

15 October 2019

Mr Evan Lutton
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Dear Evan

RE 2019 draft benchmarking report for transmission networks

Thank you for providing TasNetworks with an advance copy of the Australian Energy Regulator's 2019 Benchmarking Report for transmission network service providers, ahead of its publication later this year. We appreciate the opportunity to review and comment on the report prior to its release.

The draft report tells a positive story for Tasmania's transmission network, with TasNetworks rated for the fourth year in a row as the most productive network of the five that form the backbone of the National Electricity Market (**NEM**). While the favourable comparison with the performance of other networks is welcome, TasNetworks acknowledges that the transmission networks within the NEM are a diverse group of businesses and there are likely to be many operating environment factors, as well as inherent differences between networks in terms of their design, size and density, which have a significant bearing on their underlying productivity and their benchmarked performance.

From TasNetworks' perspective, it is perhaps more salient that the draft report indicates that there was a significant increase in TasNetworks' productivity in 2017-18, and a continuation of the ongoing improvement which can be seen over the past five years. That TasNetworks has performed well against the AER's MTFP benchmark is also made noteworthy by the fact that the MTFP calculations were changed in 2017 in a way that, for the years prior to 2014-15, reduced TasNetworks' productivity to levels that were similar to the larger transmission network service providers which advocated for change in the benchmarking models. Prior to the change in methodology, TasNetworks had been assessed as clearly and consistently the best performing network since 2006.

Despite such a positive assessment of TasNetworks' transmission network in the draft 2019 annual benchmarking report, we continue to have reservations about the benchmarking models being used by the AER. The sensitivity of networks' productivity scores to different specifications of benchmarking model, as well as the significant variations in individual networks' performance between years, demonstrates why great caution needs to be exercised when publishing and interpreting raw benchmarking scores.

The often marked inter-year variations in network productivity also seem to suggest specification issues with the benchmarking models, given that many of the parameters that describe transmission networks and which might be expected to impact on network costs and efficiency, such as the number



of connection points and circuit length, have – in TasNetworks case, at least – changed very little since the first year benchmarked by the AER (2006). Operating expenditure for the Tasmanian transmission network was also quite stable over the benchmarked period, until it began decreasing after 2013-14. Yet despite this stability, TasNetworks’ productivity score often displays against-trend variations.

As we have noted previously, our concerns centre on the inputs and outputs that inform the productivity calculations. In particular, we continue to have concerns about the use of energy throughput and downstream customer numbers as measures of transmission network output.

Energy throughput

TasNetworks is not alone in experiencing significant fluctuations between years in the energy throughput of its network, a variable that impacts on network productivity scores yet is typically driven by factors that are beyond networks’ control. In Tasmania, for example, the on-island consumption of energy is entirely driven by customer load (which is often affected by climatic conditions), and while the consumption of power in Tasmania itself has been relatively stable in recent years, it has been in decline, which has an unavoidable negative impact on assessments of TasNetworks’ productivity.

In Tasmania’s case, fluctuations in energy throughput for the State’s transmission network are also driven by the trading of energy over the Basslink interconnector, which is essentially a function of the prevailing hydrological conditions in Tasmania and Hydro Tasmania’s trading strategies, rather than any factor within TasNetworks’ control. The dip in TasNetworks’ MTFP score that was observed in 2015-16 was largely a function of the prolonged outage of Basslink from 20 December 2015 to 14 June 2016, again something over which TasNetworks had not control but which impacted on the energy conveyed by Tasmania’s transmission network and TasNetworks’ productivity scores.

We note from the draft benchmarking report that improvements in total factor productivity made by AusNet in 2017-18 through a reduction in operating expenditure, which to most minds speaks of an improvement in a business’ efficiency, were entirely offset by a decline in energy throughput, and ElectraNet’s productivity deteriorated by 6 per cent due to a fall in energy throughput. Without knowing the exact reasons why these declines in energy throughput occurred, unless they were in some way attributable to the networks in question, it appears unreasonable to effectively hold them to account for a reduction in an output over which they have no control.

As we have contended before, there is an inherent risk associated with drawing inferences about productivity change on the basis of a variable which is subject to exogenous influences, something of which most users of the Report are unlikely to be aware. Noting that in Tasmania large industrial customers account for around 60 per cent of on-island electricity consumption, we are also conscious of the fact that the addition or loss of major industrial load in Tasmania could have a material impact on the way TasNetworks’ transmission network benchmarks, even though the addition or loss of load and the ensuing change in energy throughput will not be a function of TasNetworks’ performance.

If the amount of energy delivered by transmission networks is to remain as a measure of network output used in the AER’s benchmarking models, we are of the view that consideration should be given to the use of a ratcheted figure, in the same way that ratcheted demand is used as an measure of output, or at least a moving or weighted average measure of consumption that might smooth out annual variations in the volume of energy transported by a network, and provide for a better measure of the underlying productivity of networks over time.

Customer numbers

When the AER first proposed the substitution of end-user numbers for voltage-weighted number of connections as an output measure in its benchmarking models, the AER acknowledged that there was not wide-spread support for the concept. At the time the changes were being contemplated TasNetworks was one of the parties that argued against the use of downstream customer numbers and our position has not changed.

While the previous output measure of voltage-weighted connection numbers was not without its own shortcomings, replacing it with customer connections was not, in our view, a superior solution. While end-user customer connections are relevant to distribution network service providers because they are a driver of cost, TNSPs incur no costs when a new customer connects to the distribution network. They do, however, incur costs when providing access to generators, distributors and customers who connect directly to the transmission network, which the use of voltage-weighted connection numbers at least recognised.

The relevance of distribution customer numbers as an output measure for TasNetworks is even more questionable when you consider that four major industrial users use around half of the energy supplied by TasNetworks' transmission network between them. And throughout the benchmarking period assessed by the AER, the total number of entry and exit points supported by the Tasmanian transmission network has remained almost constant, increasing by just two to 82.

With most augmentation of the transmission network in Tasmania now being driven by the connection of new generation rather than new load customers or load growth, a focus on downstream customers also ignores the connection of generation as a driver of network costs and a measure of network productivity.

We remain of the view, therefore, that incorporating end-user numbers in the MTFP model does not capture important aspects of network scale and complexity, or represent an output that either correlates, or has a causal relationship with TNSP costs or productivity.

Lastly, we note that in the draft annual benchmarking report for *distribution* networks for 2019, the AER sets out plans for the ongoing development of its economic benchmarking, including a number of key issues that it intends consulting on during the coming twelve months. While there is no similar discussion of benchmarking development in the draft report for transmission networks, we note the AER's statement in the draft benchmarking report for transmission networks that MTFP analysis for transmission networks is still in a relatively early stage of development. We would, therefore, encourage the AER to consider the case for similar initiatives in the coming year in relation to the benchmarking methodology it applies to transmission networks and to engage with stakeholders about ways in which the benchmarking models might be improved. The small number of electricity transmission networks in Australia makes efficiency comparisons at an aggregate expenditure level arguably more difficult than it is for distribution networks, and TasNetworks would welcome the opportunity to work with the AER to refine its transmission network benchmarking, for the benefit of all users of the annual benchmarking reports.

Once again, thank you for the opportunity to comment on the AER's draft 2019 Annual Benchmarking Report for transmission network service providers. To discuss the views expressed in this submission, please contact Scott Lancaster, Senior Regulatory Analyst, on (03) 6271 6519 or at scott.lancaster@tasnetworks.com.au.

Yours sincerely



Chantal Hopwood
Leader Regulation