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Level 9
99 Gawler Place
Adelaide SA 5000
Postal Address:
GPO Box 2010
Adelaide SA 5001
T 1300 858 724
F 08 8410 8545

Commissioners Philip Weickhardt & Wendy Craik
Electricity Network Inquiry
GPO Box 1428
CANBERRA CITY ACT 2601

Email: electricity@pc.gov.au

Dear Commissioners

Electricity Network Regulation - Nuttall Consulting Report: Victoria over-capacity review

AEMO welcomes the opportunity to contribute to the Productivity Commission's (PC) public inquiry (Inquiry) into electricity network regulation.

As we pointed out in our recent submission to the Inquiry, electricity prices have been rising over recent years and rising network investment costs have made a significant contribution to these rises. We demonstrated by our national energy forecasting project[1] that the scale of recent network investments are unjustified given the actual level peak demand and that particular projects that are in the pipeline are, given our forecasts, similarly unjustified.

We also argued that the statutory planning standards leads to uneconomic network investments. Deterministic redundancy standards encourage costly over-investment in network assets and low asset utilisation. In contrast an economic approach seeks to optimise existing capability of the network. Victoria is the only state that applies such an approach.

A comparison of the Victorian, Queensland and NSW transmission prices show us that all regions enjoyed similar transmission charges up until around 2006. After 2006 transmission prices in Queensland and NSW rose considerably in comparison to Victoria. This reflected a larger network investment program in the former jurisdictions. The large comparative increase in network expansion and associated cost increases is not in dispute. However, the reason posited by Grid Australia is that the Victorian network has "had excess capacity for much of the life of the NEM. [2] However, there was no evidence provided for this assertion.

Prior to NEM commencement, both the Victorian and NSW networks had excess capacity. Historically, both states invested in high cost, high capability 500 kV infrastructure, some of which was not required. In contrast, Queensland had not engaged in such extensive network development and as a result, the Queensland network was at the time, highly efficient.

Today, we consider that things have changed. While the NSW network remains in over-capacity, many years of expensive network augmentation, along with many committed projects still in the pipeline, has meant that the Queensland network has become and is forecast to remain in over-capacity for many years to come. Meanwhile, more prudent investment decisions has caused the Victorian network to be the most efficient.

[1] As a result of our national forecasting review all jurisdictional planners have revised their forecasts downwards considerably.
[2] Grid Australia Response to First Interim Report, Transmission Frameworks Review, 27 January 2012 p. 7

We engaged Nuttall Consulting to explore this matter and prepare an independent expert report to confirm our view. On the basis of market operations and other data, Nuttall Consulting concluded that since 2006, the Victorian transmission network has been the most efficiently planned and operated network of the three assessed.

We believe that the reason for this reversal is that the incentives provided by the current network investment framework reward network owners for building and installing assets rather than provide network services. Furthermore, the asset focused planning standards, both deterministic or hybrid exacerbate this bias. In contrast an economic planning approach focuses on service provision and better matches the needs of customers with the prices they eventually pay.

We attach the Nuttall Consulting report along with the supporting data and calculations.

Yours sincerely

David Swift
Executive General Manager Corporate Development

Cc: John Pierce, Chairman, AEMC and Rainer Korte, Grid Australia

Attachments: Nuttall Consulting Report: Victoria over-capacity review and supporting documentation