

23 April 2004

Mr Sebastian Roberts  
General Manager  
Regulatory Affairs – Electricity  
Australian Competition and Consumer Commission  
GPO Box 520J  
Melbourne Vic 3001

Dear Sebastian

## **DRAFT DECISION**

### **REVIEW OF REGULATORY TEST FOR NETWORK AUGMENTATIONS**

SPI PowerNet is pleased to have the opportunity to provide comments in respect of the Commission's draft decision arising from its review of the Regulatory Test. SPI PowerNet has previously contributed to the Commission's consultation on this matter, most recently in response to the Commission's Discussion Paper in March 2003.

SPI PowerNet submits the following comments for consideration by the Commission:

#### **1. Definitional Changes – value of supply reliability**

SPI PowerNet concurs with the Commission's conclusion that "the principle of market efficiency would suggest that the value of VCR should be used to represent the true value of supply reliability", and accordingly supports amendment of the Regulatory Test to permit a value of customer reliability to be applied in determining market benefits.

However, SPI PowerNet is not convinced with the Commission's view that consideration from a competitive neutrality perspective "would suggest that the VoLL wholesale price cap be used". The Regulatory Test is a comparative test, requiring alternative projects, including generation options, to be assessed. For this purpose a consistent value would be used, ensuring competitive neutrality in the assessment.

The draft decision proposes that either value may be used as the measure for the value of customer reliability, together with the suggestion that the two values be applied in sensitivity analysis. For a Network Service Provider (NSP), in conducting the regulatory test, this approach appears acceptable, if not entirely unambiguous.

However, the draft decision does not provide any clarity as to the value for customer reliability that the ACCC will adopt in determining an ex-ante capital expenditure cap for TNSPs, which proposal is outlined in the Commission's supplementary paper

released with the draft decision<sup>1</sup>. Without clarification of this point there remains the possibility that the ex-ante capital provision will not be consistent with the TNSP's economically efficient network augmentation plan.

## **2. Use of Reliability Limb Vs Market Benefit Limb**

SPI PowerNet concurs with the Commission's conclusion that both limbs of the Regulatory Test should be maintained, on account of the obligations imposed by the National Electricity Code.

However SPI PowerNet wishes to reiterate its view that the apparent disparity in network investment that can be justified by the choice of limb applied to the test is inconsistent with the basis on which reliability standards have been established. The deterministic reliability standards were traditionally used as surrogate for the more complex analysis of benefits offered by a quantified value of reliability.

SPI PowerNet is satisfied with the philosophy of the market benefit limb, however, the company's view is that the implementation of market benefits in some instances has contained imperfections that may have lead to an undervaluing of transmission augmentation under the market benefit limb. Uncertainty regarding treatment of the value of reliability (refer item 1 above) is a particular concern, and SPI PowerNet is concerned that other potential benefits of augmentation may also be omitted from the economic analysis.

## **3. Competition Benefits**

In SPI PowerNet's view the consideration of competition benefits is moving in the right direction. SPI PowerNet agrees that benefits of increased competition arise from transmission augmentation. As economic benefits these exist to the extent that the combined producer/consumer surplus has been increased on account of the augmentation.

In its submission in response to the Commission's Discussion Paper, SPI PowerNet expressed the view that the estimation of competition benefits is extremely subjective, and heavily dependent on assumptions. Accordingly SPI PowerNet supports the Commission's proposal to conduct further research into the derivation of competition benefits.

In the meantime there remains an absence of developed and accepted principles for the simulation of market outcomes in response to increased competition. Therefore, SPI PowerNet recommends that a high degree of transparency should be provided in respect of the determination of competition benefits in applying the Regulatory Test. Assessment by stakeholders of the claimed benefits, and comparative assessment of differing views on the level of benefit, would otherwise be problematic.

## **4. Concluding Remarks**

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<sup>1</sup> Supplementary Discussion Paper, Review of the Draft Statement of Principles for the Regulation of Transmission Revenues, Capital Expenditure Framework, 10 March 2004

SPI PowerNet supports the basic design of the regulatory test and, in accordance with this letter, amendments proposed in the draft decision. However, SPI PowerNet considers that confidence in the objectiveness of the test would benefit from further work to establish the full economic benefit of augmentation to achieve a better alignment between the outcomes that arise from the market benefit limb with the reliability limb. Improved confidence in the ability of the market benefit test to deliver the appropriate level of investment is necessary.

I would be pleased for you to contact me if you would like to discuss the views submitted in this letter.

Yours sincerely

*(Letter sent by electronic mail)*

CHARLES POPPLE

**GENERAL MANAGER COMMERCIAL**