

5 February 2025

Ms Clare Savage  
Chair  
Australian Energy Regulator (AER)

Submitted via email: [resetcoord@aer.gov.au](mailto:resetcoord@aer.gov.au)

Dear Ms Savage

### **Basslink Conversion Application: Draft Determination**

Hydro Tasmania welcomes the opportunity to respond to the Australian Energy Regulator (AER) on the Basslink Conversion Draft Determination.

Hydro Tasmania disagrees with the conclusions of the Draft Determination not to convert Basslink to a regulated asset. Conversion is the only pathway to Basslink's full availability, utilisation, and accessibility for the market. A regulated Basslink provides the certainty needed to ensure efficient interregional trade, mitigate systemic market risks, and support the ongoing energy transition.

This means that regulation of Basslink by the AER, with the resulting minimisation of risk and maximisation of competition in generation and storage, will result in the lowest costs to consumers.

Regulation will also ensure that the Marinus project is developed in the knowledge that Basslink will operate at maximum availability and asset life. This will result in the most efficient investment decisions on the two stages of Marinus Link, also at the lowest cost to consumers.

The AER's draft decision is based on counterfactual assumptions that should be reconsidered against current market realities. If the assumptions are appropriately adjusted, the case for regulation becomes clear, rather than being "finely balanced." Specifically:

1. The determination assumes that a contract between Basslink and Hydro Tasmania could achieve similar outcomes to regulation, but this does not reflect commercial realities. The conditions that enabled past agreements no longer exist, and merchant operation is the realistic counterfactual when assessing the benefits of regulation.
2. Hydro Tasmania would have strong incentives to strategically bid to maximise the value of any contract that involved it acquiring bidding rights. Any scenario other than regulation will result in less utilisation of the link.
3. The benefits of regulation are underestimated due to assumptions about Marinus Link. Given investment decision delays and likely schedule changes, an open-access Basslink remains

critical for interregional reliability and renewable integration.

4. Strategic bidding of an unregulated Basslink could significantly increase Victorian wholesale electricity prices. Analysis of AEMO pre-dispatch data indicates prices could have increased by approximately 20 percent in 2024 had Basslink been operating as a merchant interconnector instead of 'open access'.
5. The conversions of Murraylink and Directlink took into account the benefits that certainty of open interconnectors bring to the market. The ACCC and AER respectively recognised that the only certain way to ensure an open link is through regulation and certainty promotes investment.
6. The continued operation of the Frequency Control System Protection Scheme (FCSPS) is critical to Basslink's full availability, but there is no certainty of how it will operate under merchant regime. A regulated framework provides certainty to ensure the scheme continues to facilitate full utilisation of the link.
7. The determination may be irreversible. Failure to regulate now could permanently undermine interconnection certainty, discourage investment, and introduce inefficiencies that harm the long-term interests of consumers.

Hydro Tasmania urges the AER to reconsider its draft determination in light of the evidence produced for the counterfactual cases, and recognise that the benefits of regulation are in the long-term interests of consumers. Regulation would ensure a transparent, reliable and efficiently utilised interconnector that supports market stability and Australia's energy market transition. Please see the following Appendix for the detail of Hydro Tasmania's submission.

Hydro Tasmania appreciates the AER's consultative approach and would welcome the opportunity to discuss this submission. Please contact John Cooper ([REDACTED]) if you would like to discuss.

Yours sincerely



Richard Bolt  
Chairman

## Appendix

### 1. Counterfactuals

The AER has considered some possible counterfactuals to conversion, including Basslink operating as an unhedged merchant interconnector, or Basslink's owner contracting its capacity to Hydro Tasmania to be bid as a merchant interconnector by Hydro Tasmania.

Hydro Tasmania has no plan to extend the current NSA which results in Basslink being bid as an open link.

APA has stated that if the draft decision is confirmed as final, "APA will seek to maximise the value of the asset, in the best interest of APA's investors, by progressing our plans to trade Basslink capacity in the spot market<sup>1</sup>". It is clear from this statement that APA has no present appetite for a services agreement with Hydro Tasmania and intends to operate the link to maximise the value for shareholders rather than customers.

Accordingly, merchant operation should be the counterfactual that the AER uses when assessing the benefits of conversion in its final determination.

If APA's incentives change in the future and they do have a willingness to contract with Hydro Tasmania or another party, it is inappropriate to assume any future contract would require Basslink's capacity to be bid at (or near to) zero and fully available as an open link. In this regard we ask the AER to base its final determination on the following premises:

- The original Basslink Services Agreement (BSA) was a 25-year transaction and far from anything that could be considered today. It was intended to facilitate construction of Basslink and NEM entry for Tasmania and it was not subject to any ACCC authorisation. The agreement (including bidding provisions) was negotiated in that context.
- The existing Network Services Agreement (NSA) was established as part of the resolution to a long-running dispute related to Basslink's previous ownership. The agreement provided a transitional framework that maintained market certainty by retaining consistent bidding provisions from the BSA. APA agreed to a short-term revenue stream below its long-term income expectations, based on an expectation that regulation would be approved.
- These historic contracts should not be used to draw inferences about what bidding provisions are likely to feature in any hypothetical future agreement that Hydro Tasmania and the owner of the link may negotiate, because the context for any future negotiation, however unlikely, will be very different to those historical circumstances.
- The AER should not assume that a Ministerial Notice related to Basslink bidding would be reissued if Hydro acquired bidding rights; especially in the case of unrestricted exports to Victoria. The previous Ministerial Notice was issued under unique circumstances to support Tasmania's NEM entry. It placed no restrictions on positive bidding on northwards flows

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<sup>1</sup> APA ASX announcement, 17 December 2024, <https://www.apa.com.au/news/asx-and-media-releases/aer-releases-draft-decision-on-basslink-regulation-proposal>

consistent with the focus of the ACCC at that time<sup>2</sup>. There is no policy basis or commercial incentive for Hydro Tasmania to prioritise exports under an unregulated model. If intervention were considered necessary to maintain open flows, it would highlight the risks of merchant operation, and therefore the commerciality of acquiring bidding rights, further justifying the case for using the unhedged merchant operation as the counterfactual to conversion.

- The parties' incentives and assessments of value in any hypothetical future contract will differ, which may result in no commercial 'meeting of the minds' sufficient to result in any agreement, or only in short term contracts addressing a specific risk, strategy or market opportunity.
- Hydro Tasmania does not expect it will be commercial to contract with Basslink upon Marinus Link 1 commissioning and even less so with anticipation of Marinus Link 2.

Adjusting the counterfactuals based on these clarifications leads to a clearer and stronger case for conversion. The AER's current assessment does not reflect the reality of commercial incentives or contracting feasibility, reducing the validity of the Draft Determination's conclusions.

## 2. Interaction of Basslink Conversion and Marinus Link

The draft determination notes that Marinus Link Stage 1 will be operational in 2029 and Stage 2 in 2036, based on the Draft 2024 ISP. It did note that the final 2024 ISP has since adjusted these estimates, now forecasting Stage 1 for 2030 and Stage 2 for 2032. Despite treating Marinus Link as an "actionable ISP project," the AER acknowledges that transmission projects have historically faced delays, and all stakeholder submissions on Marinus Link timing noted that these assumed dates are likely optimistic.

The Final Investment Decision (FID) for Stage 1 has already been delayed to May 2025, and a decision on Stage 2 will not be considered until after FID on Stage 1. This uncertainty presents a contradiction in the AER's reasoning:

- If Marinus Link is delayed, the benefits of Basslink's conversion increase, as Basslink remains the primary interconnector ensuring interregional reliability.
- If only one Marinus cable proceeds, Basslink remains critical for system redundancy and balancing variable renewable generation.

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<sup>2</sup> In its NEM entry decision in 2001 (<https://www.accc.gov.au/system/files/public-registers/documents/D03%2B38178.pdf?ref=0&download=y2.2.4> – page 31) the ACCC said that it "believes that positive bidding of Basslink on northward flows of electricity raises less competition concerns than other forms of non-zero bidding. While a positive bid would allow Hydro Tasmania to export electricity at higher prices than at which it sells in Tasmania, Hydro Tasmania does not have a dominant position in the Victorian region. Consequently, Hydro Tasmania will bear the dispatch risk that a positive bid on Basslink will mean that it does not get the opportunity to export or, if it does, at a level below the maximum of 600MW."

- Contrary to the AER’s concerns, we anticipate that regulation would reduce the risk that Basslink will be stranded, because decisions on the timing of Marinus, particularly a second stage, would be conditioned by knowledge that Basslink’s economic life and availability has been maximised by regulation. Basslink is more likely to be stranded if it is forced to seek market revenues in competition with regulated links.

The ACIL Allen modelling indicates that Basslink conversion delivers net market benefits, particularly in scenarios where Marinus Link is delayed or only one cable proceeds. Even if Marinus Stage 1 is delivered in 2029 (or 2030 per the final ISP), Basslink regulation remains beneficial under many scenarios. Given the high risk of delays that attend to projects of this scale and complexity, the case for Basslink regulation today is considerably stronger.

Additionally, Marinus Link RIT-T modelling concluded that there is positive market benefit for both stages with Basslink assumed to be an open-access link, meaning its potential displacement as an unregulated MNSP has not been accounted for. The implications of this are major and serious:

- Regulating a new link (or pair of links) in preference to an existing merchant link is economically inefficient. ACIL Allen modelling notes that if Basslink operates as an MNSP, it “may struggle to meet its operating and maintenance costs if both stages of Marinus are developed.” This could force Basslink to exit the market entirely, creating an unnecessary loss of capacity, which could be replaced by new capacity earlier than otherwise required at a higher consequent cost to consumers.
- AEMO’s 2024 Integrated System Plan (ISP) highlights the \$142 billion investment challenge facing the NEM’s transition. This adds to the waste involved in stranding an existing asset in anticipation of future new infrastructure.

Building new interconnection while failing to support the efficient use of existing infrastructure by securing its operation as an open link would be an economically unjustifiable outcome.

### **3. Economic Impact of Reducing Link Capacity: Insights from AEMO Pre-Dispatch Data**

Hydro Tasmania has conducted a preliminary assessment of the potential spot market impacts of one potential approach to MNSP bidding. That is where the link is used in a strategy to maximise revenue by reducing utilisation. The analysis relies on AEMO’s 2024 pre-dispatch data as a proxy for prevailing prices, which reflects projected price sensitivities to changes in supply and demand —specifically by reducing capacity by 150 MW and 300 MW<sup>3</sup>.

The analysis highlights a clear incentive for strategic bidding of Basslink exports, which results in an economic cost to Victorian consumers. This incentive exists for BPL as a merchant interconnector and would also exist if Hydro Tasmania secured bidding rights under a contract. It must be assumed that any counterfactual with active link bidding will result in less utilisation of the interconnector than regulation.

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<sup>3</sup> This analysis is retrospective it has not factored in how other market participants would react to the change in behaviour of the interconnector.

By opportunistically reducing the links capacity by 150-300MW, the analysis shows increased export value could have been achieved. Key findings from the analysis comparing strategic bidding to an open link:

- Higher export revenue could have been achieved from strategic bidding:
  - Actual export value of Basslink in 2024: \$48.8 million.
  - Alternative scenario with strategic link bidding: \$67.4 million.
- Consumer cost impact in Victoria:
  - Victorian generation-weighted average price would have risen from \$101/MWh to \$119/MWh under this strategic bidding scenario.
  - Total wholesale electricity costs would have increased from \$4.4 billion to \$5.2 billion—an \$800 million cost increase to Victorian consumers.
- Market liquidity and reliability concerns:
  - Merchant operation of Basslink introduces uncertainty and potential for reduced liquidity in contract markets, leading to less contract availability and higher contract premiums. This would have a flow on impact to the cost of hedging products for retailers, placing upward price pressure additional to the underlying wholesale cost impacts.
  - Reduced certainty in Tasmania-Victoria energy flows weakens system resilience, making it harder to rely on Basslink for market and operational stability and increasing the risks arising from volatility.

Previously, the AER stated that "the Hydro Tasmania agreement counterfactual is likely to result in greater utilisation of the interconnector at times of northward flows compared to the merchant counterfactual, lessening the benefits of conversion." While there may be specific instances where Hydro Tasmania's bidding incentives lead to higher link utilisation, the revenue potential from greater price separation would create a strong commercial incentive for Hydro Tasmania to strategically bid if it had such rights.

#### **4. Assessing Market Efficiency Assumptions in ACIL Allen's Modelling**

The modelling provided by ACIL Allen showed significant overall and consumer benefits in the case of conversion, while the market benefits viewed in isolation create misleading conclusions—particularly in Table 3.3 of the Draft Determination.

##### *Economic Relativity of HT Trading vs. Merchant Operation in Table 3.3*

The negative values in the HT Agreement cases suggest a lower economic cost to the market, but this is based on a flawed premise. The modelling assumes that Hydro Tasmania's generation revenue would offset the value of strategic link bidding, creating an artificially efficient outcome. In reality, and as discussed above, Hydro Tasmania has strong commercial incentives to maximise price separation rather than prioritise full link utilisation, meaning the assumed market benefits of an HT Agreement are overstated.

*Key Observations from Table 3.3*

<b>Comparisons</b>	<b>Marinus Link does not proceed</b>	<b>1 Marinus Link cable proceeds (2029)</b>	<b>2 Marinus Link cables proceed (2029, 2036)</b>
Difference between Merchant Full & Extension	\$112M	\$115M	\$110M
Difference between HT Agreement Full & Extension	-\$171M	-\$174M	-\$172M

In addition, APA is ready to operate as a merchant interconnector. If Hydro Tasmania were able to contract the bidding rights it must be assumed the contract price APA would desire would reflect Basslink’s expected merchant revenues discounted for certainty. This means Hydro Tasmania would need to generate sufficient revenue to justify securing the bidding rights, which is only likely to be achieved through active link bidding – reinforcing that open access cannot be assumed.

## **5. Lessons from Directlink and Murraylink Conversions**

The history of regulatory conversions underscores the need for consistent treatment of interconnectors to promote efficiency, certainty, and public benefit. Two key examples—Murraylink and Directlink—provide critical context for understanding the issues at stake in Basslink’s proposed conversion.

- *Murraylink Conversion (2003)*

Murraylink applied for regulatory conversion just one week after commencing operations as an MNSP. The ACCC approved conversion in 2003, using the regulatory test as the basis for the exercise of its discretion.

The ACCC recognised the importance of consistency in assessing conversion and new regulated transmission (achieved via use of the regulatory test), enabling MNSPs to reduce the risk of investment by being able to convert on this basis, while ensuring that consumers are not paying for inefficient private investment, thereby encouraging efficient investment in both private and regulated interconnection.

During its assessment, the ACCC considered market feedback that MNSPs have a structural incentive to withhold capacity to maximise price differentials and acknowledged that the market had no entitlement to assume open operation from an MNSP unless regulatory conversion was granted. It noted the arguments put forward by the Allen Consulting Group that operating Murraylink on an

open access basis may provide a more certain environment for the planning of the national electricity grid<sup>4</sup>.

- *Directlink Conversion (2006)*

In assessing the conversion of Directlink, the AER took the view that it was appropriate to apply the same approach as the ACCC had in Murraylink (using the regulatory test), noting that to maintain an environment conducive to efficient investment it should not be setting a higher threshold for conversion than it would for new regulated transmission as doing so may be to the detriment of the long term interests of consumers<sup>5</sup>.

Submissions to the AER at the time raised additional concerns about the lack of transparency in MNSP operations and the potential for market power abuse, particularly where merchant operators could control bidding strategies and price separation. The ACCC again approved conversion, highlighting that the regulatory framework provided appropriate safeguards to balance market efficiency with public interest.

- *Relevance to Basslink*

Hydro Tasmania's Basslink Services Agreement (BSA) historically ensured predictable interconnector flows, functioning similarly to a regulated model. However, its termination exposed the market to significant risks, including strategic bidding, increased price separation, and unpredictable capacity availability. The NSA which was entered into following a short period of MNSP operation provides certainty of an open link until the end of June 2025. So unlike Directlink and Murraylink, the market did not have to face the fundamental lack of certainty regarding open operation at the time Basslink started operation, rather this point has been deferred until expiration of the NSA. However, at that point (June 2025), all the same concerns raised in the submissions on Directlink and Murraylink arise.

The historical approach to regulatory conversions highlights the importance of applying consistent principles to conversion and new regulated transmission, in order to support market efficiency, competition, and public confidence. A consistent approach to the historical regulatory conversions would support conversion of Basslink in the current circumstances.

## **6. The Basslink Frequency Control System Protection Scheme (SPS)**

Making Basslink's full capacity available to the market is only possible with the continued operation of the Frequency Control System Protection Scheme (FCSPS), which requires the procurement of large quantities of Tasmanian load and generation for tripping. The regulation of Basslink with a determination that includes a mechanism for procuring tripping to support the full flows of Basslink on an ongoing basis would provide certainty to the market that full import and export capability of Basslink is available to the market indefinitely (subject to loads and generators being willing to contract for these services).

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<sup>4</sup> Page 23 of the ACCC's final decision 1 October 2003

<sup>5</sup> Page 19 of the AER's draft decision 8 November 2005



- The FCSPS enables the tripping of Tasmanian generators to support the full export capacity of Basslink (594 MW). Basslink’s export capability would be limited to 144 MW if these generators were not provided.
- The FCSPS enables the tripping of major industrial loads in Tasmania to support the full import capacity of Basslink (478 MW). Basslink’s import capability would also be limited to 144 MW if these loads were not provided.

Hydro Tasmania has historically provided generator tripping services and contracted with loads to provide load tripping services to TasNetworks as a part of the FCSPS. In the context of the BSA and NSA, Hydro Tasmania had a commercial incentive to provide or procure these services. The current contract for generator tripping expires on 30 June 2025. Hydro Tasmania’s arrangements with the major industrial customers vary, but more than three quarters of the currently procured load tripping services expire on 31 December 2025.

The AER should not necessarily assume that the FCSPS will continue to operate in the same way in non-regulated scenarios, given that Hydro Tasmania would act commercially in considering any ongoing provision of generator or load tripping.

## **7. Long-Term Risks of Rejecting Basslink Conversion**

It is important to recognise that a decision to reject Basslink's conversion to a regulated interconnector may be permanent. There is no certainty that the owner would make a future application, so this may be the only opportunity to ensure ongoing open operation and highest utilisation of the link for its life. The effect of the NSA is that the current mode of operation remains very similar both to its operation under the BSA, and its expected operation under regulation (apart from some technical differences noted below) but only until June 2025.

On termination of the BSA, Basslink was an unhedged MNSP, and continuation of its current operational mode could not be assumed by the market. However, with the expectation that conversion to a regulated model was the long-term objective, the NSA was agreed upon as a pragmatic solution to maintain stability and defer the need to address the full legal and market implications until a final decision was made. If the AER’s final decision is not to regulate, the market will need to make a significant adjustment on conclusion of the NSA. Open access will no longer be guaranteed, and AEMO and market participants will have to manage less predictable and potentially less efficient access.

ACIL Allen’s analysis stated that “there would be no differences in the timing of capital costs associated with entry to and exit from the NEM regardless of whether Basslink is converted.” However, this assumption only holds true for investment decisions that do not rely on predictable access to Basslink. If open access is no longer guaranteed, uncertainty around interconnection may deter or delay new investments in generation and storage. This will not be limited to investments either, the Wholesale Contract Regulatory Instrument (WCRI) mechanism for consumer pricing in Tasmania also assumes an open access link.

The market will have to adjust its commercial operations to manage this heightened risk after years of predictability. The conversion of Murraylink and Directlink reflected a widespread market view that open access at zero price to interconnectors is strongly preferred, and that MNSP operation is fundamentally incompatible with the way the NEM was heading at the time of those conversions and

has continued to head since those conversions. This remains true, but is not stated in the draft determination, it should underpin the final determination.

Unregulated interconnectors also present unique challenges that amplify risks to the market. For example:

- Unlike regulated interconnectors, unregulated links are not subject to administered pricing mechanisms, creating misalignments during market suspension or price events.
- During counter-price flows, an unregulated Basslink could receive significant compensation—resulting in market inefficiencies that would not occur under regulation, as occurred in 2022.