



Hydro Tasmania
the renewable energy business

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Dr John Tamblyn
Chairman
Australian Energy Market Commission
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Dear Dr Tamblyn

Draft National Electricity Amendment (Pricing of Prescribed Transmission Services) Rule 2006

Thank you for giving us the opportunity to discuss the Draft Rules with you late last week. That discussion was very useful and has given us a much better understanding of the manner in which the Commission expects its latest transmission pricing proposal will operate in practice.

I would also like to thank you for allowing us additional time to incorporate the outcomes from that discussion into our formal submission.

I now enclose Hydro Tasmania's formal submission in relation to the Draft National Electricity Amendment (Pricing for Prescribed Transmission Services) Rule issued on 19 October 2006 ("**Draft Rule**"). The Submission has been divided into two parts for ease of reference.

Part A deals with Hydro Tasmania's main concern in relation to the operation of the Draft Rule. Part B then deals with a number of drafting issues.

Hydro Tasmania would appreciate the opportunity of a further discussion with the Commission concerning the various issues raised in the attached submission. If you have any questions in the meantime, please contact John Arneaud on 0408 589 513 or by email on john.arneaud@hydro.com.au.

Yours sincerely



David Bowker
Manager Regulatory Affairs

DETAILED SUBMISSION

1. **Outline of Hydro Tasmania's remaining concerns**
 - 1.1 Hydro Tasmania considers that the new Rules are likely to have greater impact on Hydro Tasmania (as compared to other Generators) due to the unique nature of Hydro Tasmania's generation portfolio and the manner in which its power stations are connected to the Tasmanian *transmission system*.
 - 1.2 Because a hydro electricity power station must by definition be located at the relevant water source and its generating capacity is subject to the limitations of that water source, Hydro Tasmania has a number of smaller power stations located in relatively isolated locations.
 - 1.3 Some of these power stations are connected via radial transmission lines which also serve a relatively small customer load within the vicinity of the power station. Those radial lines are currently treated (and have been historically treated) under the current Rules as part of the 'shared' *transmission network*.
 - 1.4 In particular, because those radial lines are used for multiple purposes, they do not meet the current test in Schedule 6.2 of the Rules for entry assets. That is, under the current Rules for an asset to be treated as an entry asset, the asset must be 'fully dedicated to providing *connection* to a single *Generator* or group of *Generators connected* at a single point within the *transmission network*'.
 - 1.5 This is just one example of where Hydro Tasmania's unique connection arrangements may give rise to unintended results under the Draft Rules.
 - 1.6 Hydro Tasmania is still concerned that the application of the Draft Rule to some of its connection arrangements could potentially result in Hydro Tasmania paying significantly higher entry charges than is currently the case under the existing Rules.
 - 1.7 However, Hydro Tasmania also understands from the Draft Determination (see point 2 below) and its subsequent discussions with the Commission that this is not the Commission's intended outcome under the Draft Rules.
 - 1.8 Hydro Tasmania asks the Commission to give effect to this intention when making its Rule Determination by including:
 - (a) further savings and transitional provision in new clause 11.6 which will ensure that the new Rules will operate in a manner which is consistent with this intention; and/or
 - (b) further explanations and examples in its Rule Determination which confirm this intention and explain in more detail how the new Rules will give effect to this intention.
 - 1.9 The Submission has been divided into two parts for ease of reference. Part A deals with Hydro Tasmania's main concern in relation to the operation of the Draft Rule. Part B deals with a number of drafting issues.

Part A - Main Concern With Draft Rule

2. Our understanding of the Commission's intention

2.1 Hydro Tasmania notes that the Commission believes the current Rules broadly ensure that the appropriate parties are paying the appropriate amount for transmission services¹. In particular, the Draft Rule is based on a number of key propositions, including:

- (a) confirming the broad acceptability of the approach to pricing in the existing Rules;
- (b) confirming that existing arrangements may largely continue to apply; and
- (c) providing certainty regarding pricing outcomes².

2.2 The comments in the Draft Determination concerning the Commission's view about the likely outcome of the new causation-based cost allocation approach also suggest that no substantial change in pricing outcomes is intended. The Commission suggests that 'to the extent changes from the status quo occur' these 'should be relatively minor'³.

2.3 Hydro Tasmania's submission therefore takes (as a starting point) that the design of the new pricing rules should not deliver outcomes which are significantly at variance to the current position.

2.4 Further, to the extent that outcomes of that nature may result, it is appropriate that these outcomes should be avoided either by changing the drafting of the new pricing rules or by including further provisions in the new pricing rules (such as additional savings and transitional provisions) which will ameliorate these outcomes in particular instances.

3. Application of new clause 11.6.3 to Hydro Tasmania

3.1 The entry services provided to Hydro Tasmania under its existing *connection agreement* with Transend will be deemed to be *prescribed transmission services* for the purposes of new Chapter 6A⁴.

3.2 Those entry services will be *prescribed transmission services* under the deeming provision because those services are being provided using assets included in the

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¹ Draft Determination, paragraph 2.4.1 at 24.

² Draft Determination, paragraph 2.4 at 24.

³ Draft Determination, paragraph 4.1.4 at 43.

⁴ Deemed under clause 11.6.11

regulatory asset base of Transend under its revenue determination in force on 9 February 2006.

- 3.3 Subject to our comments in paragraph 3.4 below, the services would therefore also be 'transitioned *prescribed entry services*' (for the purposes of new draft clause 11.6.3) because they are being provided under a 'transitioned *connection agreement*' (i.e. a *connection agreement* entered into on or before 24 August 2006 which provides that prices for those services are to be calculated and determined in accordance with applicable pricing rules under the NER as in force from time to time).
- 3.4 In this regard, Hydro Tasmania asks the Commission to confirm that a pre 24 August 2006 *connection agreement* which defines the agreed boundaries of the *connection assets* in relation to each *connection point* covered by that *connection agreement* would be classified as a 'transitioned *connection agreement*'.
- 3.5 As you are aware a *connection agreement* can provide that prices are to be calculated and determined, in accordance with applicable pricing rules under the National Electricity Rules, and by reference to the agreed *connection assets* for each *connection point* detailed in that *connection agreement*.

4. **Why Hydro Tasmania believes there may be potential for a price shock**

- 4.1 The potential for price shocks arises from the new approach taken in the Draft Rule to attributing costs to transitioned *prescribed entry services*. Hydro Tasmania has been concerned that this approach differs in important respects from the method of allocating categories of *transmission system* costs set out in Schedule 6.2 of the current Rules.
- 4.2 Hydro Tasmania's principal concern has been that the transitional provisions will mandate cost allocations which could result in a significant proportion of the cost of some shared *transmission network* assets (for example radial lines) which are presently being treated as part of the shared network, being attributed to the provision of transitioned *prescribed entry services*. If this was in fact the result of the new transitional provisions, Hydro Tasmania entry charges would be significantly increased.
- 4.3 Following our discussions with the Commission we understand that this concern is intended to be addressed in the manner set out in paragraph 5 below.

5. **Use of the term 'transmission network connection point' in clause 6A.22.5(a) and clause 11.6.2**

- 5.1 During our recent discussion with the Commission, it appeared that the Commission was suggesting that Hydro Tasmania was unlikely to suffer a price shock in the general circumstances outlined above if its *connection agreement* contained an agreed point of *supply* which supported the current treatment of the relevant *transmission system* asset (eg a radial line of the type referred to in paragraph 1.4 above).
- 5.2 Hydro Tasmania has assumed for the purposes of this Submission that this position is based on the reference in draft clause 6A.22.5(a) to the new concept of a '*transmission network connection point*'.

- 5.3 If Hydro Tasmania is correct in this assumption (and in its understanding of the Commission's comments), we ask the Commission to explain this concept in more detail in its Rule Determination. In particular, we would like the Commission to comment on the specific issues outlined below in paragraphs 5.4 to 5.11.
- 5.4 As the Commission is aware, the current Rules define a '*connection point*' to be the agreed point of *supply* (i.e. the agreed point of delivery of electricity) established between a *Network Service Provider* and a *Network User*.
- 5.5 In Hydro Tasmania's experience whilst this term could be used to define an agreed point of *supply* on the *transmission network*, it has more commonly been used to define the point of *connection* between the relevant *Network Users* assets and the *transmission system* (i.e. the point of *connection* between the relevant *Network Users* assets and the relevant *connection assets* being provided by the NSP).
- 5.6 It is also quite common for a *connection agreement* to define the agreed boundaries of the *connection assets* for an identified *connection point* by reference to the *connection point* and the point at which the relevant *connection assets* connect to the shared *transmission network*.
- 5.7 It appears to follow from the approach outlined in paragraphs 5.5 and 5.6 above that the boundary between the *connection assets* and the shared *transmission network* will now be defined as the *transmission network connection point*. Could you please confirm that this understanding is correct.
- 5.8 Given that the term '*transmission network connection point*' is a new definition, Hydro Tasmania asks the Commission to provide further details concerning how this new type of *connection point* will be identified in the case of existing *connection agreement* (which may not have established an agreed point of *supply* with the *transmission network* in these exact terms).
- 5.9 As noted in paragraph 5.7 above, this definition appears to be referring to the same point as the agreed boundary between the *connection assets* for a particular *connection point* and the shared *transmission network*. If this is correct, it would also appear to follow that this agreed boundary should be relevant to the determination of the *attributable connection point cost share* for a *transmission network connection point* under draft clause 11.6.2 (because it provides clear evidence as to which of the TNSP's existing assets are directly attributable on a causation basis to the provision of *prescribed entry services* at the relevant *transmission network connection point*).
- 5.10 If the assumptions outlined in paragraphs 5.6 to 5.9 above are correct, Hydro Tasmania asks the Commission to make this clear in draft clause 11.6.2. In other words, if a pre 24 August 2006 *connection agreement* establishes the agreed boundary between the *connection assets* for a *connection point* and the shared *transmission network*, draft clause 11.6.2 should make it clear that this will be used to establish which of a TNSP's existing assets are directly attributable (on a causation basis) to the provision of *prescribed entry services* at a *transmission network connection point* as at 24 August 2006.

Part B - Drafting and Clarification Issues

6. Clarifying the process under clause 11.6.2

6.1 The Draft Determination suggests that as at 24 August 2006:

'assets currently in existence are attributed to prescribed service categories on a directly attributable (i.e. causation) basis *at that point in time*, and take existing generation and load as given. This means each TNSP would need to make an assessment, for each transmission asset within their RAB, as to the provision of which prescribed transmission service or services would necessitate (i.e. 'cause') the presence of that asset were the asset to be developed on that day.'

6.2 A number of issues arise from this statement. These issues are explained in paragraphs 7 to 9 below.

7. How do clause 11.6.2 and the 'priority ordering' provisions interrelate?

7.1 Both draft clause 11.6.2(a) and draft clause 6A.24.2(d) operate as adjustments or modifications to what would otherwise be the workings of the attributable cost share rules in clause 6A.22.4(a). The issue is how draft clause 11.6.2 and 6A.24.2(d) are intended to operate together.

7.2 Clause 6A.22.4(a) is made 'subject to any adjustment required under the principles in clause 6A.24.2'. It is therefore clearly made subject to the latter clause.

7.3 However, it is not clear that clause 11.6.2 is anything other than a **causation** test designed to say which of existing assets as at 24 August 2006 are to be regarded as attributable (in a causation sense) to providing a category of services.

7.4 The clause says nothing about how much of the **cost** of the asset identified as directly attributable to the provision of a service is then to be allocated to that category of services.

7.5 We have assumed that where an asset in existence as at 24 August 2006 is to be regarded as directly attributable to the provision of more than one category of *prescribed transmission services* (applying draft clause 11.6.2) then the issue of how much of the cost of that asset is to be attributed to each category remains to be determined by clause 6A.24.2(d).

8. How does clause 11.6.2 relate to clauses 6A.22.4 and 6A.22.5?

8.1 On its literal wording all that draft clause 11.6.2(a) does is to require the TNSP to work out in respect of each asset in existence as at 24 August 2006 what the asset is being used for, and to ask itself whether a particular asset can be said to be 'directly attributable (on a causation basis)' to the provision of a category of services as at that date.

8.2 Draft clause 11.6.2(a) does not then go onto explain how this 'snap shot' should be feed back into draft clause 6A.22.4(a).

- 8.3 Presumably where an asset is directly attributable to more than one category of *prescribed transmission services* the 'priority ordering' rules for the determination of the stand-alone amount will apply instead.
- 8.4 Since Part J is to be applied on an annual basis to come up with the price for *prescribed transmission services* the implication from clause 11.6.2 seems to be that the causation snapshot taken as at 24 August 2006 attributing assets to various classes of services on that date is to apply for all time thereafter when working out the *attributable cost share* ratio each year.
9. **Does draft clause 11.6.2 clarify the intended operation of the causation test?**
- 9.1 Draft clause 11.6.2 provides no further explanation as to how one determines whether an asset is 'directly attributable (on a causation basis)' to a category of services.
- 9.2 The Rules themselves continue to say little about what is meant by determining whether something is 'directly attributable' to another thing on 'a causation basis'. In particular, the Draft Rule says nothing about how the dividing line is to be drawn between that which is 'directly attributable' to a category of services and that which is not.
- 9.3 It seems to be necessarily implicit in draft clause 11.6.2 that an existing asset may be 'directly attributable' to the provision of more than one category of services (i.e. if this was not the case, it would follow that the 'priority ordering' provisions would be redundant).
- 9.4 What the clause does **not** do is tell the TNSP how it is to make that judgment or what criteria are to be applied in forming that judgment. That remains completely unexplained in the rules. This means that a TNSP's judgment in this regard is effectively unconstrained.
- 9.5 Hydro Tasmania's believes that the TNSP should be required to exercise this judgement in a fair and reasonable manner after taking into account the terms of the relevant *connection agreement* and in particular, any terms of the relevant *connection* provisions which operate to established an agreed point of *supply* with the shared *transmission network*.
10. **Draft Clause 11.6.2 applies only for purposes of Part J**
- 10.1 Draft clause 11.6.2 is drafted so that it applies only for the purposes of Part J (i.e. the clause modifies or clarifies the 'directly attributable' test used in the definitions of '*attributable cost share*' and '*attributable connection point cost share*'. However, it appears that the rules in Part J do **not** apply to the pricing of transitioned *prescribed entry services*.
- 10.2 The new transitional provision (i.e. draft clause 11.6.3(b)) makes it clear that the rules in Part D for calculating and determining prices for *negotiated transmission services*

are to apply instead of the rules in Part J. That is, the cost allocation rules under Part G are to apply for this purpose⁵.

- 10.3 The cost allocation rules under Part G do **not** 'pick up' or apply those found in Part J. Unless this is corrected, it seems that draft clause 11.6.2 offers no protection at all to Hydro Tasmania.

11. **Draft Clause 11.6.3 - Prices for prescribed entry services under existing agreements**

- 11.1 The Commission now believes that where the 'cause' of a transmission asset is determined to be an entry service, the pricing framework should be consistent with the pricing and cost allocation framework introduced for negotiated transmission services⁶.

- 11.2 Hydro Tasmania considers that there are still a number of uncertainties which arise from the adoption of the new pricing framework by the Commission, and the drafting of new draft clause 11.6.3. These uncertainties are outlined in paragraphs 12 to 18 below.

12. **Is the process mandatory?**

- 12.1 The first uncertainty is whether this process is intended to be mandatory (i.e. are the rules for calculating and determining prices for negotiated transmission services in the circumstances covered by draft clause 11.6.3(a) mandatory?) .

- 12.2 There are some indications in the Report that the process is intended to be mandatory⁷. However the clause says that those rules 'may' be applied which suggests an element of discretion. If so, who makes the decision whether they apply or not? Is it at the election of the TNSP or do both parties have to agree? If not mandatory, what is to happen if those rules are not applied?

13. **Impact on existing rights if process is mandatory**

- 13.1 If the Commission intends to set a mandatory process for fixing prices for transitioned *prescribed entry services* under transitioned *connection agreements*, then this may have the effect of defeating a 'change of law' renegotiation provision in a transitioned *connection agreement*. Hydro Tasmania understands that these provisions are relatively common in early NEM *connection agreements*.

- 13.2 If the method for fixing prices in draft clause 11.6.3(b) is mandatory it may negate the effect of this type of clause.

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⁵ Clause 11.6.3(c) of Draft Rule.

⁶ Draft Determination, paragraph 4.1.4 at 44.

⁷ Particularly at Draft Determination, paragraph 4.1.4 at 44.

14. Uncertainty about how Part D negotiation process operates

- 14.1 The second uncertainty relates to what the Commission intends by the statement in draft clause 11.6.3(b) that the 'rules for calculating and determining prices for *negotiated transmission services* in Part D of Chapter 6A may be applied to transitioned *prescribed entry services* for that purpose'.
- 14.2 The issue is how you apply the provisions of Part D for that purpose. Hydro Tasmania can see at least two possible ways in which Part D could be applied for this purpose under draft clause 11.6.3(b).
- 14.3 Part D is not easily applied where there already is a *connection agreement* between a TNSP and Generator, and where a service is already being provided. Part D presupposes that there is a provider of a service and someone who wishes to receive that service from the provider. It sets out the framework for negotiation of the price for the future provision of the service, and a mechanism for determination of that price by commercial arbitration in default of agreement.
- 14.4 How is that to be translated to this situation? Is it envisaged that each year the TNSP will negotiate charges with the Generator according to a negotiating framework, and if they cannot agree on a figure the price will be determined by commercial arbitration? In other words, instead of a TNSP notifying charges by 15 May each year as under the current Rules will there be an annual negotiation about charges?
- 14.5 Or does the Commission envisage that each TNSP and Generator who are parties to a transitioned *connection agreement* will negotiate amendments to their *connection agreement* using the Part D framework to provide for the method of determining future prices for *transitioned prescribed entry services*?

15. Uncertainty about how cost allocation under Part G is to be applied

- 15.1 There are several issues which arise from the direction in draft clause 11.6.3(c) that:
- 'Transitioned *prescribed entry services* may be treated as *negotiated transmission services* for the purposes of cost allocation under Part G.'
- 15.2 These are:
- (a) Is it mandatory to apply the cost allocation rules in Part G?
 - (b) If so, how is this to be done?
 - (c) How, if at all, do the cost allocation rules under Part G and Part J interrelate?
 - (d) Are the changes to the causation-based cost approach in Part J, which are made by draft clause 11.6.2, also intended to apply to Part G? In other words is draft clause 11.6.2 also meant to qualify draft clause 11.6.3?
- 15.3 We comment below on each of these issues.
- 16. Is the application of Part G mandatory?**

- 16.1 Clause 11.6.3(c) provides that transitioned *prescribed entry services* 'may' be treated as *negotiated transmission services* for the purposes of cost allocation under Part G.
- 16.2 Is this intended to be mandatory or discretionary? The use of the word 'may' suggests the latter, but some comments in the Report suggest the former.
- 16.3 If it is not mandatory, who makes the decision whether they apply or not? Is it at the election of the TNSP or do both parties have to agree? If not mandatory, what is to happen if the Part G cost allocation procedures are not applied? Does Part J apply instead?

17. How can Part G be applied?

- 17.1 If it is mandatory to apply the cost allocation rules in Part G by treating a transitioned *prescribed entry service* for this purpose as if it was a *negotiated transmission service* (which for all other purposes it is **not** under the Rules), then how is this to be done?
- 17.2 While in Part G the *Cost Allocation Principles* (with which the *Cost Allocation Guidelines* and through it the *Cost Allocation Methodology* must be consistent) include the principle that only costs which are directly attributable to the provision of a particular category of transmission services may be allocated to it⁸, Part G does not otherwise contain the 'directly attributable (on a causation basis)' test found in Part J and draft clause 11.6.2.
- 17.3 Given this, Part G does not provide the protections which the Commission suggests in the Draft Determination would 'appropriately address' the concerns previously expressed by Hydro Tasmania.
- 17.4 Until the TNSP's *Cost Allocation Methodology* for the purposes of Part G is approved by the AER⁹ it will be unclear how the TNSP proposes to allocate costs to a particular category of transmission services.

18. How, if at all, do Part J and Part G inter-relate?

- 18.1 As presently drafted, clause 11.6.2 applies only to, and qualifies, the pricing rules in Part J (see paragraph 10 above). Since draft clause 11.6.3 directs that pricing for transitioned *prescribed entry services* provided under transitioned *connection agreements* must take place by applying Part D and the cost allocation under Part G, it would appear these provisions operate quite separately¹⁰.

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⁸ Rule 6A.19.2(3)(i).

⁹ Under Rule 6A.19.4. This will not happen until some point after 28 March 2008.

¹⁰ Except insofar as the *Cost Allocation Principles*

- in Rule 6A.19.2(5) provide that the same cost may not be allocated more than once; and
- in Rule 6A.19.2(7) provide that costs which have been allocated to *prescribed transmission services* must not be reallocated to *negotiated transmission services*.

- 18.2 The Rules should clarify that draft clause 11.6.2 also qualifies clause 11.6.3.
19. **When will the new Rules commence to be effective?**
- 19.1 Hydro Tasmania understands that the new Rules will first be applied in its case from 1 July 2009 (i.e. at the expiry of Transend's current regulatory control period under its existing ACCC revenue determination).
- 19.2 Clause 11.6.3 of Chapter 11 of the Rules says that, subject to this rule 11.6, 'old Part C', including Schedule 6.2, continues to apply for the duration of a current regulatory control period. Hydro Tasmania assumes that this position will be maintained under the final Rule.

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This may mean that costs attributed under Part J to *prescribed transmission services* may not therefore be attributed to transitioned *prescribed entry services* which are treated under draft clause 11.6.3 as *negotiated transmission services* for the purposes of pricing those services under Part G.