

13 August 2024

The Office of the Tasmanian Economic Regulator
Level 3
The Treasury Building,
21 Murray Street, Hobart

office@economicregulator.tas.gov.au

Re: Review of the Approach to Regulating Retail Electricity Prices

Dear Mr Dimasi,

Thank you for the opportunity to comment on the Office of the Tasmanian Economic Regulator's Review of the Approach to Regulating Retail Electricity Prices.

We will restrict our comments to the future of Basslink and its potential implications for the setting of retail tariffs.

On 19 May 2023 Basslink submitted to the Australian Energy Regulator (AER) an application to convert Basslink to a regulated Transmission Network Service Provider (TNSP), from its current registration as a Market Network Service Provider (MNSP), and a request for commencement of a process as an Intending TNSP. On 15 September 2024 Basslink submitted a revenue proposal as an intending TNSP for Basslink to the AER, along with additional supporting information for its conversion application.

The AER will make a draft determination on conversion and the revenue proposal in October 2024 and a final determination on the conversion application in February 2024. Should the AER approve conversion, Basslink will become a regulated Transmission Network Service Provider (TNSP) on 1 July 2025.

As OTTER has identified, the current contract with Hydro Tasmania ends on 30 June 2025. It remains APA's preferred position that Basslink be converted to a regulated TNSP. However, if conversion is rejected by the AER, there are three counterfactuals to conversion:

- Basslink operates as an "unhedged" MNSP.
- Basslink contracts with a third party other than Hydro Tasmania.
- Basslink contracts with Hydro Tasmania.

We briefly discuss each of these outcomes and the possible impacts on the wholesale electricity or network charges below.

1. Basslink as a regulated TNSP

If Basslink becomes a regulated TNSP then we will charge Basslink's regulated revenue to the relevant Coordinating Network Service Providers, AEMO and TasNetworks, in accordance with the AER's determined Basslink Pricing Methodology. Under the National Electricity Rules TasNetworks will recover its share of these costs from distribution- and transmission-connected customers in accordance with its AER-determined Pricing Methodology.

Basslink will provide an estimate of the forecast revenue to be charged to TasNetworks as soon as possible after the AER's final determination in February 2025 in preparation for the commencement of the Regulatory Year on 1 July 2025.

It is our view that the current process as outlined by OTTER for the recovery of network tariffs in section 4.2 is sufficiently flexible that it will not need amendment should Basslink become a regulated TNSP.

We note that AEMO will pay settlement residue auction proceeds and charge negative inter-regional settlement residues to TasNetworks for the Victoria to Tasmania directional interconnector, created as a result of Basslink becoming a TNSP. Under the National Electricity Rules, TasNetworks will net off this net revenue against its regulated revenue when charging customers.

As a result, we anticipate that the bill impact on customers from Basslink's conversion will be materially lower than the per annum charges of \$8 per Tasmanian residential customer and \$15 per Tasmanian small business customer calculated by Basslink and quoted by OTTER. These quoted costs only account for the costs of Basslink and not the offsetting revenue from settlement residue auctions.

2. Basslink as an “unhedged” MNSP

An interconnector registered as a Market Network Service Provider earns revenue in the National Electricity Market equal to its loss-adjusted flow, multiplied by the difference between regional reference prices in the regions it connects. In this scenario, Basslink would seek to maximise revenue earned by optimising Basslink flows as a function of spot prices.

Broadly speaking, this will result in a reduction of Basslink flows compared to history, where Basslink's full capacity has been made available to the market at a \$0 difference between Victorian and Tasmanian prices. In turn, holding other factors constant, a reduction in Basslink flows would result in an increase in pool prices in Tasmania and Victoria.

Absent a contract of the nature of the existing Network Services Agreement (or the preceding Basslink Services Agreement), Hydro Tasmania will not have access to a financial product which effectively allows some of its generation to “earn” the Victorian pool price. We note that the current mechanism that the OTTER uses to determine the wholesale electricity component uses Victorian forward electricity prices, and this method may not be robust to a change to Basslink's operations and contracting strategy.

3. Basslink contracts with a third party other than Hydro Tasmania

In this scenario, APA Group contracts dispatch rights for Basslink to a market participant other than Hydro Tasmania. This market participant would optimise the bidding of Basslink capacity to maximise its portfolio revenue and manage market risk. As in the scenario of unhedged MNSP operation:

- This scenario will likely result in a reduction in Basslink flows compared to history, where its full capacity has been made available to the market at a \$0 difference between Victorian and Tasmanian prices.
- In turn and holding other factors constant, a reduction in Basslink flows would result in an increase in pool prices in Tasmania and Victoria.
- Hydro Tasmania will not have access to a financial product which effectively allows some of its generation to “earn” the Victorian pool price.

We note that the current mechanism that the OTTER uses to determine the wholesale electricity component uses Victorian forward electricity prices, and this method may not be robust to a change to Basslink's operations and contracting strategy.

4. Basslink contracts with Hydro Tasmania

If Basslink's capacity was to be contracted to Hydro Tasmania under an arrangement similar to the existing Network Services Agreement, then the proposed OTTER methods for estimating network and wholesale electricity cost are likely robust. Basslink notes that there is currently no consideration of an extension to the existing Network Services Agreement with Hydro Tasmania.

5. Conclusion

In conclusion, the proposed arrangement for recovery of Network Charges does not appear to need any adjustment in the event Basslink becomes a regulated TNSP.

However, the approach for the calculation of the wholesale component of the retail electricity prices is not robust to a number of scenarios in the event Basslink does not become a regulated interconnector. Notably, under the majority of scenarios, Hydro Tasmania does not have access to a financial product to allow some of its generation to "earn" the Victorian regional reference price.

We are happy to discuss the matters raised in this letter with OTTER further. If you have any questions or wish to discuss these matters further, please contact Mark Allen on mark.allen@apa.com.au.

Sincerely



Mark Allen.
Senior Regulatory Manager
APA