Basslink Conversion Application and Electricity Transmission Determination

Tasmanian Government Submission

February 2024

Tasmanian Government

1. Context

Basslink's development arose out of considerations by successive Tasmanian governments in the late 1990s regarding the State's next energy source. At that time, the sustainable supply of electricity from the State's hydroelectric system was in balance with demand and the State had no access to natural gas (as an energy substitute for electricity or as a source of fuel for electricity generation). After detailed considerations, the State opted to progress Basslink as its next energy source, and with Basslink, become a participating jurisdiction in the National Electricity Market (NEM)[1].

The competitive expression of interest process to seek a developer for Basslink, managed through the Basslink Development Board, had no in-built preference for the link to be progressed as either a regulated interconnector, or as a market network service provider (MNSP), as provided for under the-then National Electricity Code. However, what emerged from the competitive process was a MNSP model – the final shortlisted proponents had a preference for this approach because of the perceived risks arising from having the link progressed as a regulated interconnector.

Accordingly, Basslink was progressed by National Grid as an MNSP, with a suite of commercial arrangements negotiated between it and Hydro Tasmania to provide the commercial model for its development, rather than it being progressed at the expense of electricity customers in Tasmania and Victoria through regulated transmission pricing arrangements.

Because of the nature of those commercial arrangements, particularly the former Basslink Services Agreement, and the current Network Services Agreement, for the vast majority of Basslink's life, it has performed like a regulated interconnector[2] - it has been generally available at its full import and export capabilities, with flows northward and southwards being

[1] For a more detailed contextual understanding of Basslink's development, see:Chapter 1 of Volume 2 of the Independent Review of the Tasmanian Electricity Supply Industry, available at https://nla.gov.au/nla.obj-1863482070/view

[2] A primary difference under these agreements is that Hydro Tasmania has secured all of the interregional revenues arising from Basslink's operations (in return for the facility fee it pays to BPL), rather than these being made available to the market via settlement residue auctions.

determined by spot prices in Victoria and Tasmania, rather than flows being determined by those factors plus capacity bids from the link[3].

Since it commenced operations in 2006, Basslink has provided material benefits to both Tasmanian and Victorian customers, and the NEM more widely. In this context, the appropriateness of an equitable outcome for Tasmanian and Victorian customers arising from Basslink's conversion cannot be overstated.

Importantly, the strategic role that Basslink plays has shifted over time and continues to develop. It was initially conceived as an energy supply option and risk management tool for Tasmania, particularly in respect of hydrological risk, and as a means of providing transitional energy flows for major disruptions in the State's supply/demand balance, such as the potential closure of a major industrial customer in Tasmania.

As Australia moves through the energy transition, particularly the shift from firm thermal energy on the mainland to variable renewable production, the importance of interregional trading between Tasmania and Victoria, with our existing reliable deep storage and world-class untapped renewable reserves (both energy and capacity) becomes increasingly important. While Basslink will always be important to Tasmania, it is becoming increasingly important to the NEM, and particularly the Victorian region (as the adjoining NEM region). This is a key consideration in thinking about Basslink's future, either as a regulated interconnector or as an ongoing MNSP.

Ensuring that Basslink remains operational over its initial design life (around 2046) and beyond and can transmit electricity freely between Tasmania and Victoria is a NEM-wide strategic matter.

From Tasmania's perspective, the Government welcomes APA's acquisition of Basslink Pty Ltd, and the approach it has taken to both the interconnector assets and to its dealings with Tasmania. The Government supports the conversion of Basslink to a regulated

[3] For a relatively short period during 2022 whilst Basslink Pty Ltd was in administration, there were no commercial arrangements between BPL and Hydro Tasmania, and BPL made its own capacity bidding decisions. This coincided with a period of NEM-wide market instability, and accordingly, the operations of the link at that time are not necessarily representative of trading situations that would routinely face an unhedged MNSP-Basslink.

interconnector, so that it will operate within the economic regulatory framework under the AER's remit, making it like every other interconnector in the NEM.

In the Government's view, the regulatory path provides superior outcomes for Tasmania and Tasmanian electricity customers because:

- it ensures that there will be open flows of electricity between Tasmania and Victoria (retaining the outcome that has to date been delivered through commercial agreements between BPL and Hydro Tasmania but cannot be assured in the future), which is particularly relevant for hydrological risk management;
- it provides a stable revenue stream and a more financially secure commercial model for the ongoing operation of the link, and the benefits it brings to Tasmania, relative to the MNSP arrangements;
- it ensures a transparent process for scrutinising operating and capital expenditure for the link consistent with maintaining reliability over Basslink's useful life;
- it provides a customer-centric process for Tasmanian electricity customers (and those in Victoria) to express preferences on material issues that drive Basslink's performance and costs (such as the trade-off between reliability and costs, insurance, and risk appetite, as demonstrated in the regulatory proposal); and
- it will provide the path to a more appropriate allocation of the cost burden of Basslink, which currently fully sits with Tasmania via the commercial agreements between BPL and Hydro Tasmania.

For these reasons, the Government supports conversion of Basslink to a regulated asset. The next important consideration related to conversion is setting the initial regulated asset base. In this regard, the Government's support of APA's proposal is not unqualified.

The Government well-recognises that should the AER determine there is a case for Basslink to shift from being a MNSP to becoming a regulated link, then its cost burden will be redistributed – from Hydro Tasmania[4] to Tasmanian and Victorian electricity customers.

[4] In the Government's view, the ultimate incidence of the costs of Basslink remain with Hydro Tasmania under the BSA and the NSA. This is because Hydro Tasmania must bid competitively in order to be dispatched into Victoria and can't pass Basslink-related costs onto its Victorian positions. In the case of Tasmanian customers, the wholesale price factored into retail prices paid by small customers are set via a regulatory tool (which bases prices on Victorian contract prices and has no reference to Basslink-related costs), prices paid by C&I customers through retailers are referenced to those regulated prices or are regulated contracts in their own right, and the prices negotiated with major industrial users are commercially negotiated, again without reference to Basslink (or other) Hydro Tasmania costs.

This important issue has framed the Tasmanian Government's objectives for Basslink's regulation, which are:

- for Basslink to achieve conversion in a manner consistent with the National Electricity Objective and National Electricity Law and having regard to the interests of Tasmanian consumers, including by achieving a transmission revenue allocation outcome to Tasmania that is minimised and no more than the benefits that Tasmanian customers receive;
- for conversion to optimise the reliability, efficiency in maintenance and operation, availability, and performance of Basslink; and
- that the outcomes from the conversion consideration and the corresponding revenue determination to be not inconsistent with the Operational Requirements set out in the Basslink Operations Agreement as they currently apply.

These matters are taken up below.

2. Conversion

The Government agrees with the AER's framing of the conversion test as being a 'with or without' regulation question. An important aspect of determining the 'without' limb of the question is reaching conclusions about the counterfactual to regulation – what would the situation be for Basslink and customers if regulation was not approved?

What is known is that Basslink is now a MNSP and that there is a time-limited commercial agreement with Hydro Tasmania in place that sees the link physically operate like a regulated interconnector (the Network Service Agreement). Should the AER determine not to classify Basslink's network services as prescribed transmission services, it could not be simply assumed that a replacement agreement would be entered into by the parties, such that the link would operate as it has over the past 17 years.

As discussed above, there is no robust empirical evidence of how Basslink performs (in terms of flows), and what the outcomes for customers are, with Basslink operating as a genuinely merchant MNSP. Basslink has previously operated as an 'open link'. This presents a challenge that the AER must embrace. The historic flows across Basslink and the impacts on spot (and eventually contract) prices over the vast majority of its operations are indicative of the outcomes of a regulated interconnector because Basslink has been made available at a zero price difference, and, moreover, the actual bidding of market participants in Tasmania and Victoria have also reflected that fact. That omelette cannot be unscrambled.

The only approach available to understand how Basslink *might* operate in the future as an unhedged MNSP is modelling. That modelling would need to consider the strategic bidding behaviors of not only Basslink (in framing commercially optimal transport bidding strategies[5]), but also the corresponding impacts that would have on the bidding activities of market participants in both Tasmania and Victoria in response to those potential transport bidding strategies.

The Government notes that APA's application does not provide any insights into the outworkings of the 'without' regulation counterfactual and considers that this work should be undertaken as part of the consideration of the merits of conversion, so that all interested parties have a basis of information to work from.

As the AER points out in the Issues Paper (p.12), the answer to the question of whether the benefits of regulation outweigh the costs to consumers "*will in part be influenced by the value of Basslink's RAB [the AER] may consider appropriate were Basslink to be regulated. The greater the value of the RAB, the greater the regulated transmission charges. In turn, this means the greater the benefits need to be to make conversion worthwhile for consumers*".

The Government agrees and while, for the reasons noted above, it supports regulation of Basslink it also believes the without regulation counterfactual is an important consideration in considering the value of the RAB.

A related issue of relevance not addressed in the Issues Paper is whether it is reasonable for an asset owner to receive a windfall gain because of a change in status from a MNSP to a regulated link, especially in the context of any such windfall being at the cost of electricity customers.

The principal income stream to Basslink as a MNSP is the interregional price differences that can be obtained from flows across the link, which include opportunities for withholding transfer capability via transport bidding. BPL may be able to convert those revenues into other

[5] The MNSP framework enables the link operator to bid transport capacities (much like a generator bids its generation capability) that makes flows across the link conditional on price difference being at least as much as those bids. Conceptually, the dispatch engine assumes that no flows are available across the interconnector, but flows become possible according to the bidding of the interconnector. The transport bids can't drive up price differentials between regions (with spot prices in each connected region being based on bids within that region). Rather what they do is drive down the price differences that would have *otherwise* arisen in the absence of interconnection. In the case of Basslink, given its history of generally being made available at a zero price difference, a shift to transport bidding with positive values if the link becomes an unhedged MNSP could be interpreted as driving up price difference.

contractual revenue streams (as it has under the BSA and the NSA with Hydro Tasmania), but the IRRs are BPL's core business value.

In the context of Basslink, Marinus Link is expected to commence in 2030 (the first cable of 750MW), and by 2032, is expected to be operating as a 1500MW interconnector. Marinus Link will operate as a regulated link (ie free flows), and this will have a marked impact on the ability of Basslink operating as a MNSP to withhold capacity to drive price differentials (and therefore IRR revenues).

Plainly, the business value of BPL to its equity holders in its status of a MNSP will be highly contingent on the impacts of possible future interconnection, such as the proposed Marinus Link. The conversion application contains no information on this subject, and it is an important missing element. The Government does not have availability to undertake modelling that examines the business value of BPL as a MNSP, and therefore it is unclear whether APA as the owners of Basslink stand to receive a windfall gain from conversion.

Picking up the point made in the Issues Paper linking Basslink's potential RAB to the question of conversion, the Government is of the view that the asset value that informs the revenue setting process for Basslink should be set such that the overall present value of future returns to the equity holder should not be higher than that available to it under its status quo setting of an MNSP.

The proposed RAB of $831 million, which is founded upon the depreciated actual cost of Basslink, generates a revenue requirement of around $220 million for return on capital over the first 5-year determination period. This is around 40 per cent of the overall revenue requirement, and therefore customer cost impact, of $560 million over that period. In short, the allowed return on assets is the single largest driver of the cost consequences of Basslink's regulation for electricity customers.

The Government considers it important in making the case for conversion that it be demonstrated that the present value to APA from a regulated income stream of around $112 million pa average, of which some 40 per cent is from return of capital, does not present a windfall gain passed from electricity customers to equity holders of the asset.

The issue of the counterfactual is also relevant in considering the modelling of benefits of Basslink's conversion. The Government notes that the application does not present any such results – it makes the case for conversion on conceptual arguments.

However, APA has commissioned modelling from EY on the benefits of Basslink in support of the proposed RAB. That modelling seeks to show Basslink's market benefits as the difference in modelled market outcomes from two scenarios:

1. Basslink does not operate from 1 July 2025; and
2. Basslink operates as a regulated interconnector enabling free flows from that date.

This is the accepted methodology for considering a RIT-T for a new interconnector and is valid from the perspective that the only scenario under consideration for a new regulated link (like Marinus Link) is that the project proceeds as a regulated interconnector, or it does not proceed at all.

That plainly is not the case for Basslink, which has been operational for 17 years, and has a design life of 2046. The Government argues that the default scenario is that Basslink does continue to operate as a MNSP, at least up to the point that it can recover its operating costs and stay in business capital expenditure needs from IRRs through transport bidding. If modelling showed that at some point the value of IRRs were less than such requirements, the approach of modelling 'no Basslink' past that point could be a valid consideration in examining the benefits of Basslink in a regulated status versus the status quo.

In the context of considering conversion, the Government considers that the better approach would be to measure the difference between market outcomes of Basslink operating as a regulated interconnector from 1 July 2025 to that which could arise from Basslink being an unhedged MNSP from this date, but continuing to operate (as long as it remains commercial), rather than simply being turned off.

The modelling of market outcomes that assumes Basslink simply ceases to operate from 1 July 2025 overstates the benefits of Basslink, because in the pre-Marius period, it is assumed that there are no flows between Tasmania and Victoria, and that following Marinus, flows are lower because Basslink is assumed not to exist. If this is then contrasted to a situation where Basslink flows freely in these periods, it is perhaps unsurprising that there are large gross benefits derived from the modelling.

In reality, absent of regulation (the 'without' test), Basslink would bid to maximise revenue, which would suggest that there would be some flows, rather than no flows at all (modelling would be required to estimate the quantum). It appears inconceivable that APA would simply cease Basslink on 1 July 2025 ahead of Marinus Link, when it is the only potential provider of

interregional transfers – there is revenue to be made in doing so provided that the IRRs exceed operating costs. This may well extend past the timeframes for the two Marinus Link cables (if there are periods where despite MarinusLink there is price separation between Tasmania and Victoria).

Accordingly, some share of the purported benefit of Basslink will arise in the absence of Basslink being regulated, because the 'no Basslink' is not a realistic scenario, particularly in the pre-Marinus period. Even if flows under an unhedged MNSP model were just half of those modelled under a regulated model, a good proportion of the purported benefits of a regulated Basslink would still be delivered[6].

At this time, there is no modelling available to enable interested parties to have any insight into what could be possible in that regard. There is nothing in the regulatory application that establishes that even after phase 1 or phase 2 of Marinus Link that it would be commercially unviable to continue to operate Basslink.

What is required to address these issues is an enhanced understanding of the incremental benefits to customers from regulation through modelling by APA of the 'no regulation' counterfactual. It may be the case that the net benefit test is still delivered, but at this time, there is insufficient evidence to establish whether this is the case, and most importantly, to consider whether the proposed revenue determination, and particularly the proposed asset value of $831 million should be applied, particularly given the enduring consequences this decision will have for electricity customers over the regulatory life of the asset.

For the avoidance of doubt, the Government is not arguing against Basslink becoming a regulated interconnector.

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[6] This is particularly important given the nature and size and timing of the modelled profile of benefits in the EY assessment. The largest annual modelled benefits of Basslink under that methodology are in the pre-Marinus period. Given the impact of discounting, this will heavily skew the measured present value of benefits overall. If those benefits are actually materially lower, because they are just the incremental benefits arising from regulation relative to the default MNSP scenario, the present value of regulation will be materially lower than the measured gross benefits of the link in its entirety. Importantly, a large proportion of those modelled benefits in this period are in the form of avoided capex (ie capex that would otherwise be required if there were no flows because Basslink does not exist). It appears highly unlikely that if Basslink was not regulated and continued as an MNSP, that this capital investment would be triggered, given the potential (and the Government argues, likely reality) that Basslink could trade and displace the need for that investment. By contrast the modelling assumes that absent regulation, that investment will be triggered, which overstates the benefits of regulation.

The Government is arguing that regulation is a preferable framework for Basslink, because of the reasons argued in Section 1. What is critical in the conversion decision is the RAB that customers will ultimately fund, and that this should be determined having regard to two principles:

- it should not provide a windfall return to the equity owners of Basslink relative to the status quo; and
- it should be set such that the incremental benefits to customers from regulation (over the status quo) are not greater than the costs that they will face arising from conversion.

At this time, it is entirely unclear whether the proposed regulated asset base of $831 million, based on APA's assessment of the depreciated actual cost of Basslink is supportable having regard to these principles, and therefore whether the proposed revenue for the link, of around $110 million per annum is reasonable. The process needs to shed light on this.

3. Revenue allocation

The regulatory proposal contains several options in relation to the way in which Basslink's AER-determined Aggregate Annual Revenue Requirement (AARR) would be shared between Victoria and Tasmania. Those options include:

- a geographic approach, where the allowable revenue would be allocated in proportion to the physical location of the assets; or
- an energy-flow model, where the allowable revenue would be allocated in proportion to measured flows across the link (over some period of time); or
- a market-size approach, where the allowable revenue would be allocated based on the number of connections in each region.

Revenue allocation and the NER

In the Issues Paper (p.30), the AER argues that clause 6A.29.1(b) of the NER requires that the allocation of Basslink's AARR must be allocated between Victoria and Tasmania according to 'use'. That clause states:

> *Each transmission Network Service Provider must determine the Aggregate Annual Revenue Requirement (AARR) for its own*

transmission system assets which are used to provide prescribed transmission services within each region.

The Tasmanian Government considers that clause to be unhelpful in providing any guidance on revenue allocation methodologies.

The whole of clause 6A.29 deals with the situation where there are multiple TNSPs within a single region, which will be the case in Tasmania should Basslink become a TNSP[7]. Clause 6A.29.1(b) requires that where there are multiple TNSPs in Tasmania, that each TNSP must determine the AARR for its own (ie no other TNSP) assets that are used to provide prescribed transmission services within Tasmania. The reference to 'within each region' in the clause pertains to the services provided, not the assets that are used to provide those services. This implies that the clause *does not* direct the revenue allocation to be geographically based[8].

In the case of Basslink, all Basslink's network assets[9] are required to provide transmission services in Victoria (including the assets located in Tasmania), and similarly, all its assets are required to provide transmission services in Tasmania (including those located in Victoria).

The Government argues that the purpose and effect of clause 6A.29.1(b) is to indicate that:

- BPL can't include the costs of assets for MurrayLink or DirectLink in relation to Basslink's allowable revenues, because they are not <u>used</u> to provide those services into Tasmania; and

- BPL is precluded from recovering revenue for assets that it may own but are not <u>used</u> to provide transmission services in either Victoria or Tasmania.

The Government agrees with the AER that the NER does not provide any guidance on what the term 'use' might mean and does not provide a methodology for determining the proportions of the 'use' of an interconnector in each region.

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7 TasNetworks will be the coordinating TNSP, there will be Basslink, and potentially Marinus Link.

8 If that was intended, then the clause would have been written differently – presumably it would read "… for its own transmission system assets within each region which are used to provide prescribed transmission services within each region. It is noted that the Issues Paper does not seek to establish that the clause requires a geographical approach.

9 The connection assets to the Tasmanian network, the Tasmanian convertor stations, the sub-sea cable, underground and overhead cables and the Victorian converter stations and the Victorian converter station.

Given this, and the point above, the Government argues that the NER does not provide any helpful guidance in ruling in or out any revenue allocation methodology.

The appropriate revenue allocation model

The Government is firmly of the view that if the AER determines that Basslink should be converted, then the market-size approach should be implemented to allocate the AER-determined annual revenues for this interconnector.

APA's regulatory application highlights that on balance, the preference expressed by stakeholders in aggregate (i.e. considering customers in both Victoria and Tasmania) was for the market-size approach to be adopted.

In this context, the Government's view about revenue allocation is well-aligned with that of consumers in both jurisdictions. The vast disparity between the market-size of Victoria and Tasmania is a well-recognised issue in relation to fairly recouping the costs of interconnection between the two regions.

In relation to Basslink, the market-size approach proposed by APA, which on APA's numbers, would result in an annual cost of $11 per customer in Victoria and $8 per customer in Tasmania (those estimates have not been tested by the Tasmanian Government) provides an outcome that would deliver fairness in outcomes between customers in both regions. Like customers would face similar pricing consequences.

By comparison (and again using APA estimates), a geographic approach would see Tasmanian customers paying seven times more than Victorian customers, and an energy-flows approach would see Tasmanian customers facing six times more than Victorian customers.

It is difficult to see how either of these outcomes would represent a fair or equitable outcome for an asset that has been in operation for 17 years, meeting the energy needs of Victoria and Tasmania alike. In the context of conversion, the highest weighting should be given to equity.

What is particularly important is that the above models have been robustly tested with consumers in both Victoria and Tasmania as part of APA's stakeholder engagement approach in preparing its regulatory application.

If equity is to be given a lower weighting in the consideration of revenue allocation models, and noting the absence of any material guidance in the NER, the Government argues that

the next-best approach would be to base the revenue allocation on the prospective benefit share of the Basslink over the balance of its operating life.

As noted above, as Australia moves through the energy transition, the role of interconnection between Victoria and Tasmania will increasingly be about Tasmania's deep hydro storages providing the much-need firming capability the remainder of the NEM needs as it is increasingly supplied by non-firm renewable generation. Flows across the link will increasingly reflect the cycle of lower value (but abundant) renewable energy in the NEM (via Victoria) effectively being stored as deferred hydro production in Tasmania, and then re-accessed by the NEM via hydro production in Tasmania. That is not to suggest that Basslink would provide no benefits to Tasmania, rather the balance of benefits will be materially fall to the NEM. A value-weighted flows approach would provide some insight into this matter, but at this time, the regulatory application does not contain this information.

Net revenue to be recouped through transmission charges

The regulatory proposal sets out the proposed gross revenue requirements for Basslink. What is of keen interest to many stakeholders is the consequences of Basslink's regulation for the transmission costs that they will face in their electricity bills. Those bill impacts will be a function of:

- the overall revenue requirement (the AARR);
- the revenue allocation arrangements between Victoria and Tasmania; and
- the value of the IRRs and potential subsequent settlement residue auction proceeds arising from flows across the link, which will be allocated directionally.

Currently, stakeholders have no visibility in the regulatory application of the potential future likely proceeds from IRR/SRA proceeds. While this might not be directly relevant to the AER's requirements to set the AARR (and may be seen as unnecessary for present purposes), the absence of this information means that participants are only partly informed about the potential consequences of Basslink's regulation for them. The Government considers that the consultation process would be enhanced by modelling being provided on the potential value of IRRs and the impacts that those estimates would have on the ultimate transmission costs faced by different classes of electricity customers in each of the two regions.

4. Revenue Requirements

Tasmania has always wanted Basslink's owner to operate the interconnector efficiently and effectively and to continue to invest in the asset to ensure its ongoing sustainable operations. The previous arrangements, which were founded upon commercial agreements between the asset owner and Hydro Tasmania, has demonstrated shortcomings. Economic regulation by the AER, through transparent and open processes, provides the path to ensure these outcomes are delivered in the long-term interests of Tasmanian energy consumers, as well as customers in the NEM more widely.

Basslink Operations Agreement (BOA)

The BOA was originally negotiated with Basslink's developers, National Grid and the Tasmanian Government, as a foundational document for the project.

The BOA is effectively the contract between the State and BPL that requires BPL to operate Basslink until 2046 (its initial design life) and for it to meet agreed performance standards. It provides a regime for the State to require BPL to minimise and cure defaults.

The position taken by the Government during BPL's insolvency and subsequent sale was that the BOA will continue to be a necessary and enduring document, whether Basslink becomes a regulated interconnector, and that is reflected in the Agreement.

With respect to APA's submission, the BOA requires the operation of the interconnector until 2046 and sets out the high-level requirements for BPL's maintenance and disaster recovery practices and availability.

The Tasmanian Government is supportive of prudent and efficient operating and capital expenditure over the life of the asset that contributes to the requirements contained within the BOA.

Among other things, the BOA requires BPL to:

(a) Operate and maintain Basslink and the Basslink facilities in accordance with:
   i. Good Electricity Industry Practice; and
   ii. The Operator's then applicable Maintenance Plan and Disaster Recovery Plan.

The Maintenance Plan means BPL's plan for maintaining the operational integrity of Basslink including its spare parts retention plan during the Term in accordance with Good Electricity Industry Practice, as updated from time to time.

The BOA picks up the meaning of Good Electricity Industry Practice as that provided under the NER.

In section 8.4 of its submission document to the AER (p. 187), APA has outlined its subsea cable repair strategy and forecast costs. Given the importance of Basslink to energy security in Tasmania, the Government is supportive of the step change in the subsea cable repair strategy detailed in the regulatory application, and welcomes APA's proactive approach in managing this issue. While the BOA sets the maximum repair times allowed before a default can arise, those cure periods do not express the Government's preferences about how long BPL should take to effect a repair. Rather, they are the periods that have been contractually agreed before the matter is escalated to a default under the BOA. The Government's preference is that cable failure is addressed as expeditiously as possible, and that the regulatory framework should provide the resources and incentive for this to occur.

System Protection Scheme

On pp. 189 of the submission document, APA notes that, "*An allowance for costs associated with a System Protection Scheme (SPS) may also need to be added, depending on the outcome of a review that is underway regarding the future operation of the SPS*."

The System Protection Scheme (SPS) is also referred to on pp. 40 of the AER's Issues Paper.

The SPS consists of two schemes, the Network Control System Protection Scheme (NCSPS) and the Frequency Control System Protection Scheme (FCSPS). The NCSPS manages critical transmission line contingencies within the State while the FCSPS manages the contingent loss of the interconnector. These were critical schemes that formed one element of the selection process for the Basslink proponent as part of the Basslink Development Board's process and are required given the nature and scale of Basslink relative to the Tasmanian electricity system.

Based on the experience gained through the Basslink NCSPS, TasNetworks has proposed a more generalised Tasmanian NCSPS and this has formed part of its 2024-2029 revenue determination. With that whole-of-state approach being implemented, the need for a specific Basslink NCSPS will be obviated.

The FCSPS is required for Basslink due to the size of the disturbance arising from a trip of the link and the ability of the balance of the Tasmanian system to respond. Without the

FCSPS Basslink would be constrained to 144MW, the maximum allowable contingency size as defined by the Tasmanian Frequency Operating Standard (FOS).

With the FCSPS in place, if the link trips in northward flow, there are instantaneous generator tripping arrangements that manage the frequency response in the Tasmanian system to be within the FOS. Similarly, if the link trips in southward flow, there are instantaneous load tripping services to maintain the FOS.

As noted in the regulatory application, while BPL is the beneficiary of the FCSPS (in that it enables the asset to connect to the Tasmanian network and achieve flows in both directions at greater than 144MW), because of the commercial model that has historically applied to Basslink, BPL has not been involved in the commercial arrangements that procure the load tripping services, and the generator tripping is currently provided by Hydro Tasmania at no cost to BPL.

There is policy work underway in Tasmania looking at possible future models for the procurement of load tripping services in Tasmania, in light of a range of factors, including the potential regulation of Basslink, the development of Marinus Link, and the development of large scale on-island renewable generation, which may well exceed 144MW. On the status quo, each of these assets would need to procure load tripping services on a bilateral basis with individual counterparties. The policy work is exploring if a centralised procurement model would lead to lower cost and more efficient and more sustainable outcomes than the current arrangements and how such a procurement model could be implemented.

Regardless of the outcome of this work, the Government considers that the procurement of load and generator tripping services (through the Basslink SPS directly, or through a whole-of-state approach) is a legitimate cost to Basslink in order for it to operate above 144MW in either direction. Accordingly, the Government is of the view those costs should form part of Basslink's overall allowed operating expenditure under a regulated interconnector model on the same basis as all other operating costs incurred in delivering the prescribed transmission services. They are not Tasmania-specific costs because they are required to achieve transfers above 144MW in either direction. The alternative of those costs not being recoverable would be to restrict Basslink flows in both directions to 144MW, which would materially reduce the benefits of the link to the NEM (and the regulatory value of the interconnector).

Control and protection system

A significant component (nearly 60 per cent) of the proposed capital spending program over the first revenue period is the hardware and software of the control and protection system. APA is proposing that the system be replaced in the 2025-30 period, to ensure safe and reliable operation. It argues that this timing has been informed by feedback from customers during the consultation process.

From the Government's perspective, the reliability of Basslink will always be important, but particularly so in the pre-Marinus period when it is the only source of interconnection. Accordingly, as a matter of principle, the Government supports this ultimately-necessary work being undertaken and funded through the revenue determination in the first revenue period.

That said, this project has been valued at $44.2 million, so the Government would support close scrutiny of the proposed costs by the AER from the perspective of prudency and efficiency.