which arise from the Bill and should guide the AER (and other market

1 Draft Decision, p.1.

2 National Electricity Law - schedule to the *National Electricity (South Australia) Act 1996* (NEL); National Gas Law – schedule to the *National Gas (South Australia) Act 2008* (NGL); National Energy Retail Law – schedule to the *National Energy Retail Law (South Australia) Act 2011* (NERL).

bodies) in their implementation of the emissions reduction objective and fulfillment of their regulatory roles. These intentions:

- Reflect the commitment of all governments in Australia to achieve net zero by 2050 or earlier.
- Are to support achievement of a decarbonised energy system and contribute to government emission reduction targets.
- Underline the role of market bodies in enabling this transition.
- Require decision makers to continue to promote efficient investment in, operation of and use of services in the long term interests of consumers.
- Add achievement of emissions reduction targets to the dimensions of consumer interest.
- Require as a minimum the consideration of achievement of targets set out in the AEMC target statement.
- Include emissions reduction as a new form of market benefit.

The relevant portions of the 2nd Reading Speech in the House of Assembly are extracted below:

> The government is delivering an important national reform to incorporate an emissions reduction component into the national energy objectives—long overdue reforms. The Statutes Amendment (National Energy Laws) (Emissions Reduction Objectives) Bill 2023 reflects the commitment by all Australian governments to net zero greenhouse gas emissions by 2050 or earlier.
>
> […]
>
> […] As currently framed, the energy objectives do not refer to emissions reductions, either directly or indirectly.
>
> Changing this will send a clear signal to wider industry, market participants, investors and the public of all Australian governments' commitments to achieve a decarbonised, modern and reliable energy system that contributes to the achievement of Australia's emissions targets. These reforms are long overdue.
>
> This bill will integrate greenhouse gas emission reduction and energy policy into the national energy laws. […] The bill's amendments will clarify that the Australian Energy Market Commission, the Australian Energy Market Operator, the Australian Energy Regulator and other decision-makers under the laws should explicitly consider the achievement of emissions reduction targets alongside the existing components when they use their respective powers and functions.
>
> […]
>
> As we transition towards a low emissions energy system, these changes are intended to ensure the transition is managed in the long-term interests of consumers—in respect of not just emissions reduction but also price, quality, safety, reliability and security. […]
>
> The bill frames the emissions reduction objective by reference to the achievement of targets set by a participating jurisdiction, be it the commonwealth, a state or a

territory, for reducing or that are likely to reduce Australia's greenhouse gas emissions. These targets could include those with an explicit objective of emissions reductions or those that are likely to contribute to emissions reductions, such as a renewable energy target or an electric vehicles target. The intent of this wording is to allow energy market bodies the discretion to consider appropriate targets relevant to a matter under consideration. […]

The bill requires the Australian Energy Market Commission to prepare, maintain and publish a targets statement that lists the targets that must, at a minimum, be considered by decision-makers, comprising government or regulatory entities such as market bodies, in applying the emissions component of the national energy objectives. […]

[…]

Introducing an emissions reduction component implies that the reduction of greenhouse gas emissions is a new category of market benefit to be assessed in market body decisions and processes where appropriate. To operationalise the emissions reduction component under an economic efficiency framework, a methodology for valuing emissions reduction for the purposes of regulatory decision-making is required.[3]

3. Impact of the amendments on the AER's functions

When exercising its economic regulatory functions and powers the AER are required to consider the NEO and NGO.[4] Similarly the NERL requires the AER consider the NERO.[5]

The NEO, NGO and NERO were amended to add to the list of consumer's long term interests,

the achievement of targets set by a participating jurisdiction-

(i) for reducing Australia's greenhouse gas emissions; or

(ii) that are likely to contribute to reducing Australia's greenhouse gas emissions.[6]

The NEL, NGO and NERL explicitly require that when having regard to the NEO, NGO and NERL objective, 'a person or body must consider, as a minimum, the targets stated in the targets statement.'[7] The term 'as a minimum' indicates scope to consider other relevant targets of a jurisdiction.

Consequently, the AER must now consider the achievement of emission reduction targets in the AEMC targets statement.

3 2nd Reading SA House of Assembly 14 June 2023, Hansard pp.4378-4380.
4 s. 16(1)(a) NEL; s. 28(1)(a), NGL.
5 s. 205 NERL.
6 s. 7, NEL; s. 23, NGL; s.13, NERL.
7 s. 32A(5) NEL; s. 72A(5), NGL; s.224A(5), NERL.

The requirement to consider the “achievement of” targets set by a participating jurisdiction means the AER:

- Must do more than simply consider emissions reduction per se, and should also consider relative impact on the achievement of targets (both positive, and otherwise).
- Must do more than simply classify any level of emissions reduction as contributing to Australia’s emissions reduction commitments.
- Must consider the targets intention to bring about a specific end point. Specifically the level of emissions reduction required by the targets, and the timeline for achieving this reduction.
- When considering the achievement of this end point, must consider the emissions impact of any expenditure (whether positive or otherwise) and the time line of this emissions impact.
- Should consider the emissions impact of all expenditure. Whether this in the form of expenditure that reduces emissions, or expenditure which increases or perpetuates emissions.

Energy Ministers in responses to consultation on the draft Orderly Exit Mechanism Framework, acknowledged that consideration of emissions targets will be a relevant consideration when governments negotiate or mandate that coal generators are maintained online after the date their operators have proposed for closure. This is not expenditure on emissions reductions, but expenditure that continues or increases emissions.[8]

4. Proposed approach to an emissions reduction guidance note

4.1 Existing relevant AER and AEMC guidance

In the September 2023, AER Guidance on amended National Energy Objectives, noted that,

> The AER and other market bodies will take these targets into account when applying the relevant objective in those jurisdictions.
>
> With the implementation of these changes, emissions reduction will no longer be part of the external context for our decision making, but one of the central considerations in determining if our decisions are in the long-term interest of consumers. Our

8 See *Response to Stakeholder Submissions*, June 2024, p.9 and p.63, https://www.energy.gov.au/sites/default/files/2024-08/oemf-response-to-stakeholder-submissions.pdf.

> decisions will shift to internalising emissions impacts rather than treating them as an external factor.[9]

The AEMC has guidance on "How the national energy objectives shape our decision". This includes a section entitled "The big picture: decision-making in a transitioning sector" which places decarbonisation alongside other changes such as technological change and stake-holder behaviour changes. The AEMC states,

> When making decisions, we cannot lose sight of the bigger picture and the depth and breadth of the reforms that are occurring and the need to manage the unprecedented challenges facing the sector. Nor can we ignore that the pace of change is accelerating as we navigate through the uncertainty this rapid transition brings.[10]

The AEMC has also issued an appendix to its guidance dealing specifically with emissions reduction. This explains that the AEMC is internalising emissions considerations in its decision making following the amendment to the national energy objectives. It also notes it intends to consider the impact on emissions reduction targets of each project it undertakes, not merely those which may reduce emissions.[11] The AER should also consider achievement of emission targets in all expenditure decisions, and not simply proposals to spend money on emissions reduction.

The JEC recommends the AER draws on the AEMC note when drafting its own emissions reduction guidance.

4.2 Regulated services and expenditure that contribute to meeting emission reduction targets

Question - *We are interested in any views as to whether there are further specific considerations that we should take into account in considering whether proposed expenditure which contributes to the achievement of emissions reduction targets relates to relevant regulated services.*

The JEC agrees that only expenditure related to 'providing regulated services' can earn regulated revenue. The AER should take a progressive (though not unfettered) view of what is within the scope of 'providing regulated services' and what spending fits this criteria. Regardless, networks spending on emissions reductions project must be determined to be prudent and efficient in promotion of consumers' interests.

We note that the AER only propose to consider the achievement of emissions targets where expenditure will reduce emissions, not where it may increase emissions, or maintain ongoing

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9 *AER Guidance on amended National Energy Objectives*, September 2024, p. 5, https://www.aer.gov.au/documents/aer-guidance-amended-national-energy-objectives-final-guidance-note-september-2023

10 *AEMC, How the national energy objectives shape our decision*, 1 August 2024, p.8, https://www.aemc.gov.au/sites/default/files/2024-07/Final_AEMC%20guide%20on%20energy%20objectives%20markup%20for%20new%20MCE%20statement%20%28effective%201%20Aug%202024%29_0.pdf, (AEMC Guidance).

11 AEMC Guidance, Appendix A.

network systems and continuing emission. We consider this to be an inappropriately narrow interpretation of their requirement to consider emissions (as detailed in earlier sections).

The AER is required to consider the energy objectives and this now involves a requirement to consider achievement of emissions targets in assessment of all expenditure which may have an impact on emissions (regardless of what that impact may be).

We contend the AER must be satisfied that allowable expenditure is that which a prudent operator would incur in a way consistent with the amended energy objective (including the emissions reduction and targets aspect).

The NGR were amended to explicitly require consideration of the NGO when determining what expenditure a prudent service provider acting efficiently would incur when providing services. Rule 79(1)(a) now reads:

> (1)Conforming capital expenditure is capital expenditure that conforms with the following criteria:
>
> (a)the capital expenditure must be such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of providing services in a manner consistent with the achievement of the national gas objective;
>
> […]

See also NGR rule 91(1).

Amendments to the NGR requirement to determine if the overall economic value of expenditure is positive do not limit consideration to the value of emissions reduction. Rather it refers to 'changes' to emissions.[12] Accordingly, excessively adding to emissions would result in a 'negative net value'. We consider this consistent with our interpretation that all emissions impacts, and relative contributions to emission targets, must be considered.

4.3 Emissions accounting and scope

Question - *We are seeking stakeholder views on what the relevant scope of emissions can be considered in forming a view on a capex or opex proposal. We note that this issue is currently being consulted in our review of the Cost Benefit Analysis Guideline and Regulatory Investment Test (RIT) Application Guidelines. We will consider submissions in response to these guideline review processes insofar as it relates to the EFA Guideline and the emissions reduction guidance note.*

The scope of emissions to be considered is crucial. Ministers intend the scope is economy wide emissions in Australia. The AEMC rule change, included amending the rules to allow

12 See rule 79(3), NGR.

consideration of net benefits outside the electricity and gas networks.[13] Consequently, all scope 1, 2 and 3 emissions reductions in Australia should be considered.

The AEMC guidance also captures this stating,

> In estimating the emissions impacts of a proposed rule change, we consider all material emissions reductions or increases in Australia that would be likely to result from the rule change (directly or indirectly). This includes emissions impacts across the economy.[14]

5. The proposed amendments to the EFA Guidelines

Question - *Do you agree with the proposed updates to the EFA Guidelines?*

Question *- Are there any additional updates, related to the amended national energy objective, we have overlooked that need to be incorporated?*

We do not consider the proposed EFA guidelines to be sufficient, with the narrow references to only emissions reduction expenditure not meeting the requirement to consider emissions and the achievement of targets.

The AER must consider the emissions impact of all expenditure. Whether this in the form of expenditure that reduces emissions, or expenditure which perpetuates or increases emissions.. In short, any expenditure which has an impact on the achievement of emissions targets.

Whenever, exercising its economic function the AER must consider the NEO. The Ministers intention was to help achieve a decarbonized, modern and reliable energy system, as part of efforts to achieve net zero by 2050. Any expenditure which will supports new fossil fuel generation, or the continued use of fossil fuel generation must be examined against the emission reductions targets. Of specific relevance is the target of 82% renewable generation in the NEM by 2030. But state targets will also be of relevance for example Victoria's target of 95% renewable generation by 2035.

Emissions reduction is a relevant consideration to whether any expenditure is prudent and efficient. Consequently additional amendments to the EFA Guidelines should be made in order to properly ensure consideration of achievement of emission targets.

- Achievement of emissions targets should be included as part of the section 2.5 - Assessment principles.

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13 See s. 7(c) NEL; s. 23(b) NGL; s.13(b) NERL; section 4.3, AEMC *Final Determination Harmonising the National Energy Rules with the updated energy objectives*, 1 February 2024, https://www.aemc.gov.au/sites/default/files/2024-01/final_determination.pdf; rule 79(3) NGR; clause 5.15A.1 NER; *MCE statement about the interim value of greenhouse gas emissions reduction*, 19 July 2024, p.3, https://www.aemc.gov.au/sites/default/files/2024-07/19%20July%202024_Amended%20VER%20MCE%20Statement%20to%2030%20June%202026.pdf.

14 *AEMC Guidance*, p.14.

- Similarly, achievement of emissions targets should be references in section 3 – Capital expenditure assessment.

- Emission data should be required to be provided by proponents, and this requirement added to section 5 - Information requirements.

6. Continued engagement

We welcome the opportunity to meet with AER and other stakeholders to discuss these issues in more depth. Please contact Michael Lynch at mlynch@jec.org.au regarding any further follow up.