



AUSTRALIAN ENERGY  
REGULATOR

GPO Box 520  
Melbourne VIC 3001  
Telephone: (03) 9290 1444  
Facsimile: (03) 9663 3699  
[www.aer.gov.au](http://www.aer.gov.au)

Our Ref: (46372 – D12/24515)  
Contact Officer: Mark Wilson  
Contact Phone: 08 8213 3419

15 February 2012

Mr John Pierce  
Chairman  
Electricity Supply Industry Expert Panel  
GPO Box 123  
Hobart TAS 7001

By email: [contact@electricity.tas.gov.au](mailto:contact@electricity.tas.gov.au)

Dear Mr Pierce

**Submission to Independent Review of the Tasmanian Electricity Sector – Draft Report**

The AER welcomes the opportunity to comment on the Electricity Supply Industry Expert Panel's draft report on its review of the Tasmanian electricity sector.

As you are aware, the AER monitors the wholesale electricity market and is responsible for compliance with and enforcement of the National Electricity Rules (Electricity Rules).

The AER has followed the Panel's progress on its review closely and provided detailed analysis on the issues raised by the Panel in its August submission to the Panel's issues paper. This short submission focuses on the market power issues raised in the draft report and highlights a link to the AER's rule change proposal for the economic regulation of networks.

**Market Reform**

As highlighted in the AER's submission to the issues paper, the AER considers there are problems with the structure of the wholesale market in Tasmania.

The AER strongly supports the Panel's work in considering options for reform. In our submission to the issues paper we said that structural reform is the most effective way to address market power and promote competition in generation and retail markets.

We also said that the panel should carefully consider all possible structural solutions in an effort to achieve competitive and efficient market outcomes in Tasmania.

The Panel states in its draft report that it also prefers a structural solution, and that Reform Path 2 is its preferred option. The AER supports further consideration of this option, noting that the Panel has yet to fully address a number of threshold issues. These include consideration of how other assets, including wind generation, the AETV gas plant and Basslink may be incorporated into Reform Path 2. A substantial amount of the detail involved in Reform Path 2 is still to be decided, which may overcome these potential difficulties.

In the event that a structural solution could not be implemented, a regulatory approach such as the auction of hedge contracts proposed under Reform Path 1 may be a necessary solution to the market power issues in Tasmania. However, as pointed out in the draft report, the effectiveness of this option hinges on there being a sufficient number of retailers to compete for contracts. Therefore, the AER considers that it is important that the Panel develops an option, or a fallback position, that would be robust in the event that the reforms do not establish or attract a sufficient number of retailers for a competitive market.

The AER does not consider reform path 3 to be a viable option for reform. The AER considers the intraregional congestion and disorderly bidding that would be likely to arise from implementing such an option would make it unworkable.

## Networks

With regard to the performance of the Tasmanian network service providers (NSPs), and in particular the tendency of Transend and Aurora to overspend their capital expenditure allowances, the AER notes that the current regulatory framework includes only limited incentives on NSPs to spend within their allowances. The current rules require that all actual capital expenditure incurred within a regulatory period be automatically rolled into the asset base at the start of the next period. From then, the NSP may earn a return on the capital expenditure regardless of whether the expenditure is efficient and/or prudent or is greater than forecast. The AER has submitted a rule change proposal to the AEMC (*Economic Regulation of Network Service Providers, September 2011*) which, among other things, strengthens the incentives on NSPs to maintain financial discipline.

The AER would be happy to discuss any implementation issues associated with the proposed reform paths as the Panel assesses options in arriving at its final decision.

If you have any questions regarding the information in this submission I would be happy to meet to discuss them. Please contact Tom Leuner on (03) 9290 1890 or Mark Wilson on (08) 8213 3419 in the first instance.

Yours sincerely



Andrew Reeves  
Chairman