Chris Pattas
General Manager
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Dear Sir,

Please find following a submission on the revised regulatory proposal and associated attachments lodged by TasNetworks covering the next regulatory period, which is due to start on 1 July 2019 with a five year duration.

Contingent Projects

TasNetworks seems to be proposing to retain three transmission contingent projects in its revised regulatory proposal:

- the North West 220 kV Network Redevelopment;
- the Sheffield to Palmerston 220 kV Augmentation; and
- Project Marinus (the proposed second Bass Strait interconnector).

For the first two projects, revised trigger events are given in the relevant Project Needs Analysis Documents:

> a) A net economic benefit can be obtained by increasing transmission capacity for low cost generation committed to connect at or west of Burnie Substation in North West Tasmania; and/or
>
> b) A commitment to proceed with a second Bass Strait interconnector connecting at 220 kV at or west of Burnie Substation.
>
> c) Successful completion of a RIT-T and a determination by the AER that the proposed investment satisfies the RIT-T.
>
> d) TasNetworks Board commitment to proceed with the project subject to the AER amending the revenue determination pursuant to the Rules.

and,

> a) A net economic benefit can be obtained by increasing transmission capacity for low cost generation committed to connect in North West and/or West Coast of Tasmania; and/or
>
> b) A commitment to proceed with a second Bass Strait interconnector connecting in North West Tasmania.
>
> c) Successful completion of a RIT-T and a determination by the AER that the proposed investment satisfies the RIT-T.
>
> d) TasNetworks Board commitment to proceed with the project subject to the AER amending the revenue determination pursuant to the Rules.

In each case, event (a) is not independent of event (c): if (a) can be demonstrated, it will contribute to (c).

It is not clear that the first two contingent projects are independent of each other. They seem to be two stages of an overall augmentation required to remove generation constraints that may arise in the future due to the proposed connections in the same areas

of Tasmania (although one does extend to include future generation on the west coast as well).

Further, considering the project needs analyses for the first two contingent projects, Table 1 in each of the documents gives different values for putative connections to the 110 kV network in north-west Tasmania, even though it would be expected to be the same. This brings into question the analyses presented in these documents.

The first two contingent projects are considered by TasNetworks to be essential for Project Marinus. For this reason, it seems unusual that event (b) should be a trigger for either of the first two contingent projects when considered as stand-alone projects.

Also, since these two are essential for, and consequential to, Project Marinus, it would be expected these works should be included in the project scope for that project to enable a full assessment of the costs and benefits under the RIT- T. But TasNetworks states that the works covered by the first two contingent projects are not contained in the scope for Project Marinus. Consequently, any RIT-T performed without consideration of consequential augmentation will be inadequate.

The Project Specification Consultation Report for Project Marinus (attached to TasNetworks' Revised Regulatory Proposal) ostensibly provides an overview of the costs and benefits of the project as a whole. Nonetheless, it does not include the first two contingent projects, nor is it clear whether there are other consequential works not included in the scope. Neither does the report clearly identify which portion of those costs and benefits applies to the Tasmanian jurisdiction and the TasNetworks regulated network businesses. It is difficult, therefore, to ascertain the effect of the proposed contingent project on Tasmania and assess the appropriateness of investment.

Curiously, revised trigger events for Project Marinus itself do not seem to have been included in the revised regulatory proposal, despite TasNetworks identifying the project as a contingent project.

Innovation Projects

TasNetworks has proposed four "innovation projects" in its revised regulatory proposal to:

> ... address customer feedback that there should be an increased focus on 'innovative projects' that are linked to our 2025 strategy.

This is not, on the face of it, a good reason for expenditure.

It is noted, also, that TasNetworks did not originally propose expenditure on innovation projects in its regulatory proposal:

> In this proposal, however, we have not directly attributed expenditure to the 'innovation' category - as innovation is an activity that affects investment decisions across the entire business, rather than being a standalone activity.

Introducing an explicit forecast for innovation expenditure in the revised regulatory proposal runs counter to the requirement in the National Electricity Rules that a revised regulatory proposal be used only to address issues identified by the AER.

Distribution Network Pricing

In its Tariff Structure Statement for the distribution business, TasNetworks aims to achieve cost reflectivity in residential pricing through removing discounting existing in the current tariff suite and moving to a time of use pricing regime for all customers. That is, residential users will eventually pay the same rate for electricity used for general purposes, heating and hot water.

Heating is essential in Tasmania due to the climate; hot water is essential everywhere. That is, doing without heating or hot water is not a viable option. Electricity is the major energy source for heating and hot water since gas reticulation is limited. That is, there is limited potential for substitution. Competition in energy generation in Tasmania is practically non-existent: there is one generator with significant market power. Competition in energy retail for residential customers is similarly non-existent: there is one retailer that covers the residential sector. So, Tasmanian residential customers are reliant upon regulation to ensure that the price that they pay for electricity is reasonable.

The AER has oversight of part of the end price for Tasmanian residential customers through its administration of the economic regulation of the monopoly distribution and transmission networks. In doing so, it should have regard for the National Electricity Objective (NEO), one aspect of which is "price".

The AER has traditionally addressed the price issue by ensuring that regulated expenditure is reasonable, and that there is limited price increase within a regulatory control period. An aspect of price that has not previously been considered is "affordability". There is little point having a regulated price that meets all of the requirements of economic theory if the consumer is unable to afford consumption.

Aligning the rates for electricity used for general purposes, heating and hot water will create a significant impost on Tasmanian residential consumers, potentially making access to heating and hot water unaffordable. Moving to the alternative time of use offerings will not address the issue: the rate for general power, hot water and heating are immediately aligned.

In the long term, when all residential customers are on time of use offerings, the tariffs will need to recover the revenue for that customer class, just as the current suite of consumption-based tariffs should. Cost-reflective tariffs will not look as enticing, especially when combined with the effect of decreasing economic demand under a revenue cap regime.

While other jurisdictions do not have the luxury of multiple residential tariffs, Tasmania does, and this has driven both direct consumption behaviour and indirect drivers of consumption such as house design. It seems inappropriate that this accident of history is to result in financial hardship to a large number of Tasmanians as a consequence of regulatory action.