Hydro Tasmania
The power of natural thinking

8 August 2014

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Australian Energy Regulator
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Sent via email: Transendrevenuereset@aer.gov.au

Dear Chris

Submission to Tasmanian Transmission Revenue Proposal

Thank you for the opportunity to respond to the Tasmanian Transmission Revenue Proposal (Revenue Proposal) as submitted by Transend (now TasNetworks) for the 2014-19 period.

As a generator with thirty hydro power stations and one thermal power station connected to the Extra High Voltage (EHV) system in Tasmania, Hydro Tasmania has a significant investment and interest in the continuing reliable, effective and economic provision of transmission services in Tasmania.

Overall Hydro Tasmania supports TasNetworks proposal to reduce costs to customers over the next reset period and their prudence over the last two years in not recovering the full maximum allowed revenue.

This position is consistent with reductions in capital intensive upgrade programs, the expectation of reduced demand forecasts and the current difficult economic conditions for customers. We anticipate that the synergy of including Transmission and Distribution functions within TasNetworks as well as improving economic outcomes will also improve operational delivery.

One of the significant factors influencing the Revenue Proposal is the assignment of the Weighted Average Cost of Capital (WACC) of 7.58 per cent by TasNetworks, this value is determined by utilising the AER methodology. As the WACC value directly impacts costs particularly on direct connected customers (including generators), the reduction of this value from historically higher levels is noted.

It is noted that the current Revenue Proposal identifies AEMC's Transmission frameworks review as a potential impact on connection arrangements for generators, but as at this stage the outcome is unknown, the proposal is based on the existing connection arrangements. Hydro Tasmania's view is that the implementation of Optional Firm Access (OFA) will incur significant market costs with no material benefit.

The following comments address some of the more detailed issues raised in the Revenue Proposal.

Forecasts

It is noted that in section 7.5.1 *Tasmanian Maximum Demand*, TasNetworks is predicting, "*the average growth rate in winter maximum demand for the next 15 years has increased slightly to 1.29 per cent per annum for the medium scenario".*
In contrast in the *National Electricity Forecasting Report (*recently prepared by *AEMO), chapter 7.4.1 table 13 (Tasmanian) Winter maximum demand* indicates only a 0.1 per cent increase per annum between 2014 and 2023 (ie 10% POE case*,* Maximum Demand in 2014 is 1756 MW and in 2023 is 1765 MW, minimal load growth over the 9 years indicated). Section 5.7.3 in the Revenue Proposal notes the differences between TasNetworks' and AEMO's forecast methodologies. Given the importance of the maximum demand forecast for network planning and the significant difference between the two forecasts we request TasNetworks to review these forecasts with AEMO.

Capital Projects:

The Newton-Queenstown Security Augmentation detailed in the Revenue Proposal, as it stands, has the potential to impact on the connection and operation of Hydro Tasmania's assets, namely John Butter's power station, the Upper and Lower Lake Margaret power stations near Queenstown and Newton Pumping Station. Hydro Tasmania is also concerned that the proposed reliability upgrade may impose a 14 million dollar impost on Tasmanian consumers. It is noted that significant recent reduction in local demand would render necessary a reassessment of the need and scope of this 14 million dollar proposed upgrade.

Hydro Tasmania would appreciate the continuing opportunity to be consulted on this project that potentially affects our operations in the area.

Hydro Tasmania notes the proposed Waddamana-Palmerston 220 kV Security Augmentation and recognises the importance of TasNetworks' efforts to reduce risks and impacts associated with potential loss or restriction of capacity on this key North-South transmission corridor. Due to the high capital costs forecast for this project, TasNetworks should be encouraged to explore non-network solutions as a more cost effective approach, leveraging on their considerable expertise in this area.

It should be noted that Hydro Tasmania provides a number of network support services to enable the efficient, secure and reliable day to day operation of TasNetworks' transmission network. These support services include voltage support, fault level support and inertia support. While Hydro Tasmania currently receives no payment for these services, the individual network support services provided by Hydro Tasmania obviate and/or defer the need for investment by TasNetworks in the Tasmanian transmission network.

Service Target Performance Incentive Scheme (STPIS)

Hydro Tasmania agrees with the principle of the Service Target Performance Incentive Scheme (STPIS) and the three components proposed by TasNetworks.

Service component: Hydro Tasmania supports the general proposal for a service component to provide a financial incentive to improve service levels. Given the recent capital upgrades it is hoped that the overall service reliability is improved and as such it would seem appropriate that the performance targets set for these parameters would have "stretch" targets rather than to be simply based on historic averages.

Market Impact component: TasNetworks move to include a Market Impact component is a positive move to ensure that the TNSP (Transmission Network Service Provider) is aware of not only the technical and physical impacts of outages but is also aware of the market impact. Hydro Tasmania expects that consideration of this component by TasNetworks will involve ongoing organisational learning and a more responsive approach to market issues.

Network capability component: Hydro Tasmania welcomed the opportunity of being consulted by TasNetworks' on the assessment of projects funded through the NCIPAP (Network Capability Incentive Parameter Action Plan).

TasNetworks was responsive and informative in providing information on the relevant projects and keeping us up to date on the progress of the proposals, as well as giving opportunities to provide further input. TasNetworks' consideration of the proposed project timings to minimise market impacts was appreciated.

As well as the NCIPAP projects finally proposed, TasNetworks also reviewed a number of other network augmentation projects proposed by Hydro Tasmania, which in the end didn't meet the market benefits test.

Other Issues

Management of stranded assets

One issue facing TNSP's in the future is that with potential reduction in demand, there is an increased risk of stranded assets, transmission assets that are no longer required to serve customers. As well as considering augmentation where additional assets are required, as a matter of principle it is suggested that it would be appropriate for TNSP's to also address and report on the issue of potentially removing assets or writing down the value of assets that were no longer required to serve customers.

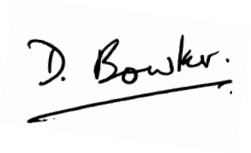
Optical ground wire (OPGW) Project

TasNetworks' expenditure totalled approximately $36 million[1] on establishing an extensive optical fibre ground wire network along the 220kV transmission backbone in Financial year 2013/14. In Hydro Tasmania's view this expenditure was questionable due to the market impacts and increased costs for Hydro Tasmania and other customers and did not seem to materially improve the level of service provided. Thus we have previously challenged numerous times whether the OPGW projects were in keeping with TasNetworks' (then Transend) key objective of the maintenance of existing service levels and the provision of transmission services at the lowest sustainable cost.

The above is an example of where closer scrutiny of past capital expenditure proposals should have occurred. Given the expenditure has occurred, should this expenditure remain in TasNetworks' regulatory asset base or consideration be given to remove these asset values from the regulatory asset base in accordance with S6A.2.3 of the National Electricity Rules (if deemed not contributing to the provision of prescribed transmission services).

If you have any questions relating to this response, please contact the undersigned on (03) 6230 5775 or by email david.bowker@hydro.com.au.

Yours sincerely



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[1] Available on page 16 of this link - https://www.tasnetworks.com.au/Aurora/media/pdf/Transend-Annual-Report-2013.PDF