

**PRESENTATION TO THE ACCC PRE-DETERMINATION  
CONFERENCE ON TRANSGRID'S DRAFT 2004-2009  
REVENUE CAP DETERMINATION –  
JOHN BYRNE ON BEHALF OF TRANSGRID**

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**ACCC PRE-DETERMINATION  
CONFERENCE ON  
TRANSGRID'S DRAFT  
2004-2009 REVENUE CAP  
DETERMINATION**

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Mr Chairman, I would like to make a few closing remarks in reference to TransGrid's submission and the subsequent Draft Determination.

I have found the various presentation of value and tend to agree with the majority of sentiments expressed.

However, there is a point I would like to make in regards to earlier presentations:

§ A number of the presentations use data which does not reflect TransGrid's acquisition of the Snowy Mountains Hydro Electric Authority transmission assets in 2002. Inclusion of the revenue determination in relation to these assets, significantly change past and future figures.

David Croft has earlier expressed the major issues of concern to TransGrid in the Draft Decision. The focus of my presentation is the level of Operating Expenditure proposed and the risks TransGrid faces in having its revenue determination occur at the same time the Commission is reviewing the regulatory principles which underlie the determination.

## § **Operating Expenditure**

The Commission in its Draft Determination has examined TransGrid's Performance over a ten year period – the five years covered by the current determination and the proposals in regard to the next five years to be covered by the draft determination being debated.

## **Assets**

- **Opening Assets – Jul 1999 - \$1,934 million**
- **Opening Assets – Jul 2004 - \$2,923 million**
- **Closing Assets - Jun 2009 - \$4,081 million**
- **Over 10 year period under review, assets double.**



Over that time period, TransGrid's Asset Base will increase from just under \$2 billion to just over \$4 billion ... effectively a doubling in the value of assets TransGrid will be required to maintain.

## Operating Expenditure

- **ACCC Allowance – 1999/00 - \$101 million**
- **ACCC Allowance – 2004/05 - \$118 million**
- **ACCC Allowance – 2008/09 - \$125 million**
- **Over period under review, opex allowance increases only 24%.**
- **CPI Increase 10 year period – 32%**



Over the same ten year period, TransGrid Operating Expenditure allowed by the ACCC will increase from \$101 million in 1999/00 (the first year of the current revenue period) to \$125 million in 2008/09 (the last year of the next revenue period).

This represents an increase of only 24% in nominal terms and a reduction in real terms. This in a period where the asset base doubles in value.

While the Commission may not be “convinced by TransGrid’s assertion on the direct proportionality between aggregate investment and the efficient level of operating and maintenance expenditure”<sup>1</sup>, it must recognize that at some stage, increased assets under management must lead to some proportion of increased costs.

TransGrid agrees that new technology and process changes should result in productivity and efficiency gains. However, to expect operational costs can continue to be cut without some eventual effect of service standards is naive.

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<sup>1</sup> NSW and ACT Transmission Network Revenue Caps – TransGrid 2004/05 – 2008/09 – Draft Decision – 28 April 2004 – Page 30.

As explained to the Commission and its advisors during their review, technology changes bring with it other costs such as the need for new skills training. It also requires higher paid technical staff with the skills and competencies to operate and maintain this equipment.

The Electricity Market has also increased the complexity of running a transmission system, requiring highly skilled technical staff. Increased environmental and safety standards result in the need for higher paid specialist staff and place significant constraints on process improvement options.

There is a need for all these factors to be considered when assessing the relationship between asset growth and efficiency objectives.

## § **Cost Comparisons**

The Draft Determination proposes an efficiency target and uses other organisations to justify the proposal. Comparisons with National Grid and their efficiency targets seem a little out of place, particularly in light of their significantly different business models to any Australian TNSP and their focus on other energy forms and acquisitions.

The credibility of that particular comparison is of doubtful use, especially when National Grid's revenue from Transmission Operations in the UK is eight times TransGrid's revenue for delivering only four times as much electricity, indicating they are notionally twice as expensive as TransGrid<sup>2</sup>.

This demonstrates how notoriously difficult international comparisons are to make and how inappropriate Operating Expenditure comparisons like this are to make as noted previously by the Commission.

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<sup>2</sup> National Grid Annual Report 2002/2003, TransGrid Annual Report 2002/2003.

## § **Statement of Regulatory Principles**

### **Transparency of Process**

- **TransGrid's original Revenue Determination**
  - **Draft Determination – 12<sup>th</sup> May 1999**
  - **Draft Regulatory Principles – 27<sup>th</sup> May 1999**
- **Current Determination occurring under similar conditions**
- **Need for clear rules and processes to be defined**



For TransGrid, the manner in which the regulatory review process is occurring is of concern. In 1999, TransGrid was the first transmission organisation to enter the current regulatory regime. The regulatory rules for the regime were being developed at the same time, requiring TransGrid to submit its Revenue Request in a policy vacuum, leading to what TransGrid still views as a sub-optimal outcome. In fact, the Draft Regulatory Principles on which the determination was based were not issued until after TransGrid's 1999 Draft Determination had been released.

The Regulatory Principles are now being reviewed and TransGrid's Revenue Determination is occurring again in a period of significant uncertainty. It took some time before the guidelines for reviewing TransGrid's past performance to be clarified.

The Draft Determination claims that TransGrid has not been able to justify certain outcomes. This is almost certainly due to the lack of clear templates and guidelines associated with the provision of information. This must have

been a significant factor impeding the Commission's review of TransGrid's operations.

It is pleasing to note on this occasion that the Commission have partially recognised this issue and allowed TransGrid the opportunity to revise its future capital expenditure proposals in the light of the changing regulatory environment. A similar request was rejected in 1999 which I believe has led to some of the problems in the current review of past capital expenditure.

## Transparency of Process

- **Changes to TransGrid submission on costs without explanation in Draft Determination**
- **Example – Insurance**
  - **Insurance premiums paid**
    - 2002/03     \$5.02 million
    - 2003/04     \$5.23 million
  - **OPEX Allowance reduced to**
    - 2002/03     \$3.55 million
    - 2003/04     \$3.63 million
  - **No explanation in Draft Decision**
- **Other aspects not yet clarified such as Self-Insurance; Insurance Deductibles; etc.**



As part of the Commission's current review of TransGrid, a large amount of information has been provided, some of which appears to have been misinterpreted. For example, TransGrid's insurance costs in 2002/03 were \$5.02 million and in 2003/04, \$5.23 million. However, in the Draft Determination, the starting point for allowable insurance costs has been cut to \$3.55 million in 2002/03 and \$3.63 million in 2003/04. Reasons for this reduction are not explained in the Draft Decision.

Similarly, the Commission's thinking on other aspects of insurance are not clarified such as the treatment of Self Insurance costs and treatment of insurance deductibles.

This creates a significant risk for TransGrid in trying to respond to an issue on which clear guidelines are yet to be formulated.

## Transparency of Process

- **Difficult to provide clarification or corrections when underlying issues not understood**
- **Need for Commission to clearly define information requirements in TNSP Submissions (including format of data to be presented)**
- **Should be a key outcome of the current review of the Regulatory Principles**



In the development of the revised Statement of Regulatory Principles, it is imperative that the Commission clearly define its information requirements not simply the high level principles for TNSP regulation. The Principles should include definitions and templates of the Commission's information requirements. The TNSPs should be provided with decisions in a similar format so that any changes made by the Commission in its deliberations can be identified and lead to meaningful discussions on the reasons for such changes.

This would provide greater clarity in decisions and provide a better understanding of issues such as the treatment of pass-throughs and abnormal events.

For our part, TransGrid recognises the need for clear and detailed information to be provided to the Commission so that complex issues associated with the organisation's operations can be understood and properly evaluated.

TransGrid's written response to the Draft Determination will be aimed at clarifying the information needed by the Commission to make a considered final decision.