Government of South Australia

Hon. Patrick Conlon BA LLB (Hons) MP
Minister for Transport
Minister for Infrastructure
Minister for Energy

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AUST. COMPETITION & CONSUMER COMMISSION MELBOURNE
11 JAN 2006

Mr Steve Edwell
Chairperson
Australian Energy Regulator
GPO Box 520
MELBOURNE VIC 3001

Dear Mr Edwell

I refer to the Australian Energy Regulator's (AER) draft determination of 8 November 2005 regarding the conversion of Directlink from a Market Network Service Provider (MNSP) to a regulated network asset under the National Electricity Rules (Rules).

The AER's draft determination suggests that the AER, and its predecessor the Australian Competition and Consumer Commission (ACCC), have not learnt from past regulatory mistakes, in particular the decision to allow Murraylink Transmission Company (Murraylink) to convert from a MNSP to a regulated interconnector.

The South Australian Government strongly believes that the AER needs to give more consideration to the issue of whether a MNSP should be allowed to become a regulated network service provider pursuant to the safe harbour provisions set out in the Rules.

The safe harbour provisions were only ever intended as a safeguard against material changes in market structure or the Rules. The safe harbour provisions should not be used to protect investors who have made poor financial decisions, as was the case with the Murraylink conversion, which continues to provide little, if any, value to South Australian consumers.

As was highlighted in the South Australian Electricity Supply Industry Planning Council's (ESIPC) Annual Planning Report, during periods where South Australia and Victoria are approaching their peak loads, Murraylink does not contribute any capacity to the combined region nor provide any value to South Australia. This is likely to get worse over time with load growth increases across the region.

The ACCC's previous interpretation of the Code has created an avenue for corporate welfare and, if this error is repeated, will allow Directlink Joint Venture's inferior investment to elude the usual scrutiny that other regulated interconnectors have been subject to. Further, by allowing investors in MNSP's to have, in effect, an each way bet, the ACCC's and AER's decisions are likely to skew the flow of investment dollars toward speculative and unsound energy sector projects, rather than investment in

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assets that deliver real benefits to customers, as determined by the *ex ante* application of the regulatory test.

In addition, the 10-year regulatory reset period for Murraylink is completely out of place with established regulatory practice in Australia. This period is too long and prevents the revisiting of the regulatory asset base within a reasonable period, which is particularly egregious in this case where the benefits to customers over a 5-year period, for all intents and purposes, are likely to be negligible.

There is opportunity for the AER to correct the inappropriate precedent created by the ACCC's past deliberations. The AER should not repeat the same mistake with the conversion and valuation of Directlink that it made with Murraylink. In fact, the AER should consider reopening Murraylink's asset base to reflect its true value, which, from a South Australian perspective, thus far appears to be close to zero.

Yours sincerely

HON PATRICK CONLON MP
MINISTER FOR ENERGY

31 December 2005