Our ref: D05/4546

TRANSEND

14 February 2005

Mr Sebastian Roberts
General Manager
Regulatory Affairs – Electricity
By email

Dear Sebastian

TransGrid capital expenditure report

Transend Networks Pty Ltd ('Transend') welcomes the opportunity to comment on the Parsons Brinckerhoff Associates ('PB Associates') review of TransGrid's proposed capital expenditure program, submitted for the forthcoming regulatory period. Transend's interest in the PB Associates review is limited to its possible impact on the ACCC's approach to excluded project arrangements.

PB Associates has concluded that nearly half the value of its recommended capital expenditure allowance for TransGrid should be excluded from the ex ante cap. The dollar value of PB Associates' recommendation for excluded projects is $931m over the regulatory period. This represents a very considerable level of exclusions, and some 50% higher than the level proposed by TransGrid.

Transend notes that the ACCC's Statement of Regulatory Principles ('SRP') describes the process by which projects could be treated as excluded. In particular, the SRP states on pages 11 and 12:

> The ACCC proposes to exclude a project from the main ex ante capex allowance if the expected error presented by the inclusion of that project in the main allowance— quantified in terms of the revenue required to cover depreciation and the return on investment in that project—is equal to more than 10 per cent of the revenue required to cover depreciation and return on investment of all projects included in the calculation of the main ex ante capex allowance.
>
> The TNSP can apply to the ACCC for specific projects to be excluded from the ex ante allowance, even where this value threshold is not satisfied. It will be at the ACCC's discretion as to whether these projects will be considered as excluded projects.

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> Projects excluded from the ex ante capex allowance must be linked to unique investment drivers—such as a major point load or expected power station—rather than to general investment drivers (such as expectations of load growth within a region).
>
> Determination of the allowed investment in excluded projects will occur during the regulatory period, once the probability of the project and its expected costs become known with greater certainty, but before investment is committed.
>
> At the end of the excluded project incentive period the depreciated value of the actual investment in the excluded project that complies with the requirements of the code will be included in the RAB.

Transend's reading of the PB Associates report is that the consultant is developing its own criteria and approach for determining the quantum of excluded projects. It does not appear that PB Associates has given due consideration to the SRP in drafting its report or that its approach is consistent with the SRP.

You will appreciate that as the SRP has now been finalised after a considerable period of time, interested parties rightly expect that it will now be applied. Transend is concerned that regulatory practice is already diverging from the ACCC's own principles, and that regulatory precedents will be set and applied in this way.

Implications

Transend notes that the ACCC's principles do not outline how the excluded project regime will work. Given the number of projects excluded from TransGrid's allowance by PB Associates, and the high probability that this, as yet unknown, regime will be applied to TransGrid for a number of these projects, Transend is concerned that the revenue cap decision may introduce an unacceptable level of regulatory risk for TransGrid, and for transmission companies generally.

For TransGrid, there is the risk of 'regulation on the run' and potential significant delays in gaining regulatory approvals for excluded projects. For transmission companies and other stakeholders generally, there is the risk that TransGrid's arrangements may set inappropriate precedents for the excluded project arrangements for other transmission companies.

Transend therefore seeks assurance from the ACCC that any excluded project arrangements that the ACCC reaches in consultation with TransGrid, will not automatically form the basis of excluded project arrangements applicable to other transmission companies.

Transend has previously raised concerns that regulatory practice has not followed the agreed principles, and that this undermines the value of setting principles in the first instance. Transend urges the ACCC to ensure that the TransGrid review follows the SRP – and that any divergence is properly and fully explained in the ACCC's decision. Transend also seeks further consultation in development of the detailed application of the SRP, including excluded project arrangements.

Please contact me directly on 03 6274 3909 if you would like to discuss any of the points raised in this letter in more detail.

Yours sincerely

[by email]

Bess Clark
Manager Business Planning, Regulation and Compliance