

TEMCO submission to the ACCC on the Draft decision on Tasmanian Network Revenue Cap 2004 – 2008/9

Capex Claw back provisions

1) The draft determination provides for substantial increases in both Opex and Capex. Customers have expressed the view that they are satisfied with existing quality of service levels including reliability. Customers want a steady as she goes approach to infrastructure development with continued refurbishment to maintain the existing quality of service supplemented by judicious development capex where a demonstrated longer term benefit to transmission costs can be shared between Transend shareholders and customers alike.

- a) Clearly the Transend application while acknowledging capex alternatives such as load/ demand side management is very much focused on expanding traditional infrastructure (Transend appear much more comfortable with this type of approach and appear unwilling to give due regard to alternatives e.g. to substitute cheaper Hydro Tasmania alternatives like the mooted gas fired generation in the Hobart area for their own preferred high cost Southern Augmentation.)

It should be noted that GHD supported the Transend proposal for the Southern Augmentation on the basis that the ACCC has a claw back mechanism. This indicates that even the “fixed “ capital built into the revenue cap is has a level of uncertainty in the deliberations of the ACCCs own consultants.

It is TEMCO’s submission that the Transend view on all developmental and renewal capital (both fixed and variable) is too narrowly focused and relies on a traditional more expensive option rather than less costly options from demand or load side management and other innovative measures.

- b) All submissions to the draft suggest minimal load growth in Tasmania. As a major consumer of electricity it is interesting to note that no one has sought TEMCO’s views on our future plans including continued operation in Tasmania.. TEMCO’s ROCE for recent years has been Has the ACCC factored in the probability of more than one of the MEG customers leaving the state in the regulatory period? Has negative load growth as a result of either increased electricity transmission costs or other factors been considered?

It is TEMCO’s submission that a “minimal load growth “ assumption may be optimistic.

- c) Competition also involves competition for cash and investment. In the business environment companies compete for cash and investment funds on the basis that their capital expenditure will increase cash flow / profits via increased activity or more efficient operations that reduce unit costs. There is no element of reduced unit costs (opex per MW transmitted) flowing from Transends capital program.

It is TEMCO's submission that the capex programs fails to adequately replicate the pressures/ drivers that exist in a competitive environment. Even in an environment such as the ACCC regulation of Transend monopoly power the draft capital expenditure proposed fails any surrogate competitive test.

Points 1 a, b and c indicate that the Draft Capex submitted by Transend and moderated by the ACCC remains optimistic (ambit) in achievement and lacking in rigor from a capital cost efficiency stand point.

In view of the above we strongly support the retention of the claw back provisions proposed under the ACCC draft determination. It appears to be the only control for consumers to prevent Transend from simply increasing its own revenue stream by not meeting its capital program.

If Transend is serious in its claim that it will meet the draft approved Capex plan and its Capex plan is efficient it would not be opposing the claw back provision!

Impact on Opex of Hydro Tasmania presentation to ACCC draft determination

Hydro Tasmania in its response to the draft determination acknowledged that the increase in Transend charges by their magnitude would be a disincentive for energy use. It proposed that depreciation on assets be manipulated to defer the impact until later years thus reducing the " shock" of the massive increases in Transend charges in the early years by using a depreciation method for Transend assets known as "competition depreciation".

This proposition encourages current Transend management to abrogate their fiduciary duties.

Transend could be encouraged to increase capex further in the knowledge that the flow on depreciation charge would hit future consumers and they would not be as accountable to current consumers.

Transend assets typically 30 yrs +useful life. Transend assets by their very nature provide similar benefit to customers in early years of use to later years of use. On this basis current consumers should pay the same as future consumers for use of these assets. This will not occur if the Hydro submission on depreciation is adopted.

Accounting Standards AASB 1021 provides an authoritative commentary on determination of depreciation charges.

Depreciation should correspond “to the pattern expected in exhaustion of the assets service potential.”

“ The straight line method is a means of determining systematic depreciation charges ...commonly adopted because of its simplicity “ “ the bases for calculating depreciation charges need to be selected with proper regard for the underlying facts, but which ever basis is selected, it is essential that it be applied consistently, from financial period to financial period depending neither on the profit or loss for any one financial period.....”

It is Temco’s submission that competition depreciation does not meet these criteria, is complex and does not match cost with benefit or provide any incentive for Transend management to optimize its capital program.

Connection and Augmentation Costs Wind farms and Basslink

In regard to connection of new generators and inter –connectors (jointly referred to as generators) into the Existing Network it is clear that the code aims to have the direct cost of connection for new generation funded by the generator. **TEMCO supports this rationale.**

In respect of Augmentation of the existing Network to facilitate new generators connections it is also the aim of the code to ensure the generator funds augmentation. In particular where new generation because of the lumpy nature of its supply load requires existing network upgrades to handle resulting peaks in load such augmentation clearly has a direct link to benefits enjoyed by the generator and not the consumer. Determination of whether augmentation costs should be funded by generator or jointly funded by consumers rests with Transend but is of course subject to the regulatory test.

During the Transend Revenue Cap determination process Transend has consistently refused to provide any detailed information to consumers or other parties (e.g. no detailed historical Transend Opex or Capex data was provided).

Furthermore at a recent Treasury briefing in Launceston Transend opposed to the principal of charging a single party for existing network augmentation.

In their view such an approach is a disincentive for long-term infrastructure investment.

It is TEMCO’s submission that the ACCC should impose an obligation on Transend to provide the RNPP with detailed historical information sufficient to enable the RNPP to make an informed judgment on the funding of all augmentation projects put before it.

Opex Efficiencies

The ACCC draft predicts low growth for transmission services and allows massively increased Opex and Capex yet only maintains existing levels of reliability. This does not

constitute “ The ACCC imposing a severe stretch target in terms of operating cost reductions “as suggested in Transend’s concerns with the ACCC draft.

Under the draft determination Transmission costs per MW delivered may rise by 58% over the 5 year regulatory period.

Transend states that it has factored in efficiency gains into its forecasts for the regulatory period however did not state how these efficiencies occur.

GHD were unable to quantify the effects of these efficiencies.

It is TEMCO’s submission that if Transend is unable or unwilling to share information on its efficient costs and the ACCC consultants GHD were unable verify the efficiency of expenditure then at very least the ACCC should provide Transend with some guidance on the type of information it will require in addition to the proposed performance measures and financial incentive to specifically demonstrate efficient costs for future periods.