AGL Electricity Limited
Level 2,333 Collins Street, Melbourne
PO Box 14120 MCMC
Melbourne Victoria 8001

Telephone 03 9201 7694
Facsimile 03 9201 7059

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Mr Sebastian Roberts
General Manager
Regulatory Affairs - Electricity
Australian Competition and Consumer Commission
PO Box 1199
DICKSON ACT 2602

By email to electricity.group@accc.gov.au

Dear Mr Roberts,

Review of the Regulatory Test – Draft report

AGL supports efforts by the ACCC to increase the potential for appropriate network investment in the NEM by improving the operation of the Regulatory Tests. We are concerned, however that:

- simple attempts to include the benefits of competition in an economic test will be ineffective
- using differing values of customer lost load (VoLL vs VCR) is likely to bias investment towards networks from generation and demand side options.

AGL considers that the ACCC should take the opportunity afforded by the Code changes made by NECA regarding transmission planning to revise the basis of the Regulatory Test from an economic test of benefits to the market to a commercial test of the net benefits to those that will pay the cost of the investment. This change would also align the Regulatory Test with the beneficiary pays approach that was introduced into the Code by the network and distributed resources Code changes. The need for this form of alignment was mentioned by both the National Electricity Distributors Forum and Edison Mission Energy in their comments to the Issues Paper and by AGL in our submission to the discussion paper.

If the test were to be recast as a benefits test the process could be to:

- define the beneficiaries of the project
- determine the benefits they require and will receive from the project
- compare the proposed projects with all other projects that could reasonably be able to provide the required benefits (may be less than the benefits of the project, but should be at the level required by the beneficiaries)
- choose the option where the benefits to the beneficiaries are maximised and where those benefits exceed the cost of the option.

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To ensure that the modelled benefits were achieved the ACCC should then

- assess the actual benefits achieved at the next regulatory reset:
  - if the benefits are being achieved then the project costings should be confirmed
  - if only a reduced benefit is being achieved the contribution to AARR should be reduced so that the net benefit is positive
- once confirmed or adjusted, the project should not be subject to further optimisation (in line with the Parer recommendation) to minimise the regulatory risk of the TNSP.

This approach would allow:

- the party applying the test to replicate the outcome that would have occurred in a market setting rather than a regulated setting
- any identifiable benefits to be included in the tests, including modelled competition benefits
- the reliability arm of the Regulatory Test to be removed since that would simply be a special case of the more general test where only specific customers are beneficiaries
- a single approach for new projects and conversion between unregulated and regulated status
- confirmation of modelled outcomes (at the next regulatory reset)
- removal of optimisation risks (after the initial check of benefits)
- consistency between the test and potential approaches to financial transmission rights.

This approach would also return the Regulatory Test to what was originally intended in the Code, which was that those that pay the cost of an augmentation should see a net benefit from that augmentation.

Using this approach will also make investment decisions consistent:

- generation investments are made where enough investors see a net benefit in a generation investment either locally or remotely from the demand
- MNSP investment occurs when enough investors see a net benefit in an interconnector investment to bring supply to the demand
- regulated investments are made where the regulated entity (or another approving body), acting as a proxy investor on behalf of the wider group of beneficiaries, assesses that there is a net benefit to the investment.

AGL recommends that the Commission consider this approach since it allows regulators and TNSPs to mimic the outcome that would have occurred in the market (had sufficient investors been able to come together to consider the best investments for them) rather than trying to "shoe horn" increased competition benefits into the existing market benefits test.

AGL has concerns with the proposal to allow TNSPs to use the Value of Customer Reliability (currently assessed near $30,000) as well as the value of VoLL (currently $10,000) in the Regulatory Test. This approach means that it will be possible to determine that a net benefit occurs for a network investment based on servicing a customer load far more easily than it will be possible to determine a commercial net benefit for a market based demand side or supply side alternative. This could bias investment in the NEM towards network from supply and demand side options.

AGL is content, however, that this apparent bias towards networks is self correcting in that, as Powerlink has recently determined for Queensland, the most cost effective solution for a network issue may be to contract with an energy supplier to meet short term needs. Thus, if the Regulatory Test is applied correctly, a TNSP would source generation and demand side contracts if they proved to be the most cost effective in the circumstances. This approach, therefore, could support additional generation in the NEM on a more commercial basis than the NEMMCO Reserve Trader. It will be important, however, that the Regulatory Test be applied in such a way that all options are available to be considered if this self-correction is to occur.

If you have any questions regarding the above matters, please contact Alex Cruickshank, Manager NEM Development on (03) 9201 7694 or e-mail acruicks@agl.com.au.

Yours sincerely,

Unsigned electronic copy
Original sent by mail

Mike Bailey
General Manager Wholesale Energy

AGL Electricity Limited