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**Minister for Infrastructure**  
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**FAX TRANSMISSION COVER SHEET**

**Date:** 18 July 2003  
**To:** Mr Sebastian Roberts  
General Manager  
Regulatory Affairs - Electricity  
**Fax:** 03 9663 3699  
**Subject:** MURRAYLINK CONVERSION  
**Sender:** Brad Gay

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Dear Mr Roberts

As discussed, please find attached the South Australian Government submission on the Murraylink Transmission Company application for conversion to a prescribed service.

The hard copy will follow.

Regards

Brad Gay  
Ministerial Liaison Officer to the  
Minister for Energy

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Mr Sebastian Roberts  
General Manager  
Regulatory Affairs – Electricity  
ACCC  
GPO Box 520J  
MELBOURNE VIC 3001

Dear Mr Roberts

The ACCC has called for submissions from interested parties on the application from Murraylink Transmission Company (MTC) for conversion to a prescribed service. I am please to provide a submission on behalf the South Australian Government.

The submission provides comments on three areas of the process currently being conducted by the ACCC:

- The framework for the assessment and use of the "Safe Harbour" provisions;
- Costing of alternative projects; and
- Consistency with other electricity transmission regulatory decisions.

Framework for the assessment

The Government strongly believes that the ACCC needs to give more consideration to the issue of whether Murraylink should be a prescribed service, courtesy of the Safe Harbour provisions of the National Electricity Code (NEC). The Government considers that the Safe Harbour provisions of the NEC are only intended as a safeguard against material changes in market structure or rules. The Safe Harbour provisions should not be used to protect investors who make poor financial decisions. It is the Government's view that there has not been a material change in the market such that would warrant consideration of the Safe Harbour provision.

In addition, the Government is very concerned about the precedent that this will set for other prospective Market Network Service Providers (MNSPs). The Government remains concerned that the ACCC's current interpretation of the Code not only creates an avenue for corporate welfare, but also opens up the "back door" for MNSPs to seek conversion via this process and thereby circumvent the usual scrutiny that proposed regulated interconnectors, such as SNI, are subject to.

The ACCC should, in the South Australian Government's view, satisfy itself that there has been a material change in the market environment. In the absence of such a determination, the Safe Harbour provisions of the NEC should not apply.

#### Costing of alternative projects

As noted by several participants at the Adelaide Forum on this issue, the ACCC appears to have mistakenly decided that in order for any alternative projects to be considered, such projects must have similar technical specifications to the Murraylink asset.

Regrettably, the result of this decision will be that South Australian consumers will pay a premium for the poor choice of technology employed by Murraylink. In other words, the ACCC's assumption that Murraylink is the optimal solution is inappropriate. The ACCC must find the lowest cost and technically sound solution that meets all applicable regulatory requirements, without specific regard to the technical specifications of Murraylink.

Accordingly, the South Australian Government supports the removal of allowances for undergrounding, Phase Shifting Transformers (PSTs) and Static Var Compensators (SVCs) from the preferred alternative project, referred to as alternative 3. The South Australian Government has been advised that these items are not required and their removal would not effect the operation of the alternative transmission line within market rules.

The Government notes the correction to the Saha Energy International (SEIL) consulting report, which was used as the basis for the costing of alternative 3. It is understood that this correction has been issued due to an "arithmetic error" in relation to the double counting of allowances for profits and overheads and for interest during construction.

The table below utilises the corrected SEIL figures for alternative 3 without undergrounding. Pursuant to the technical advice that the Government has received, the PSTs and SVCs have been removed from the asset base. In addition, pursuant to advice from ElectraNet SA at the Adelaide Forum, the Monash substation connection assets have been reduced by \$4 million due to the dual role the substation performs.

The adjusted alternative 3 project costing is approximately \$77 million. As such, the Government considers that the starting asset base should be no more than \$77 million. This is consistent with the Preliminary View of the ACCC, corrected for the arithmetic error and unnecessary technical inclusions.

### Alternative 3 costings

	SEIL (26/05/2003) - without undergrounding
<b>Development costs</b>	<b>13,569</b>
Line Costs	28,620
Switchyard	58,572
<b>Total Construction costs</b>	<b>87,192</b>
Profits & O/heads	8,719
IDC	20,480
<b>Total Profits, Overheads &amp; IDC</b>	<b>29,199</b>
<b>Total (without undergrounding)</b>	<b>129,960</b>

### SA Government proposed adjustments

	<i>less</i>	
<i>Phase Shifting Transformers (1)</i>		(19,080)
<i>Static Var Compensators (2)</i>		(18,020)
<i>Reduction in Monash connection costs (3)</i>		(4,000)
<b>Adjusted due to reduced asset value (4)</b>		
	<i>less</i>	
<i>Profits &amp; Overheads</i>		(4,110)
<i>Interest During Construction</i>		(8,220)
<b>Corrected total (without undergrounding)</b>		<b>76,530</b>

(1) As per the ACCC Preliminary View, the PSTs are not considered to be required.

(2) ElectraNet SA (Adelaide Forum) indicated SVCs were not required. Advice from ESIPC has confirmed this.

(3) ElectraNet SA has advised the Monash substation plays a dual role, and thus should not be fully costed into the Murraylink asset base.

(4) Profits and Overheads have been adjusted to compensate for the reduced capital value.

This submission focuses on a high-level top-down approach to amending the alternative project discussed in the ACCC's Preliminary View, based on comments by ElectraNet SA and the South Australian Government's jurisdictional planning representative, the Electricity Supply Industry Planning Council (ESIPC) at the Adelaide Forum.

I note that in addition to this approach, the ESPIC has conducted a bottom-up analysis and has found that this figure represents an absolute upper limit to the asset value. Their analysis suggests that alternative projects in the order of \$50 million, excluding interest during construction and development costs, should be considered.

In any event, the South Australian Government suggests that the ACCC should give consideration to a mechanism, such as a technical forum, to facilitate discussion of the issues requiring further analysis and resolution. The South Australian Government believes that the technical experts should talk directly to resolve technical and modelling discrepancies, with facilitation by the ACCC, which could occur without detracting from the public consultation process.

### Consistency with other electricity transmission regulatory decisions

The South Australian Government strongly agrees with participants at the Adelaide Forum who indicated that this decision should not be a special case. As highlighted by TransGrid, Powerlink and ElectraNet SA, the asset valuation and Weighted Average Cost of Capital (WACC) suggested for Murraylink is significantly higher than for previous transmission pricing decisions of the ACCC. It is imperative that the ACCC maintain a consistent approach to regulation.

The Government can see no reason why the WACC included in the Preliminary View (8.45%) should be higher than that awarded by the ACCC to ElectraNet SA (8.30%). In any event, as Murraylink is only operating one asset which, once regulated, would operate with little or no market risk, the Government considers that the WACC awarded to Murraylink should be significantly less than that awarded, for example, to ElectraNet SA.

The Government also disagrees with the overly simplistic method the ACCC has adopted for assessing the operational expenses (OPEX) allowance. It is considered that benchmarking should be carried out to empirically determine a dollar value for OPEX that should be allowed, as opposed to the current suggestion of tying OPEX to asset value.

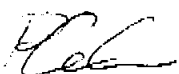
### Summary

In conclusion the Government strongly believes that the:

- ACCC should consider whether the Safe Harbour provisions are applicable in the absence of a material change in the market environment;
- Corrected valuation for alternative 3 of approximately \$77million, represents a value ceiling, other alternatives may reveal cheaper solutions;
- ACCC must apply a consistent approach towards transmission regulation; and
- ACCC should revisit its decision regarding the OPEX allowance and ensure that a dollar value is set empirically according to rigorous benchmarking.

On behalf of the SA Government I thank the ACCC for the opportunity to provide comment on this issue.

Yours sincerely



**HON PATRICK CONLON MP**  
**MINISTER FOR ENERGY**

/ 8 July 2003