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Dear Sir

Powerlink Queensland Revenue Cap Application – Feb 2001

I refer to the application from Powerlink Queensland to the ACCC for a determination of their transmission network revenue cap commencing Jan 2002. I also note the assessment of this application by PB Associates.

In general, TransGrid is supportive of the approach taken by Powerlink in its application. This letter sets out our specific comments as follows.

1. <u>Asset Valuation</u>: We note the position taken by experts at recent ACCC conferences supporting the principles of Optimised Depreciated Replacement Costs (ODRC) for valuing assets of regulated businesses. We also note the general support of these principles in the ACCC's draft Statement of Regulatory Principles document.

   In this context, we are surprised by the approach adopted by PB Associates regarding indexation to be applied to the Powerlink asset values (Section 5.1.3) previously set on an independent basis. In TransGrid's view it is not sufficient to dismiss Powerlink's indexation percentages without providing a soundly based alternative. Under ODRC principles a default indexation of zero is not justified. We also encourage the ACCC to reconsider its position not to adopt an ODRC valuation for easements. In principle the economic arguments for use of ODRC for other assets apply equally to easement valuation.

2. <u>Regulated Rates of Return</u>: We are concerned that the target return on equity of 13.97% sought by Powerlink is too low. We note in particular, the comments by the Productivity Commission in their recent Position Paper entitled "Review of the National Access Regime" that, in terms of public benefit, it is more desirable that investment in infrastructure proceed than it is to eliminate all elements of excessive returns to the owners of these assets (refer Chapter 3 and page 207).

   We also believe that the ACCC has yet to fully integrate the effects of asymmetric risks into its assessment of regulated returns. While we acknowledge that the pass through of increases in insurance costs partly addresses this issue, we do not believe that either optimisation risk or regulatory risk is fully compensated for in current levels of regulated return. This is particularly true given the long life of transmission investments, the relative immaturity of transmission regulation in Australia (principles are yet to be finalised), and legal limitations on the ACCC establishing binding precedent on future decisions of the ACCC. In this context it is worth noting the risks identified by the Productivity Commission's Position Paper on page 58.

3. Service Standards: Based on our experience with transmission service provision over many years, we would endorse Powerlink's comments on the need to apply statistical analysis to supplement targets set for transmission service performance. Indeed, the most valuable measures are often those developed by transmission businesses over time that, although not directly reflective of customer impact, provide worthwhile 'leading indicators' of future service performance.

   TransGrid's position on the development of transmission service obligations was set out in its response to the ACCC's draft determination on Transmission and Distribution Pricing and Market Service Network Providers. In essence, TransGrid believes that transmission service obligations and supporting measures should be set out in the National Electricity Code. Actual performance targets should be determined as part of the revenue reset process involving the ACCC and the respective TNSP. In this way a disciplined approach to changes in transmission service obligations is maintained through the Code change process, while allowing for variations in targets across the areas serviced by individual TNSP's.

   We also strongly endorse Powerlink's comments that TNSP's should only be held accountable for areas of performance over which they have control. In this regard, the influence of NEMMCO decisions on transmission capability needs to be fully recognised. In addition there is a fundamental link between the ability of transmission companies to make planning and investment decisions, and their ability to control service levels.

4. Mid term Revenue Adjustments: While TransGrid acknowledges the potential need for adjustments to be made to Powerlink's revenue during a reset period a cautious approach is recommended having regard for the need to develop a light handed incentive based regulatory framework. Having said this, it is conceded that it may be appropriate to make specific mid term revenue adjustments. As noted by TransGrid in its submission to the ACCC in response to the ACCC's draft Transmission and Distribution Pricing and Market Network Service Provider determination, there should be scope for specific adjustments to a TNSP's revenue cap when Code-changes introduce new service obligations on TNSP's.

5. Benchmarking Transmission Performance: TransGrid would concur with Powerlink's view that fundamental differences between transmission systems makes meaningful comparison of aggregate performance challenging. In TransGrid's case, for example, TransGrid's network has been the major part of a three State interconnection for over a decade and part of the system serving the most developed and industrialised States in Australia for much longer. Indeed, the two largest cities in Australia are served by this system. This has resulted in high service level requirements and unique challenges coordinating maintenance outages that impact on interconnected system security.

I trust that these comments will assist the Commission in developing a draft revenue determination for Powerlink that provides the incentives required for efficient transmission service delivery and recognises the legitimate commercial needs of Powerlink.

Yours sincerely

Philip Gall
Manager / Regulatory Affairs