Contact: Dave Roberts
Tel: (03) 6233 8988 Fax: (03) 6233 5646
Our Ref:

Mr M Rawstron
General Manager Regulatory Affairs - Electricity
Australian Competition and Consumer Commission
PO Box 1199
DICKSON ACT 2602

Dear Michael

APPLICATION FOR AUTHORISATION/APPROVAL OF PROPOSED CODE CHANGES

On behalf of the Tasmanian Government, the Basslink Development Board ('the Board') is facilitating the development of Basslink as a Build Own Operate (BOO) interconnector project within the framework of the National Electricity Market.

As such it has taken a keen interest in the regulatory framework for interconnectors as set down in the National Electricity Code, through participation in Working Group activities and submissions to NECA (and ACCC) regarding proposed Code changes.

The Board is relieved that the Code changes for Non-regulated Interconnectors and those associated with the Transmission and Distribution Pricing Review, as well as the Regulatory Test for New Interconnectors have now been finalised and submitted to ACCC, albeit much later than originally anticipated.

Throughout the process of developing the principles and Code changes, the Board's overriding concern has been to establish a clear regulatory environment which would allow entrepreneurial (BOO) interconnectors to be developed on a level playing field.

We believe that such an environment has now been established in regard to the provisions dealing with non regulated interconnectors connected to regional transmission networks, but only if the arrangements relating to liability for TUOS usage charges remain as drafted in the current version of the Code changes before ACCC (refer clause 5.5A(g)(2)).

However, in regard to the proposed arrangements relating to regulated interconnectors, we do not believe that such an environment has been established.

Our comments on this issue and other issues arising from the proposed Code changes are set out in the attached submission.

As you will note in our submission, we are concerned about the complexity of the Code provisions which are now proposed to apply to Transmission Network Pricing under Chapter 6 of the Code.

If it is possible to review these provisions so that their intent and application is clearer we believe that this should be done prior to their approval as an access regime.

The provisions in the Code relating to the revenue streams for regulated interconnectors with no transmission customers of their own (such as Basslink), should also be reviewed to ensure that they are transparent and commercially workable.

However, whatever decision is made in regard to the provisions relating to Transmission Pricing and regulated interconnectors, the Board requests that ACCC grant approval to the Code provisions giving effect to the arrangements for non-regulated interconnectors as soon as possible. These provisions are included in proposed changes to chapters 2, 3, 4, 5, 7 & 10 but are also covered in a number of references to network charges for Market Network Service Providers throughout Chapter 6.

Proponents will be submitting their proposals for Basslink on 14 October 1999. As it stands this is now likely to be prior to a draft determination by ACCC on the proposed Code changes.

In order for the Board to carry out its evaluation and for the shortlisted proponents to establish agreements with the various parties involved, all unnecessary regulatory uncertainty surrounding the framework for interconnectors in the NEC must be removed. This can only be done by an ACCC determination at the earliest possible date.

Yours sincerely

Chris Gillies
Director Basslink Development

17 September 1999

Basslink Development Board

Submission to the Australian Competition and Consumer Commission - 17 September 1999

NECA Proposed Changes to the National Electricity Code

1. Introduction

As indicated in NECA's covering letter to ACCC, the proposed code changes submitted for authorisation/approval on 19 August 1999 include code changes developed under two separate processes. These were:-

- the establishment of rules for non regulated interconnectors
- the Transmission and Distribution Pricing Review

The Basslink Development Board ('the Board') actively supported the first of these processes through involvement in the NECA Working Group which developed the safe harbour provisions and the associated code changes for non regulated interconnectors. This was done on the basis that the Code did not originally allow for the development of non regulated interconnectors and if such options could be anticipated for Basslink, the relevant Code provisions needed to be in place.

On the other hand the Code previously provided for regulated interconnectors to be developed and defined the mechanism under which the owner of a regulated interconnector would receive an appropriate level of revenue to support the development of a regulated interconnector. Hence, while the Board still took an interest in the Transmission and Distribution Pricing Review, it did not play an active role in the process.

The only major issues at stake for Basslink as a regulated interconnector were considered to be the Regulatory Test and the process for approval of new interconnectors. These were handled outside the Transmission and Distribution Pricing Review in any case.

NECA has sought to bring together the results of the two processes outlined above in the code changes submitted to ACCC for authorisation and approval. The Board supported this concept in principle as the resultant code changes could be presented as a complete package. However we believe that the somewhat different drivers for the two processes may have resulted in proposals which are not necessarily consistent.

Without going into detail we believe that the key drivers for the non regulated interconnector process were aimed at developing arrangements which would allow the development of new interconnectors on an entrepreneurial basis without intervention by regulators or central planning bodies. (Directlink provides a good example of this) In contrast the Transmission and Distribution Pricing Review was driven more by considerations of revenue recovery and equity in terms of who should pay regulated network charges, particularly those associated with new investment.

It should have been possible to achieve arrangements from the Transmission and Distribution Pricing Review whereby new regulated interconnectors could be developed on an entrepreneurial basis but such arrangements may be difficult to reconcile with equity considerations.

The Board's comments are provided in the above context. In providing these comments the Board's primary concern is the establishment of a framework expressed in the Code for new interconnector projects under which:-

- the benefits can be recognised and realised by developers and market participants alike;
- all suitably qualified parties can participate in the development on a level playing field:

These objectives are vital for successful implementation of any new interconnectors on an entrepreneurial BOO basis.

3. Non Regulated Interconnector Issues

The main issues for the Board associated with the code changes for non regulated interconnectors deal with the following issues:-

- Liability for TUOS charges; and
- Access undertaking:

3.1 Liability for TUOS charges

In considering this issue there are two ways in which a non regulated interconnector can be viewed. These are:-

(a) as a generator and/or customer in each of the interconnected regions; or

(b) as a transmission element which derives its revenue from operating in the market:

While the first approach may be attractive from the viewpoint of equity considerations, particularly when considering other participants in a region, it does not necessarily encourage economic decision making.

Economic decision making should be guided by market participants recognising the potential benefits of a new interconnector through the prospective market impacts and being prepared to enter into arrangements which support the establishment of the new interconnector. Alternatively a developer could choose to capture the market benefits by trading between the two regions on an entrepreneurial basis.

When the original terminology, which referred to non regulated interconnectors, was changed to Market Network Service Providers ('MNSPs') we believe this was acknowledgment of the appropriate role for such entities.

In order to encourage economic decision making it should be up to the interconnector developer to choose what degree of access is needed from/to the interconnected regions and negotiate appropriate arrangements with the relevant Network Service Provider(s). This could involve either paying for new augmentations in which case similar levels of access as for existing generators and customers could be expected. Alternatively a lower level of access might be acceptable in which case the developer might be constrained off during some operating conditions in favour of other customers or generators.

Regardless as to which of these approaches is adopted the payment of TUOS charges should be a matter for fair and reasonable negotiation between the developer and the relevant NSP based on the marginal cost and value of transmission at the relevant connection points.

This was the approach agreed by the Working Group for Entrepreneurial Interconnectors and is generally consistent with the provisions in Clauses 6.4.3 and 5.5A of the code changes now before ACCC.

Market Network Service Providers should only be liable for paying three aspects of connection and transmission costs:

- 'shallow connection costs' (ie the equivalent of entry and exit charges);
- 'negotiated use of system charges' which reflect both the benefits and costs associated with the impact of the MNSP project on the incumbent NSP networks (see draft clause 5.5 A (g) (2));
- amounts agreed with incumbent NSPs associated with the provision of 'market network service provider access' (ie 'firm access' arrangements to be negotiated within interconnected NSPs in the same way that generators may undertake such negotiations).

In no circumstances should an incumbent NSP be able to charge a MNSP for 'Common Service Charges', 'Customer TUOS Usage Charges', 'Customer TUOS General Charges' or 'Generator TUOS Charges' as those terms are defined in the draft code changes. Allowing recovery of any of these charges from an MNSP, as proposed in the code changes submitted to ACCC earlier in July 1999, would constitute discriminatory treatment vis-a-vis regulated interconnectors and in our view, would not create efficient economic signals or achieve the goal of a level playing field.

Since Clause 6.7.4(c)(2) still appears to support charging of TUOS Usage Charges and Common Services Charges to MNSPs we have some concerns as to what the actual intention is.

3.2 Access Undertaking

Under Chapter 5 of the Code, the developer of a non regulated interconnector is required to lodge an access undertaking with ACCC. The pro-forma access undertaking in Schedule 5.8 includes a commitment to abide by the Code but it is understood that other provisions could be required by ACCC.

It is the Board's view that competition law/market power issues are best dealt with under the existing provisions of Part IV of the Trade Practices Act 1973 (ie section 46 - Misuse of Market Power, section 45 - Arrangements and Understandings Which Affect Competition and section 50 - Mergers and Acquisitions which Substantially Lessen Competition).

The Board understands the possible need for other provisions (eg access pricing) in an access undertaking where there may be a risk of market power in the upstream or downstream markets (eg gas pipelines). However, in general, electrical interconnectors will be connecting between competitive energy market regions where there is little opportunity to levy excessive charges for transport services.

A requirement by ACCC to include pricing constraints in an access undertaking, which might translate into bidding limits for a MNSP and/or limits on premiums for inter regional hedge contracts, could potentially reduce the value of such an interconnector and therefore discourage its development.

We believe there should now be regulatory clarity on this issue from ACCC by establishment of a pro-forma access undertaking suitable for a non-regulated interconnectors and incorporation in the NEC.

4. Transmission and Distribution Pricing Review

One of the guiding principles for the Transmission and Distribution Pricing Review was that beneficiaries pay for the cost of new investment. As noted above, the Board supports this principle. The arrangements outlined in Chapter 6 (Refer Schedule 6.8) appear to provide for this, at least as far as generators are concerned.

The approach adopted to allocate costs to beneficiaries in Chapter 6 is deterministic and there may not be any other option under the present circumstances. However the approach has been complicated further by the specification of three different methods by which the costs for customers (distributed via TUOS usage charges) can be calculated (Refer Schedule 6.4), apparently at the TNSPs discretion (Refer Clause 6.4.3B (c)).

The long run marginal cost approach outlined in Schedule 6.4 should give some indication as to the marginal cost of transmission. This should be the correct economic basis for beneficiaries to pay however this calculation is very difficult in practice because it requires assumptions about future patterns of load and generation. In any event this approach will obviously cause problems at locations where existing transmission is adequate and no augmentations are necessary in the foreseeable future. Therefore there is a need for recovery of the remainder of the sunk costs for shared network assets through the TUOS general charge.

The arrangements outlined in Chapter 6 (Clauses 6.3.4 to 6.5.9 and Schedules 6.4 & 6.8) are now oriented towards transmission pricing on a regional basis. Hence the sunk costs are also recovered on a regional basis. There are provisions in Clauses 6.7.3 & 6.7.4 as well as Schedule 6.8 which attempt to resolve the arrangements between regions. In general, it appears that the intention is not to transfer sunk costs between regions through TUOS general charges but there seems to be some inconsistency between the arrangements described in the different references.

Because of the number of variables involved and the different options which may apply it is extremely difficult to work out exactly what would happen under particular circumstances.

However in order to test the proposed provisions we have attempted to consider the example of a new regulated interconnector, which is only used for one way transfers. It is assumed that the interconnector is not owned by either of the regional NSPs on each side. This is basically the situation which would apply if Basslink was to be progressed as a regulated interconnector except that it would be used for two way transfers:

1. The costs to cover some portion of the regulated revenue requirements of the interconnector itself could be recovered from generators in the exporting region through the exporting region NSP. (Refer Schedule 6.8)
2. The remainder of the regulated revenue for the interconnector would be partially recoverable through TUOS usage charges to the importing region NSP (Refer Clause 6.4.3B and Schedule 6.4) It is not clear which of the three methods would be used to calculate the allocation of costs but all three methods would presumably leave a shortfall which would normally be recovered through TUOS general charges.
3. The NSP in the exporting region could also levy TUOS usage charges and common service charges on the interconnector connection point payable by the interconnector under Clause 6.4.3B and 6.7.4. Alternatively these charges may be passed through to the NSP in the importing region as implied in Schedule 6.4 Item 9.

As can be seen from points 1.& 2. in this example, an independent owner of a regulated interconnector would recover less revenue under the above arrangements than his regulated revenue entitlement. The problem arises basically because he has no mechanism to levy TUOS general charges on customers, unlike regional NSPs who can use this means to recover revenue shortfalls.

Furthermore, depending on the interpretation of the arrangements under point 3 above, an independent owner of a regulated interconnector might also be expected to pay TUOS usage and common service charges to the NSP in the exporting region thus further reducing his net revenue entitlements.

The Board therefore believes that the arrangements as outlined in Chapter 6 of the Code as currently drafted are discriminatory and will only allow the development of new regulated interconnectors by incumbent NSPs.

We therefore suggest that the price allocation and billing and settlements procedures should be reviewed by the ACCC to ensure that they are 'even handed' between incumbent NSPs and new entrant NSPs established for the purpose of developing regulated interconnectors.

When assessing the code changes ACCC needs to consider that NSPs (such as Basslink) which operate regulated interconnectors will have no ability to directly bill Transmission Customers for their services, as they will only be connected at two connection points with the incumbent NSPs in adjacent regions. An NSP in this situation should have the same degree of financial certainty that it can allocate and recover its aggregate annual revenue requirement as an incumbent NSP which services a range of Transmission Customers.

5. Other Comments

In reviewing the code changes we have also noted a number of other comments which are set down in the attached Table. These comments are generally of an editorial nature but some comments deal with apparent inconsistencies which are of greater concern.

NECA Proposals for Changes to the National Electricity Code

Other Comments

Clause Reference	Comments
5.2.3	Query whether there also needs to be a reference to service standards to be set by the ACCC
5.5A(i)	Cross reference to 5.5A(g)(3) should probably be 5.5A(g)(2)(A)
5.5A(g)(2)	'Connection services' is defined by reference to 'Entry Services' or 'Exit Services' such services being either of transmission or distribution service provided to 'Transmission Customers' at a single 'Connection Point'. However the definition of 'Transmission Customer' does not include an interconnected MNSP.
6.4.1(a)(3)	Delete “use of” before “transmission use of system service asset”
6.3.4	This clause has been changed to Allocation within a Region. Hence references to “or regions” in 6.4.3C(e) and 6.4.4(b) should be deleted
6.5.4(a)(4)	“fixed” should be “general”
6.5.4(e)(2)	It is not clear in this clause whether the prices or the charges are intended to be scaled by the scaling factor
6.5.6(b)	The first reference to “common service cost” should be to “common service price”
6.7.3 & 6.7.4	These clauses seem to duplicate each other in some areas eg 6.7.3(e) and repeat information in 6.4.3
6.7.4(c)(2)	The provisions related to Market Network Service Providers are inconsistent with Clause 6.4.3B(b)
Schedule 6.7	The principles in this Schedule appear to need updating eg Items 2. & 7.