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Basslink Transmission Revenue Proposal

September 15, 2023

apa

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CEO's Foreword

We are pleased to submit our revenue proposal to the Australian Energy Regulator (AER) for the Basslink Interconnector (Basslink) for the five-year period from 1 July 2025 to 30 June 2030 (Proposal). Basslink Pty Ltd has also submitted an application to the AER to convert Basslink to a regulated Transmission Network Service Provider (TNSP).

APA is a leading Australian Securities Exchange (ASX) listed energy infrastructure business. Consistent with our purpose to strengthen communities through responsible energy, our diverse portfolio of energy infrastructure delivers energy to customers in every state and territory in Australia.

Following our acquisition of Basslink in October 2022, we have now proudly extended our footprint in Victoria and Tasmania. While we are new to Tasmania, we aren't new to energy infrastructure. For decades we have owned, operated and maintained some of Australia's most important energy infrastructure.

APA is a major owner and operator of solar farms and wind farms and a number of Australia's most critical electricity transmission interconnectors. We also own and operate one of the nation's most efficient gas-fired power generators and more than 15,000 kilometres of gas pipelines which deliver energy to families and industry across every corner of Australia.

As a result of this experience, we know the importance of energy infrastructure and we know the importance of Basslink to Victoria, Tasmania and the National Electricity Market (NEM).

Our goal is to support communities, businesses and our customers with an energy system that is reliable, affordable, and low emissions. That means our focus is on ensuring the lights stay on – at our schools, our hospitals and in our homes – in the most efficient and affordable way, supporting jobs, manufacturing, industry and economic prosperity.

We acquired Basslink because we know how important it is to Australia's energy transition. Basslink already plays a key role in delivering low-cost renewable energy to Victorians and Tasmanians and we see this role only increasing as coal generation retires and Australia boosts its renewable energy. Basslink is APA's first investment in Tasmania and we are excited to play a role in fostering the continued development of Tasmania's unique renewable energy resources.

We are focused on ensuring Basslink is a sustainable operation and can continue to deliver the reliable electricity that Tasmanian and Victorian households and businesses depend on every day. Basslink is expected to deliver significant net market benefits to consumers of over $3.7 billion- over the remainder of its life.

As well as the importance of a reliable electricity supply, we also understand the importance of ensuring Basslink's prices remain affordable. Cost of living concerns and energy affordability were key themes in the extensive stakeholder engagement we undertook in the development of this regulatory proposal, and this has been front of mind in considering Basslink's future investments and services.

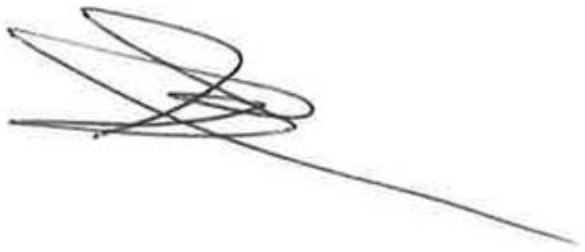
Under this Proposal, Basslink's impact on consumers' cost of energy will remain low at around $8 a year for Tasmanian residential consumers and just under $11 a year for Victorian residential consumers.

Stakeholder engagement and consumer preferences have guided each step of this Proposal. We appointed an expert Regulatory Reference Group (RRG) comprised of stakeholders representing residential, small business and large energy users in Tasmania and Victoria to support the development of the Proposal and co-design our stakeholder engagement plan. The RRG's independent advice was vital in helping to improve our understanding of the needs and expectations of different consumers.

As part of our stakeholder engagement activities we held extensive consumer workshops with over 90 consumers in Melbourne and Launceston. We undertook an online survey with more than 1,200 consumers, and we held a number of meetings with industry and government stakeholders to further understand consumer preferences and help plan Basslink's future. I was pleased to open the RRG's first meeting in December 2022 and the consumer workshops held in March and April 2023 to share our initial plans for Basslink and seek consumer views.

We look forward your feedback on our Proposal and your views on Basslink's future. We are committed to the long-term development of Basslink and continuing to work closely with communities across Tasmania and Victoria over the coming years as we put our plans into action.

Yours sincerely,



Adam Watson

CEO and Managing Director

APA Group

Introduction

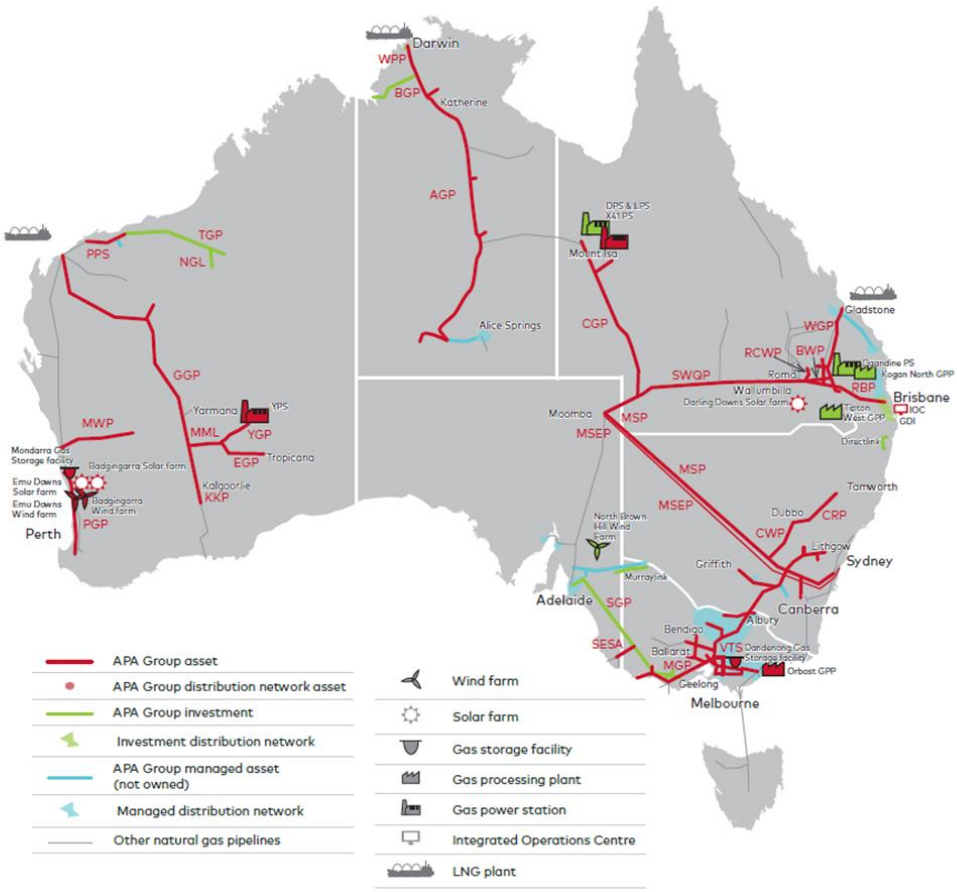
About APA

APA is a leading ASX listed energy infrastructure business. Consistent with our purpose to strengthen communities through responsible energy, our diverse portfolio of energy infrastructure delivers energy to customers in every state and territory.

Our 15,000 kilometres of natural gas pipelines connect sources of supply and markets across mainland Australia. We operate and maintain gas networks connecting 1.4 million Australian homes and businesses to the benefits of natural gas. And we own or have interests in gas storage facilities and gas-fired and renewable generation power stations.

We also operate and have interests in 681 MW of renewable generation infrastructure. Our asset portfolio includes high voltage electricity transmission assets that connect Victoria with South Australia, New South Wales with Queensland and Tasmania with Victoria.

Figure 1 – APA's assets



In August 2022, APA published its inaugural Climate Transition Plan which outlines our commitments to support Australia's energy transition and pathway to achieve net zero operations emissions by 2050.

In October 2022, we completed the acquisition of Basslink Pty Ltd which owns and operates the 370km long high voltage direct current (HVDC) electricity interconnector between Victoria and Tasmania. The Basslink acquisition adds a third electricity interconnector to APA's energy infrastructure portfolio and is consistent with our strategy to play a leading role in the energy transition.

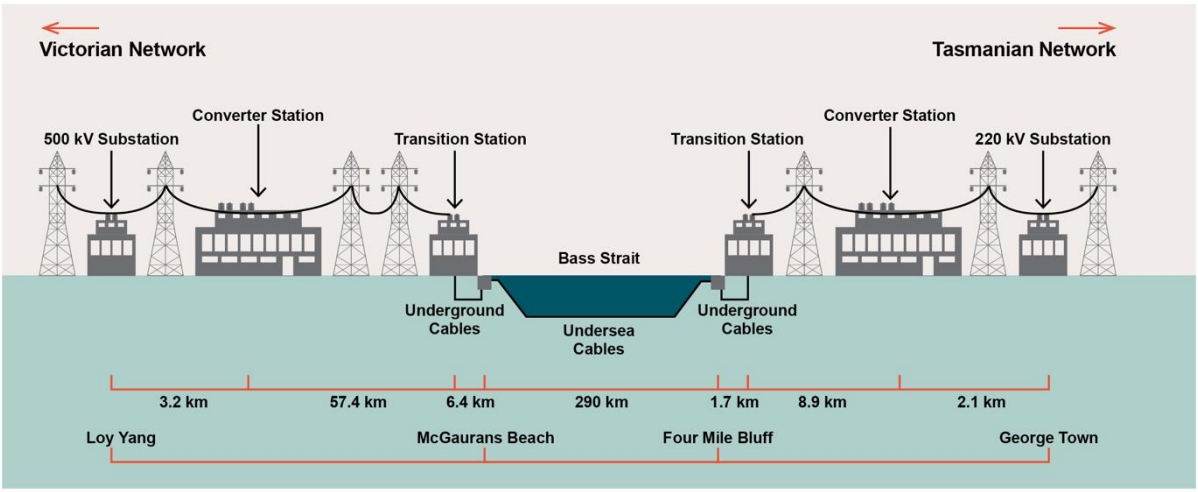
Our diverse energy portfolio means we are familiar with all the obligations and challenges that come with owning and operating critical infrastructure. We will leverage this experience when operating Basslink and apply best practice approaches when meeting new regulatory obligations (such as Security Of Critical Infrastructure obligations).

This Proposal is being made by Basslink Pty Ltd, which is the company that owns the Basslink asset. Throughout this proposal we will use the term Basslink when referring to the interconnector itself, and Basslink Pty Ltd as the company which has submitted the Proposal.

About Basslink

Basslink is a 370km long HVDC electricity interconnector between Victoria and Tasmania. Basslink starts at the Loy Yang switchyard in Gippsland (South East Victoria) and travels by a 61 km high-voltage overhead transmission line until it is submerged. From there it travels for 290 km under Bass Straight at around 1.5 metres below the sea floor. It resurfaces again near George Town (Northern Tasmania) and travels another 11km via a high-voltage overhead transmission line to the George Town substation.

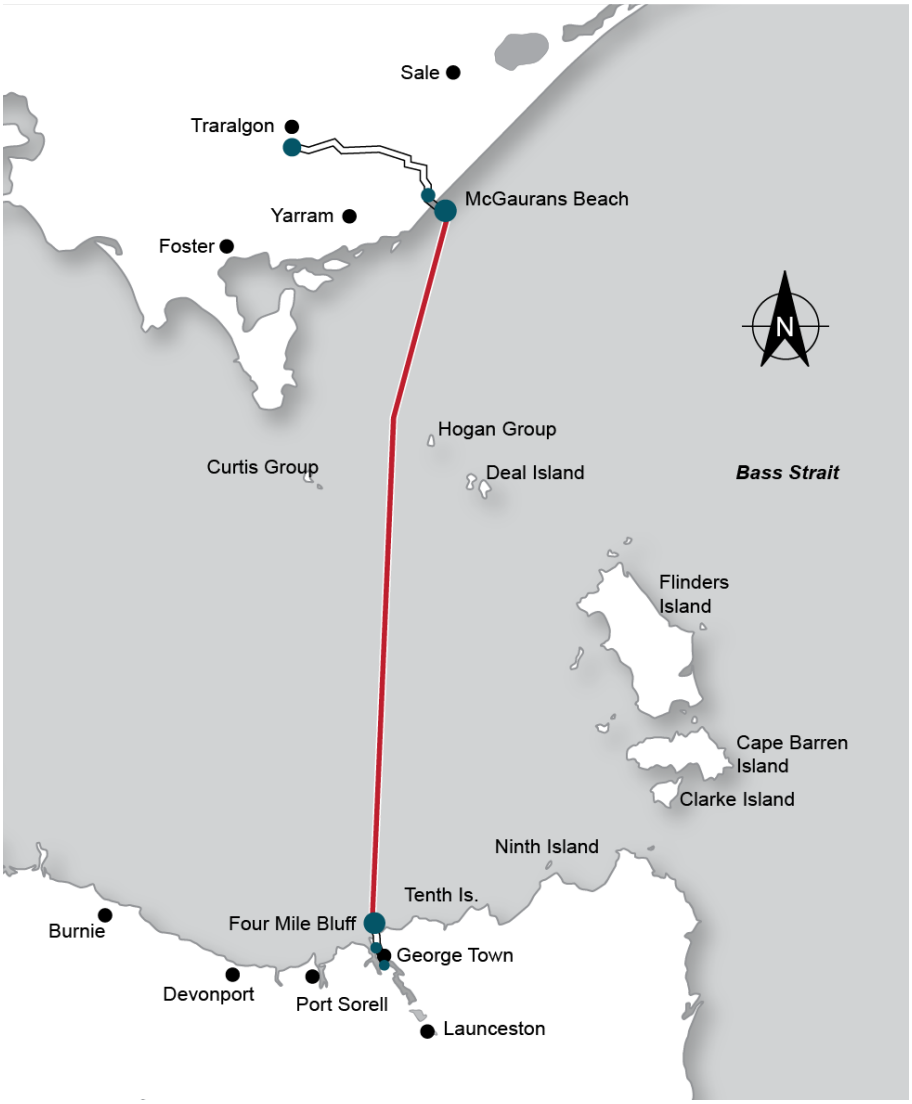
Figure 2 – Assets that make up Basslink



Basslink is currently the sole electricity interconnector between Tasmania and Victoria. Basslink plays a critical role in enhancing security of supply on both sides of Bass Strait.

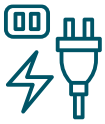
Basslink has been operating since April 2006 and has a design life of 40 years. The original construction cost of Basslink is estimated to be $988m (nominal). This is an estimate because APA was not the owner of Basslink at the time of construction.

Figure 3 – Map of Basslink



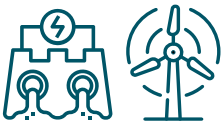
Basslink Operating Environment

Basslink was originally developed to serve the following three main purposes:



Security of Tasmanian electricity supply

- While Tasmania typically has sufficient generation capacity to meet Tasmanian energy demands, this depends on the amount of rainfall Tasmania receives.
- For example, in 2015 Tasmania experienced a record drought, leaving Hydro Tasmania with only 13 percent remaining energy potential compared to having full dams.
- The concurrent failure of Basslink forced the Tasmanian Government to re-commission a gas plant and import costly temporary diesel generators.



Access to a cheaper, more stable, electricity supply

- Basslink provides Victoria, and the NEM more broadly, with access to Tasmania's cheaper hydropower and wind power at its peak periods or when dams are overfilled.
- Basslink also provides Tasmania with access to Victoria's cheaper baseload power when water levels are low in Tasmania.
- Being able to 'smooth out' power supply and demands between Victoria and Tasmania also reduces the extent of large price variations.

Additional revenue streams

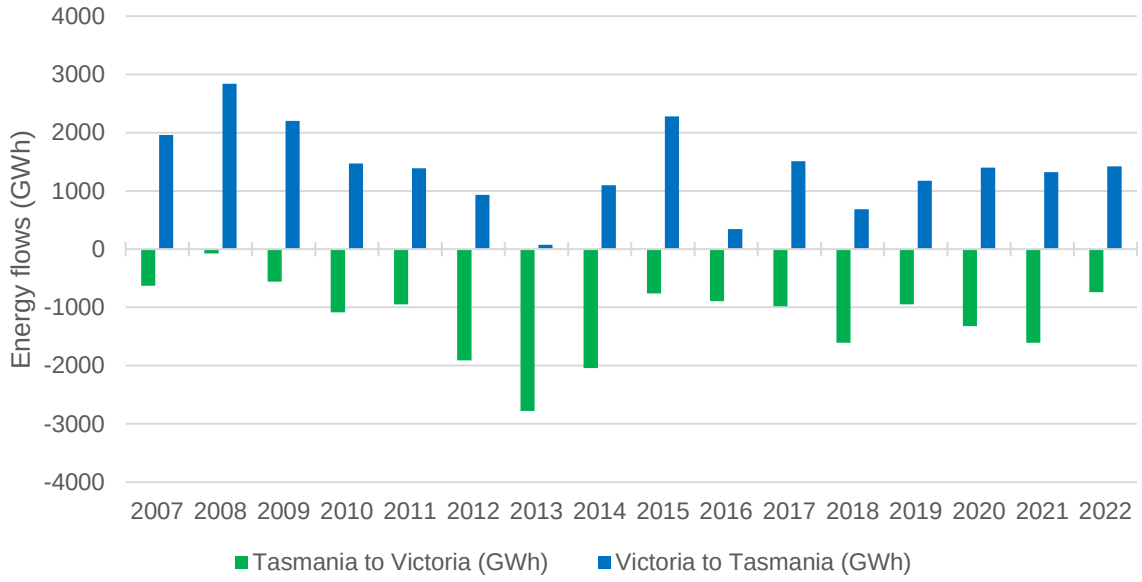
- Basslink connects Tasmania to the NEM. This provides generators across the entire NEM with access to Tasmanian customers, and vice versa.

Historical energy flows

The total energy transported across Basslink each year has recently averaged 2,300 GWh[1]. As is illustrated in Figure 4 below, the dominant direction of the flow has varied each year according to market conditions. In general:

- flows from Victoria to Tasmania are higher in summer due to excess low cost solar generation being produced in Victoria, and reduced water availability in Tasmania; and
- flows from Tasmania to Victoria are higher in winter due to higher rainfall and more hydro electricity being produced in Tasmania and less solar generation being produced in Victoria.

Figure 4 – Annual energy flows across Basslink



Historical and current revenue arrangements for Basslink

Basslink began operations in 2006 as a Market Network Service Provider (MNSP). Basslink is the only MNSP currently operating in the NEM. Directlink was similarly converted to a regulated TNSP in 2006.

The AER does not currently set Basslink's annual revenue like it does for TNSPs. The revenues of TNSPs are regulated by the AER under Chapter 6A of the National Electricity Rules (the Rules).

For most of its operational life, Basslink Pty Ltd had a commercial service contract in place with Hydro Tasmania, the Basslink Services Agreement (**BSA**).

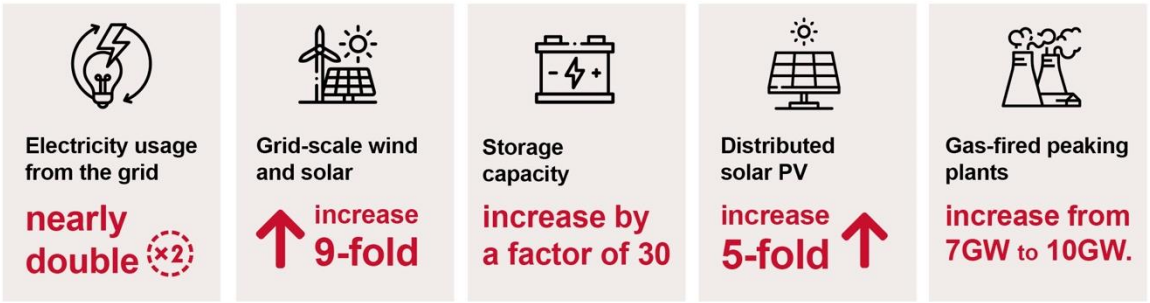
The BSA was terminated in 2022. Basslink Pty Ltd now receives revenue under a contract with Hydro Tasmania (the Network Services Agreement (**NSA**)), which provides Basslink Pty Ltd with a stream of revenue. The NSA expires in mid-2025, and the AER should not consider the continuation of this arrangement (or something similar) to be likely if Basslink is not regulated. The future of

[1] FY17 to FY22 average. Office of the Tasmanian Economic Regulator, Energy in Tasmania Report 2021-22.

Basslink, with and without conversion, is addressed in further detail below and in **Attachment 1** to the Revenue Proposal.

Basslink supports the energy market transition

The scale of investment needed to transition the NEM is unprecedented. According to the 2022 Integrated System Plan (ISP), around $12 billion of investment is needed in the NEM's grid infrastructure to accommodate the significant growth in renewable generation. AEMO's 2022 Step Change Scenario (from the 2022 ISP) anticipates the following increases by 2050 to transform the NEM:



Other studies have similar findings. For example, Net Zero Australia's recent study found that Australia needs to grow renewables as our main domestic and export energy source to 40 times the current NEM capacity. This figure considers direct use and clean fuel production like renewable hydrogen.[2]

This scale of transformation will not be a costless exercise. Efficiently using existing assets will play a critical role in delivering the most optimal pathway to net zero. Basslink is increasingly supporting the energy market transition and contributing to the achievement of emissions reduction targets. Our application for conversion and the revenue proposal are consistent with the ISP, and we have considered the ISP in all relevant elements of the Proposal.[3]

[2] AEMO, 2022 Integrated System Plan (ISP) Infographic (30 June 2022).
[3] Rule 6A.10.1(f)).

There are at least four ways in which Basslink will support the NEM's transformation:

1. **Tasmania has significant wind resources** and the commercial feasibility of leveraging those resources depends on the availability of high-capacity interconnection between Tasmania and mainland Australia.

2. **Tasmania at times receives more rain than its dam capacity allows.** Any reduction in the optimal operation of the interconnection between Tasmania and Victoria would lead to the waste of that renewable energy because water will need to be spilled from the dam, rather than being used to generate energy.

3. **Hydro Tasmania's water storages can act as long-term energy storage** that can 'firm-up' intermittent renewable generators such as wind and solar. This better enables renewable energy technologies to displace 'firm' thermal technologies such as coal and gas.

4. **Basslink enables Tasmania to export its excess renewable electricity** to the rest of Australia, attracting investment and innovation into Tasmania. This is a key enabler of the Battery of the Nation strategy announced by Hydro Tasmania

Conversion Application

Since acquiring Basslink in October 2022, APA has signalled its intention to seek conversion of Basslink from the status of an MNSP to a regulated TNSP.

The Rules do not prescribe what a conversion application must look like, nor what factors the AER, as decision maker, must take into account when making such a decision. In our view, Basslink should be converted to a TNSP if the benefits of such conversion outweigh its costs.

This section of the Proposal sets out Basslink Pty Ltd's application to convert Basslink to a TNSP.

What is the difference between a TNSP and MNSP?

TNSPs and MSNPs both provide electricity transmission services across the NEM. While there are many TNSPs, there is currently only one MNSP (Basslink) in the NEM. The key distinguishing features of TNSPs and MSNPs are as follows:

- TNSPs build, maintain and operate transmission networks in the NEM
- TNSPs' revenues are fully regulated by the AER in five yearly revenue determinations.
- The AER also imposes incentive and service performance schemes to create incentives for the TNSPs to operate their businesses efficiently and maintain reliability.

- MNSPs do not have revenues set by the AER
- MNSPs rely on price differences between regions of the NEM, or contractual arrangements, to earn revenue.
- MNSPs do not have incentive or service performance schemes imposed by the AER.

Why we are seeking conversion

There are various reasons why we are seeking to have Basslink converted to a TNSP. In summary, the main reasons are:

Better alignment of customer and business interests

- MNSPs earn revenue based on price differences between different regions in the NEM.
- These price differences may be more pronounced if MNSPs are capacity constrained.
- If Basslink is converted to a TNSP, any incentive for the interconnector to be constrained will be removed, ensuring that Basslink is available to transport as much renewable energy between Tasmania and Victoria as possible.
- This better aligns the interests of Basslink and its customers.

Reliability of supply

- The 2016 Tasmanian Energy Crisis demonstrated the importance of Basslink to energy security in Tasmania.
- Having the AER approve Basslink expenditure and maintenance plans, with input from customers, will provide stakeholders with confidence that the asset is being operated in a manner that best promotes security of supply.

Certainty of costs and revenues for Basslink and customers

- As an MNSP, revenues are unregulated and dependent on energy flows between regions. In contrast, revenues for TNSPs are approved by the AER in five yearly cycles, with greater visibility over TNSP spending plans.
- Converting Basslink to a TNSP will provide stakeholders with the opportunity to comment on Basslink's five year spending plans as part of the AER revenue determination process, as well as providing much greater certainty over costs and revenues.

Benefits of conversion outweigh the costs

- We have considered the costs and benefits of converting Basslink to a TNSP.
- We have also sought expert advice on the market benefits associated with Basslink.
- Despite the additional costs imposed by regulation, in this instance the benefits of converting Basslink to a TNSP have been shown to outweigh the costs.

Benefits of conversion

To consider the costs and benefits, we need to compare the future with Basslink operating as a regulated asset, with the future with Basslink operating as an MNSP.

It is important to note that Basslink has not been operated as a typical MNSP in the past, but has largely been operated in a manner more akin to that of a TNSP[4].

In considering a future in which Basslink is operating as an MNSP, the AER needs to think about how the market rules require a MNSP to derive revenue, and what this means for the incentives of a MNSP:

- MNSPs have an incentive to maximise revenue and bid capacity on this basis. This requires decisions about how much capacity to make available during any one time period. By contrast, TNSP assets are made available to the full transfer capacity.
- MNSP's derive their revenue in a manner dependent on both the volume of energy flows in each direction and on the price differences between Tasmania and Victoria. To optimise revenue, a MNSP would have strategic opportunities to reduce the capacity it makes available to the market in order to achieve a higher price differential. This is a legitimate dispatch strategy fully consistent with market design.
- An MNSP operating in a manner designed to seek price arbitrage would likely mean less transmission capacity would be available between Tasmania and Victoria. This would likely have the effect of increasing the average electricity price in both States, with a potentially greater effect in Tasmania. In addition, Victoria would risk having less access to peaking hydro power from Tasmania and would need to rely on thermal generation for that purpose, leading to higher greenhouse gas emissions.

In contrast, a future in which Basslink operates as a regulated TNSP would be characterised by:

Basslink operating as an 'open link' where its dispatch is driven by the efficient movement of electricity between the regions

All stakeholders having a much greater say in Basslink's spending plans and revenues, providing greater confidence that future investment is efficient and in the long-term interests of customers

Greater certainty for customers of the interconnector's availability and reliability relative to the absence of regulation

Market participants on both sides of the link gaining access to the Interregional Settlement Residue Auctions, which will enhance competition in the market.

[4] Note that during a period of administration in 2022, Basslink was not a party to any agreement with Hydro Tasmania and was largely operated as a merchant asset.

Costs of conversion

The most significant risk to consumers from regulatory conversion is the transfer of the investment risk from the investor to the users. For regulated transmission infrastructure, once investment has been deemed efficient by the AER and has occurred, users are obligated to pay enough to ensure return on and of the investment. Both the return on investment and the depreciation profile are set by the AER.

For MNSPs there are no regulated constraints on the rate of return or how quickly the capital is paid back. However, there is also no guarantee that capital will be returned. If the asset is not needed by the market and is not able to earn sufficient revenue, the risk is entirely with the investor.

This transfer of risk will only have a cost if it can be assumed that the asset would recover more revenue as a TNSP than it will as a MNSP. It cannot be assumed that Basslink as an MNSP would not be able to recover the same level of revenue over a shorter period of time, namely in the period before additional generation and transmission capacity reduces the incidences of significant price disparity between Victoria and Tasmania. However, it should be assumed that the MNSP would seek to recover those costs over a significantly shorter period than if the asset were a TNSP. As noted above, this will impact the incentives for a MNSP to make long term investments.

On balance, APA is of the view that regulatory conversion will deliver material net benefits to the NEM and electricity consumers, and that it is therefore appropriate for the AER to convert the asset to a TNSP. For Tasmania, Basslink will help achieve the Tasmanian Renewable Energy Target (TRET) and support Tasmania's energy security long into the future. Basslink can:

Protect Tasmania against the risk of energy shortages

Enable Tasmania to buy renewable energy from the mainland (especially when mainland renewables are cheaper)

Transport renewable energy to Victoria and southern states during peak demand periods

Promote the development of additional renewable generation in Tasmania by providing a path to market for that new energy

Potentially support the development of the Australian offshore wind industry via subsea electricity cables.

Regulation will ensure Basslink continues to operate as an open link and therefore support the NEM's transformation by 2050. As a regulated asset, Basslink can provide greater transparency and certainty on our costs to our stakeholders.

This Revenue Proposal

As Basslink Pty Ltd put together this Proposal three key themes emerged that supported the nature of the Proposal for the period financial years 2026 to 2030.

Reliability

Basslink is a critical piece of infrastructure in the NEM. It is vital that its capacity to transport electricity is available when it is needed most. It must be reliable, and this reliability must be a focus of the operating and capital expenditure plans.

We are placing this focus on reliability for three reasons:

- Stakeholder Engagement - the importance of Basslink's reliability was reinforced to Basslink Pty Ltd by feedback from stakeholders.
- Energy Security – the events of 2016 demonstrate the importance of Basslink reliability to Tasmanian energy security
- Tasmanian Renewable Energy Target (TRET) – the TRET is driving Tasmania to achieve 200% renewable energy production by 2040, and as an existing asset, Basslink offers the lowest cost pathway to allow this renewable energy to be shared with mainland Australia.

Converting Basslink to a regulated interconnector and ensuring it is operated with a high degree of reliability ensures this existing capacity is fully maximised for the benefit of the market.

Affordability

Consumers highlighted that energy costs and affordability of electricity are key concerns for both residential and small business consumers, with 73% of survey respondents indicating they were very or extremely concerned about energy affordability.

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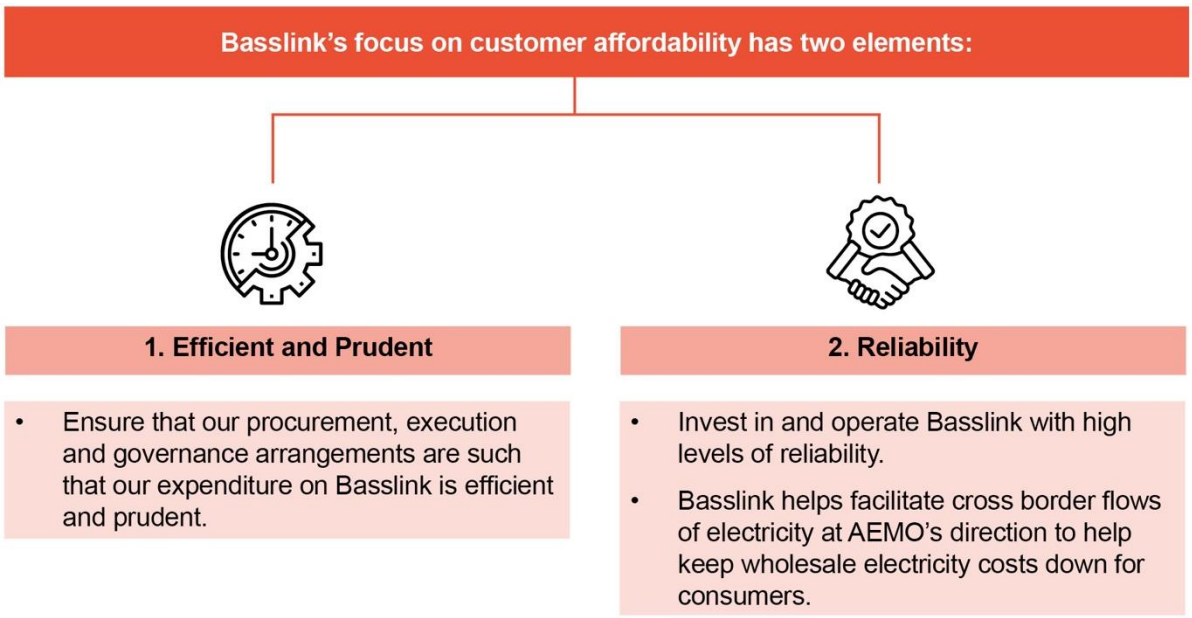


Transition

Basslink is an asset that is in a state of transition, and the impacts and potential impacts of this transition need to be taken into account when the AER is considering the appropriate regulatory arrangements. Basslink is transitioning in two relevant ways:

- If successful, it will transition into being **a regulated asset**, with all of the governance arrangements that then apply. Basslink will need to have its expenditure approved by the AER in order to recover it from consumers. This governance structure will impact how Basslink invests in its operating and capital expenditure.
- It is moving from being a stand alone asset to one that is **integrated** into APA. The integration process is ongoing, and involves transitioning Basslink from using systems and processes of a stand alone business to using the systems and processes of APA. We believe this will support the provision of more sustainable, reliable and affordable services for customers. In respect of some services, this will entail a higher level of service and may entail a higher level of cost.

Stakeholder Engagement

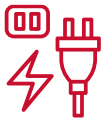
Our engagement process

Basslink Pty Ltd has approached this stakeholder engagement with the understanding that we play a critical role in the energy supply chain and our operations have a broad impact on consumers and the energy transition. We understand the importance of supporting the delivery of affordable and reliable energy to Tasmanian and Victorian consumers, as well as the important role Basslink plays in the energy transition through the supply of renewable energy to the NEM. Further detail in relation to our stakeholder engagement process is provided in **Attachment 3**.

Basslink Pty Ltd's objectives for engagement for the Basslink revenue proposal were co-designed with the stakeholder RRG. Our objectives for stakeholder engagement during the regulatory process are to deliver a revenue proposal that:

'Brings the outside in' by directly responding to the needs and preferences of our customers.

Provides sustainable returns.



Delivers a reliable supply of electricity to Tasmanian and Victorian consumers.

Directly contributes to the green energy transition in Australia.

In undertaking our stakeholder engagement program, we were committed to fully consulting with consumers to understand their views and ensure their preferences were reflected in our Proposal.

Basslink Pty Ltd established a RRG in November 2022 to support the development of the Proposal. The RRG serves as an independent advisory group comprised of a cross-section of stakeholders representing residential, small business and large energy users in Tasmania and Victoria. The RRG members include:

- Gavin Dufty, St Vincent's de Paul Society Victoria
- Leigh Darcy, Tasmanian Minerals, Manufacturing and Energy Council
- Karina Dambergs/ Chris Griffin, Northern Tasmania Development Corporation[5]
- Robert Mallett, Tasmanian Small Business Council
- John Pauley, Council of the Ageing Tasmania

[5] Karina Dambergs left the Northern Tasmania Development Corporation in late June 2023. Chris Griffin attended the September 2023 RRG meeting.

The RRG's objective is to work collaboratively with Basslink Pty Ltd under a principle of co-design on the development and implementation of the regulatory engagement plan for Basslink, including the scope, timing, themes and engagement methodology. The RRG's input was instrumental in helping to improve our understanding of the needs and expectations of different consumer segments. RRG input was used to continually refine the engagement materials and methodology Basslink Pty Ltd used in consulting with consumers, industry and government stakeholders.

The RRG provided an independent report for the AER in August 2023 outlining their views on how Basslink Pty Ltd engaged with its customers and how it has met the requirements of the AER's Better Resets Handbook. The RRG considered that, overall, Basslink Pty Ltd has met the Better Resets Handbook requirements and that Basslink Pty Ltd has engaged openly and collegially across all levels of the organisation.

The RRG also provided suggestions on how engagement can be broadened and deepened for the 2025-30 revenue proposal and beyond. Basslink Pty Ltd will continue to engage with the RRG as the AER assesses the Proposal. A copy of the RRG's independent report has been found at **Attachment 3.3** to this Proposal.

We used deep, broad and targeted engagement methods in the development of the Proposal with APA senior staff steering the engagement program and attending all engagement activities, including our CEO Adam Watson presenting to the consumer workshops.

6
Regulatory Reference Group meetings

2
online focus groups

2
in person consumer workshops

1,240
Consumers responses to online quantitative survey

1
Newsletter article

Many
Meetings with key stakeholders including Victorian and Tasmanian Governments

Further detail on our engagement process for the development of the Proposal can be found in **Attachment 3.1** and **3.2** to this proposal.

What we heard and how we have responded

We have focussed our stakeholder engagement on five priority issues based on issues identified by the RRG as key for Basslink's stakeholders and consumers. We have also considered issues where stakeholders and consumers can have the greatest impact on the Proposal, and where their opinion would genuinely influence and guide the Proposal.

Priority Issue	What we heard	How we have responded
Reliability 	• Consumers and industry stakeholders both strongly supported a high level of reliability due to concerns about the potential for electricity outages if Basslink fails. • 84% of survey participants rated having greater reliability for the future as something they strongly support (rated at least a 7 out of 10). • Consumers at the workshops wanted to ensure that there were timely repairs to Basslink's subsea cable should a failure occur in the future. Tasmanian consumers particularly referenced the need to avoid a repeat of Basslink's 2015 damaging outage doesn't occur again.	• Basslink Pty Ltd has clearly heard customers preference for a strong and reliable Basslink. We are focussed on maintaining Basslink's high levels of reliability to ensure Basslink can continue to meet the energy needs of Tasmanian and Victorian consumers. • In addition to the replacement of the timely replacement of the control and protection system discussed below, we have proposed two key investments to further strengthen Basslink's reliability in response to stakeholder and consumer feedback: - $7.0m in capital expenditure to enable Basslink to operate at higher temperatures when customer demand for electricity is high. - $7.65m annual expenditure on emergency preparedness to reduce repair times and the time Basslink would be offline in the event of a major incident.
Affordability 	• Consumers highlighted that energy costs and affordability of electricity are key concerns for both residential and small business consumers, with 73% of survey respondents indicating they were very or extremely concerned about energy affordability. • Consumers at the workshops were also strongly focussed on the bill	• Basslink Pty Ltd is conscious of consumer and stakeholder concerns around energy affordability and cost of living and is focussed on keeping Basslink's prices as low as possible while maintaining a high level of reliability to reduce wholesale electricity costs for customers.

Priority Issue	What we heard	How we have responded
	impact of the Proposal, with several remarking that the whole conversation comes down to cost. • Some industry stakeholders indicated a preference for price stability, while others noted the importance of ensuring any cost savings following the regulation of Basslink are passed through to consumers.	• Consistent with consumer concerns around energy affordability, Basslink Pty Ltd is proposing to adopt the lowest initial Regulatory Asset Base forecast, which is based on the Depreciated Actual Cost method. • The Proposal, if approved by the AER, would result in a relatively low bill impact of $11 a year for the average Victorian residential customer and $8 a year for the average Tasmanian residential customer. These bill impacts are based on the adoption of a market size approach to sharing the costs of Basslink between Victorian and Tasmanian energy consumers, which was the preference from our consumer engagement as it was considered the fairest approach. This approach results in the most comparable bill impacts between Victorian and Tasmanian consumers of the alternative cost sharing approaches we considered and engaged on. • Basslink's costs are expected to have minor real cost declines year on year for the revenue period. • Ensuring that the capacity of Basslink is available to the market will help minimise electricity prices in Tasmania and Victoria.
Capital expenditure 	• Our engagement with consumers and stakeholders on capital expenditure focussed on the replacement of Basslink's control and protection system due to the significant cost of the replacement system. In particular, views were sought on whether the system should be replaced in the upcoming 2025 to 2030 revenue period or the following revenue period post 2030. • There was strong support from consumers for replacing the control	• Basslink Pty Ltd recognises the strong and consistent preference for the earlier replacement of the control and protection system from consumers and stakeholders. We also note this preference is consistent with the high importance placed on reliability. • We have adopted the preference of consumers and stakeholders and included the replacement of the control and protection system in the capital expenditure plans of our

Priority Issue	What we heard	How we have responded
	and protection system in the 2025 to 2030 revenue period, with 73% of all workshop participants and 70% of all survey participants supporting the earlier investment. • The main reasons cited by consumers for supporting earlier investment were based on an aversion to risk, with concerns around the risks of outages and the associated impacts on consumers. The potential for cost savings from earlier investment were also noted by survey participants. • The Victorian Chamber of Commerce and Industry (VCCI) also indicated support for the earlier replacement of the control and protection system to avoid the risk of an outage.	regulatory proposal for 2025 to 2030.
Insurance 	• Our engagement with consumers and stakeholders on insurance focussed on whether APA should adopt a low insurance premium with higher risks should an insurance event occur, or a high insurance premium with lower risks should an insurance event occur. • Consumers indicated mixed views on insurance, with 72% of all workshop participants preferring the low insurance premium option and 55% of all survey participants preferring the high insurance premium option. • The preferences of workshop participants towards the low insurance premium option were largely driven by Launceston participants, with 81% preferring this option (compared to 60% in Melbourne). Many Launceston participants preferred the low premium option as they thought the risk of damage was low and this option would be cheaper overall.	• There was not a clear and consistent view from consumers on their preferences and level of risk on insurance. This may reflect the complex choices involved in this issue and differences in how consumers considered the risks of damage to Basslink. Consumers are also likely to have differences in their tolerance for risk. • On balance, after carefully considering this feedback, we have decided to adopt insurance arrangements that preference a lower level of risk to customers in the long term but includes a higher level of premium. • This approach will help to meet consumer preferences for a 'no surprises' approach because the alternative could lead to an unexpected increase in costs, should repairs be required. • We understand there are also high levels of concern around energy affordability. However, we note the bill differences between the high

Priority Issue	What we heard	How we have responded
	• In contrast, survey participants preferred the high insurance premium option as they considered it would help to manage reliability risks and would provide greater certainty about costs. • Industry stakeholders did not indicate an insurance preference.	and low premium approaches are relatively low and a high premium approach will also help to avoid bill shock for consumers should damage occur.
Cost sharing 	• Our engagement with consumers and stakeholders on cost sharing focussed on how Basslink's costs should be shared between Tasmanian and Victorian consumers. Three cost sharing options that are allowed under the Rules were discussed, including options based on the geographic split of Basslink's assets, energy flows between Tasmania and Victoria, and the market size of Tasmania and Victoria based on the number of electricity connections in each State. • Consumers indicated a preference for the market size approach to cost sharing, with 75% of all workshop participants and 44% of all survey participants selecting this option. • Participants across both the workshops and the survey selected the market size option as it was considered the fairest. Tasmanian participants were especially supportive of this option and also noted it was fairer as Tasmanians are more likely to have lower incomes than Victorians. • Victorian survey respondents demonstrated a very slight preference for the energy flows approach, with 36% supporting this option. However, this was very closely followed by a preference for the market size approach at 31%. Additionally, Victorian workshop participants displayed a preference for the market size approach at 53%	• Consumers expressed a consistent preference for the market size approach to sharing the costs of Basslink, largely as it was considered the fairest approach. • We note this approach results in the most comparable bill impacts for Victorian and Tasmanian consumers. • Although we understand a market size approach to sharing the costs of an interconnector has not previously been applied by the AER, we have adopted the market size approach in our Proposal due to the preferences expressed by consumers. • We intend to undertake further stakeholder consultation on the market size approach over the coming months as the AER assesses our Proposal.

Priority Issue	What we heard	How we have responded
	- when considering these different pillars of evidence it is clear there is strong support for the market size approach across the Victorian population. • An industry stakeholder noted a preference for either the market size or energy flow options, with another stakeholder noting costs should be allocated based on who benefits from Basslink.	

Market Benefits

The Rules operate to require Basslink Pty Ltd to provide to the AER an assessment of the market benefits of Basslink so that the AER can ensure consumers are not being asked to provide revenue to a regulated asset in excess of the benefits that asset provides to the market as a whole. Basslink Pty Ltd has commissioned EY to perform the independent assessment, with EY's report on market benefits being provided at **Attachment 2.1**.

The outcome of this comparison of the modelled market benefits with the long term costs of Basslink demonstrates that the market benefits of the operation of Basslink (as a regulated asset) significantly outweigh the long term costs under all of the scenarios modelled by EY:

Method	Result
Market benefits less long-term costs of operation – Step change/single stage scenario	$3,748 million
Market benefits less long-term costs of operation – Progressive change/single stage scenario	$4,190 million
Market benefits less long-term costs of operation – Hydrogen Superpower/single stage scenario	$3,102 million
DAC	$831 million
DORC	$1,079 million
Proposed RAB	**$831 million**

Revenue

Building Block Revenue

The Building Block Revenue is the minimum revenue that Basslink Pty Ltd needs to maintain a reliable transmission link between Victoria and Tasmania.

Each element of the Building Block Revenue is discussed in more detail in this overview but a summary of the forecast values ($m nominal) of each of these is set out below.

+	**$219.9M** Return on Capital	Basslink has used the AER's Rate of Return Instrument 2022 to calculate the Rate of Return used in the Post Tax Revenue model (PTRM). Based on the available data, the estimated nominal Weighted Average Cost of Capital (WACC) for the financial year 2025-26 is 6.6%. More detail can be found in **Attachment 9**.
+	**$140.6M** Return of Capital	Return of Capital (Regulatory Depreciation) recovers the outstanding cost of previous investments that Basslink has made to ensure ongoing reliable operation. Refer to **Attachment 6** for more information on asset classes, asset lives and depreciation.
+	**$182.7M** Operating Expenditure	Basslink's forecast operating activities are focused on delivering safety, security and reliability for the interconnector. We have adopted the AER's preferred method for forecasting operating expenditure the "Base, Step Trend" method. More detail can be found in **Attachment 8.**
+	**$0M** Revenue Adjustments	Revenue adjustments account for penalties and rewards earned though incentive arrangements (discussed in **Attachment 10**). Because Basslink is undergoing its first regulated revenue determination there are no penalties of rewards, and therefore, no revenue adjustments.
+	**$17.6M** Net Tax Allowance	Taxation is calculated based of Forecast revenue, operating expenditure tax depreciation and tax rates. Refer to **Attachment 4** for further information.
=	**$560.8M** Building Block Revenue Requirement (Unsmoothed)	The Building Block Revenue is the minimum revenue that Basslink needs in order to be able to maintain a reliable transmission link between Victoria and Tasmania. Refer to **Attachment 4** for further information.
=	**$561.5** maximum allowed revenue smoothed	The smoothed revenue is a forecast of the revenue expected to be earned by Basslink for the period, and as the name suggests, its purpose is to smooth our revenue year on year across the regulatory period. Refer to **Attachment 4** for further information.
↓	**1.6%** Average annual price change (before inflation)	The year-on-year price change is applied to revenue each year in a regulatory period. For Basslink, annual revenue is proposed to reduce, on average, by 1.6%, in real terms, each year. Refer to **Attachment 4** for further information.

The actual revenue to be recovered will vary against this forecast in the period due to the difference between forecast inflation and actual inflation experienced throughout the period. Further, the update for cost of debt throughout the period (discussed more in **Attachment 4** and **Attachment 9**).

Cost Sharing

Once the AER determines the revenue Basslink Pty Ltd can recover, it must decide how that revenue will be collected – i.e. who will Basslink Pty Ltd invoice for its transmission services and in what proportion. This is referred to as Basslink's Pricing Methodology.

As part of its Proposal, Basslink Pty Ltd is required to propose a pricing methodology for the AER's determination. This methodology does not alter how much revenue Basslink Pty Ltd is allowed to collect, but determines how it collects that revenue. For this reason, Basslink Pty Ltd does not have a commercial preference for any particular method of revenue recovery. However, we are aware that this is an issue of significant public interest, and Basslink Pty Ltd has therefore undertaken a large amount of stakeholder engagement on this issue.

Basslink Pty Ltd consulted on three different methods for allocating the cost of Basslink between Victorian and Tasmanian customers - described as the Geographic Method, Energy Flows and Market Size.

- Geographic Method – the cost split would be based on the value of the interconnector assets geographically located in each region. This is the approach the AER took in Murraylink and Directlink. This method would result in 55% of Basslink's cost being allocated to Victoria and 45% to Tasmania
- Energy Flows – the cost would be split on the basis of energy flows across Basslink, and would result in 50% of cost being allocated to Victoria and 50% to Tasmania
- Market Size – the allocation would be based on the number of electricity connections in each jurisdiction. Given the significantly greater number of connections between the number of customers in Victoria and Tasmania this results in revenue being allocated 90% to Victoria and 10% to Tasmania.

We undertook extensive public consultation to ascertain stakeholders support for the different alternatives. On balance, stakeholders generally preferred the Market Size approach to revenue allocation. This preference was very strong in Tasmania. The workshop in Melbourne had a preference for the Market Size over the Energy Flows but there was a mild preference for Energy Flows over the Market Size in the Victoria responses to the quantitative survey.

On the balance of results the preference expressed by our stakeholder engagement is to favour the Market Size approach. Therefore, Basslink Pty Ltd is proposing a pricing method based on Market Size. This would result in a bill outcome for residential and small business customers similar to the table below.

Table 11: Bill outcome (Market Size) ($ FY25 per year)

		Tas	Vic
	Residential	8	11
	Small business	15	35

Regulatory Asset Base

One of the most important elements behind the building blocks revenue model is the Regulatory Asset Base (RAB). The RAB consists of the adjusted total value of all regulated assets and is used in determining the allowance for depreciation and for a return on capital invested.

The value of the RAB is required to be forecast to the commencement of the regulated revenue period (1 July 2025).

There are two methods available to Basslink under the Rules, each of which delivers a different value:

Depreciated Actual Cost	Depreciated Optimised Replacement Cost
$831M	**$1,079M**

Basslink Pty Ltd is proposing to use the Depreciated Actual Cost to calculate the initial RAB. In addition to meeting the requirements of the Rules, this recognises the affordability concerns raised by stakeholders and adopts a method that lowers the overall cost of Basslink to customers.

Under this approach the RAB at the beginning of the 2025-30 revenue period would be $831 million. More information on the three methods to determine the value of the RAB can be found in **Attachment 5**.

Forecast Capital Expenditure

Capital expenditure, often referred to as capex, covers the investments needed to ensure that Basslink can continue to operate safely, securely, and reliably. As noted above, the principle of reliability is one of the principles driving Basslink's investment decisions outlined in this Proposal.

We need to ensure that Basslink is capable of transferring energy at times of peak demand and can quickly recover from any faults.

APA and Basslink Pty Ltd has a capital expenditure governance process that is used to identify, assess and rank projects that are important to the safe, secure and reliable operation of the interconnector. This process ensures only projects that result in benefits to customers are undertaken and that the most important projects are ranked and undertaken when they should be.

This process has identified capital expenditure projects to be undertaken over the regulatory control period. Our overall capital expenditure forecasts for the upcoming revenue period is as set out in the table below. As set out in **Attachment 7** we consider this forecast capital expenditure is required to meet each of the capital expenditure objectives (which is a requirement of the Rules).[6]

Table 22: Forecast Capital Expenditure ($m FY25)

Forecast Capital Expenditure	FY26	FY27	FY28	FY29	FY30	Total
Total	18.5	10.3	4.1	10.9	30.3	74.1

Control and protection system

The control and protection system is a computer system that ensures the safe and reliable operation and seamless integration between the Tasmanian and Victorian electricity grids. This system has a design life of 15-20 years and will need to be refreshed over the 2025-30 period – it is designed to be replaced halfway through the design life of the asset.

Operating a control and protection system beyond its design life escalates the risk of component failure, brings challenges around spare part availability, and risks prolonged outages. However, given the materiality of this project and the difficulty in balancing the risk with consumer benefit, we consulted with our stakeholders on whether we should replace the system in the 2025-30 or 2030-35 periods.

Most customers – between 68% and 77% depending on customer location – told us through multiple channels that they supported replacement of the system in 2025-30 to avoid the potential negative impacts of increased unreliability.

Given consumer feedback, the availability of next generation technologies, reliability risks and overall costs we propose to refresh the control and protection system in 2025-30 at a cost of $44.2 million.

[6] Rule cl6A.6.7(a)

Other capex

Outside of the control and protection system, ongoing capex is required to:

- refresh Information Technology and Operational Technology systems,
- meet the requirements of *Security of Critical Infrastructure Act 2018* (Cth) (SoCI Act),
- fit-out cable repair vessels (to reduce the length of outages in the event of cable damage) and
- undertake ongoing refurbishment and replacement of key components.

Excluding the control and protection system mid-life refresh, 2025-30 capex is $29.9 million, lower than the $53.3 million projected to be incurred over the preceding 5 years.

More information on our capital expenditure forecast is provided in **Attachment 7** to our proposal and **Attachments 7.1** to **7.6**.

Forecast Operating Expenditure

As part of the building block approach, Basslink Pty Ltd is allowed to recover the costs of operating the asset. These costs must be forecast at the start of the revenue period and Basslink Pty Ltd will only recover what has been forecast.

We have adopted the AER's preferred method for forecasting operating expenditure the "Base, Step Trend" method. Our forecast operating activities are focused on delivering safety, security and reliability for the interconnector. We know there will be significant changes to Basslink's operating environment in integrating with APA and becoming a regulated asset, and the improved process and risk management that will result from these changes.

We note that while every effort has been made to create a robust forecast, these forecasts are intrinsically difficult and there will be differences between the operating expenditure as forecast and the actual operating expenditure when incurred.

Our overall operating expenditure forecasts for the upcoming revenue period are set out in the below table. As set out in **Attachment 8** we consider this forecast operating expenditure is required to meet eachof the operating expenditure objectives (which is a requirement of the Rules)[7]:

Table 3: Forecast Operating Expenditure ($m nominal)

Forecast Operating Expenditure	FY26	FY27	FY28	FY29	FY30	Total
Total	36.2	38.0	39.0	36.2	33.2	182.7

[7] Rule cl 6A.6.6(a)

Incentive arrangements

The regulatory framework includes incentive arrangements that provide rewards and penalties, depending on our performance. The incentive schemes encourage us to be more cost-efficient, and improve service standards for customers.

Basslink Pty Ltd is proposing the following:

- **Service Target Performance Incentive Scheme (STPIS)** – the STPIS provides incentives for TNSPs to improve or maintain service levels. Our proposal is to have the implementation of the STPIS consistent with the implementation of the STPIS on other transmission networks.
- **Capital Expenditure Sharing Scheme (CESS)** – the CESS provides a TNSP with incentives to improve capital expenditure efficiency. Basslink Pty Ltd is proposing the application of the CESS.
- **Efficiency Benefit Sharing Scheme (EBSS) –** the EBSS provides a TNSP with incentives to improve operating expenditure efficiency. Basslink Pty Ltd proposes not applying the EBSS to the first revenue period, but with the EBSS applying in subsequent revenue periods. This is because the application of the EBSS will produce uncertain outcomes rather than create genuine efficiency incentives on the business.
- **Demand Management Innovation Allowance Mechanism (DMIAM) –** The DMIAM provides a TNSP with research and development funding to trial demand management solutions. Basslink Pty Ltd is not proposing to apply the DMIAM due to the limited demand management opportunities available to Basslink.

More information on incentive arrangements be found in **Attachment 10**.

Cost Pass throughs

The Rules provide an avenue to pass through costs incurred by a Network Service Provider in prescribed or approved events beyond our control. This regulatory framework recognises that there are unpredictable events which may incur high costs to the service provider. Customers are protected from paying these high costs beyond our control in our allowances.

As informed by the current insurance market, we propose the following pass-through events for the 2025-30 period:

Insurance coverage event

Insurer's credit risk event

Natural disaster event

Terrorism event

Asset protection studies (related to the co-location of other infrastructure, both on-shore and offshore, such as offshore wind farm infrastructure)

The above pass-through events have also been informed by stakeholder engagement conducted with our customers where we consulted on the rising insurance costs and the risk of cost pass throughs.

When preparing the above pass-through events, our Proposal has been guided by, among other things, nominated pass through event considerations provided by the Rules.

Each of the above pass-through events has been nominated with the aim of promoting prudent and efficient risk mitigation so that we can safely, reliably and securely supply to our customers as far as practicably possible. More information on cost pass throughs is provided in **Attachment 11**.

Glossary

AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
Basslink Pty Ltd	Basslink
BSA	Basslink Services Agreement
Capex	Capital Expenditure
CESS	Capital Expenditure Sharing Scheme
DC	Direct Current
EBSS	Efficiency Benefits Sharing Scheme
GW	Gigawatt
GWh	Gigawatt hours
HVDC	High Voltage Direct Current
ISP	Integrated System Plan
MNSP	Market Network Service Provider
MW	Megawatt
MWh	Megawatt-hour
NEM	National Electricity Market
NER (Rules)	National Electricity Rules
NSA	Network Services Agreement (NSA)),
NSP	Network Service Provider
NSW	New South Wales
NTDC	Northern Tasmanian Development Council
Opex	Operational Expenditure
PTRM	Post Tax Revenue model
RAB	Regulatory Asset Base
STPIS	Service Target Performance Incentive Scheme
TAS	Tasmania
TMEC	Tasmanian Mineral, Manufacturing and Energy Council
TNSP	Transmission Network Service Provider
TRET	Tasmanian Renewable Energy Target
VIC	Victoria
WACC	Weighted Average Cost of Capital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