APA submission

Providing flexibility in the allocation of interconnector costs rule change

July 2024

Australian Pipeline Limited ACN 091 344 704
Level 25, 580 George Street, Sydney NSW 2000
PO Box R41, Royal Exchange NSW 1225
P: +61 2 9693 0000 | F: +61 2 9693 0093
APA Group | apa.com.au

Ms Anna Collyer
Chair
Australian Energy Market Commission

Lodged online

1 August 2024

RE: APA Submission to the allocation of interconnector costs draft determination

Dear Ms Collyer,

Thank you for the opportunity to provide feedback to the AEMC's draft determination on a rule change proposal to enable flexibility in the allocation of interconnector costs across jurisdictions (draft determination). We support the objective of the rule change proposal.

APA is an ASX listed owner, operator, and developer of energy infrastructure assets across Australia. As well as an extensive network of natural gas pipelines, we own or have interests in gas storage and generation facilities, electricity transmission networks, and over 692 MW of renewable generation and battery storage infrastructure. Since October 2022 we have been the proud owners of the Basslink interconnector connecting Tasmania to Victoria.

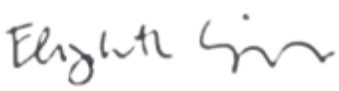
Interconnectors such as Basslink will play an essential role in the decarbonisation of the energy system. Following the Victorian coal power station, Loy Yang A, going off-line on 13 February this year, Basslink played an important role in keeping the lights on in Victoria by transporting hydro power from Tasmania, benefitting both states.

How the cost of interconnectors is shared across jurisdictions is one of the many challenging issues that must be resolved to enable the energy transition. To better align the interests of Basslink and its customers, in September 2023 APA applied to the Australian Energy Regulator (AER) to convert Basslink to a fully regulated asset.

APA is seeking to have Basslink become a fully regulated asset from 1 July 2025. The AEMC's draft rule, if made, would commence on 18 September 2025, which is after the proposed commencement of Basslink's revenue proposal. For this reason, we suggest that the AEMC consider including transitional provisions in the draft rule that would allow an interconnector cost allocation agreement to apply to Basslink from 1 July 2025.

If you wish to discuss our submission in further detail, please contact John Skinner on john.skinner2@apa.com.au or 0435 898 022.

Regards,



Beth Griggs
General Manager
Economic Regulation and External Policy

1 Executive Summary

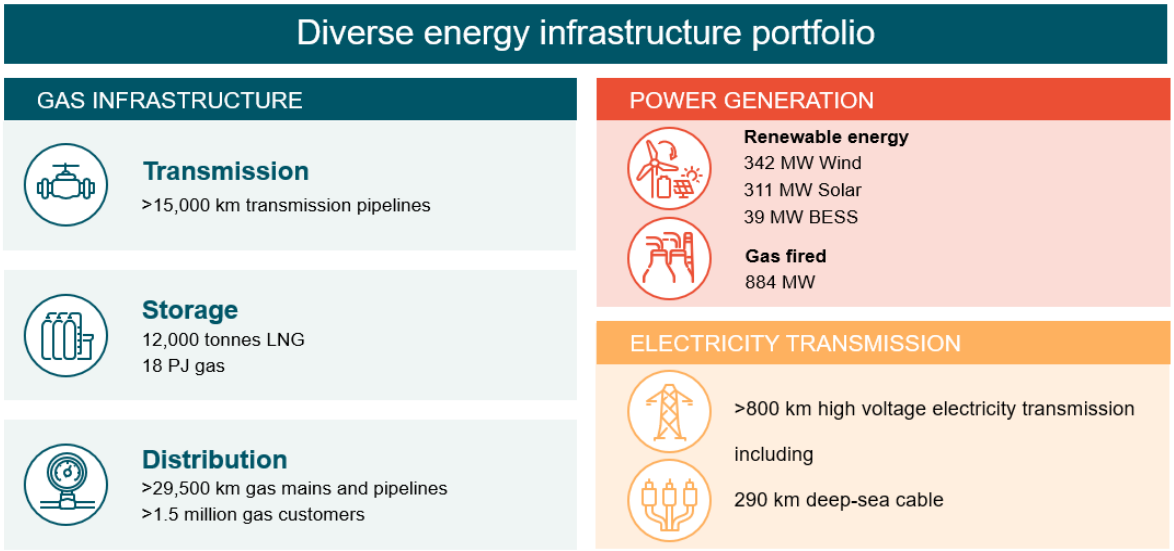
Key Points

- Basslink provides energy security for both Tasmanian and Victorian customers and is critical to helping Tasmania realise its renewable energy targets. Basslink does this for a lower cost than the alternatives.
- APA has applied to convert Basslink to a regulated asset. Regulation will better align the interests of Basslink and its customers and also allow energy consumers to have a greater say in the future operation of the asset.
- As drafted, the proposed rule could not apply to the first year of Basslink's proposed 2025-30 revenue period. The AEMC should consider including transitional provisions in the final rule that would allow an interconnector cost allocation agreement to apply to Basslink from 1 July 2025.

1.1 About APA

APA is a leading Australian Securities Exchange (ASX) listed energy infrastructure business. Consistent with our purpose to strengthen communities through responsible energy, our diverse portfolio of energy infrastructure delivers energy to customers in every Australian state and territory.

Figure 1: APA's infrastructure portfolio



Our 15,000 kilometres of natural gas pipelines connect sources of supply and markets across mainland Australia. We operate and maintain networks connecting 1.5 million Australian homes and businesses to the benefits of natural gas. And we own or have interests in gas storage facilities and gas-fired generation.

We also operate and have interests in 692 MW of renewable generation and battery storage infrastructure, while our high voltage electricity transmission assets connect Victoria with South Australia, New South Wales with Queensland and Tasmania with Victoria.

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APA acquired the Basslink interconnector in October 2022 and our objective is to support communities, businesses and customers with an energy system that is reliable, affordable, and low emissions. The acquisition of Basslink added a third electricity interconnector to APA's energy infrastructure portfolio, consistent with our strategy to expand our electricity transmission assets.

As outlined in further detail below, in September 2023 APA applied to have Basslink fully regulated and converted from a Market Network Service Provider (MNSP) to the Transmission Network Service Provider (TNSP). If approved, regulation will provide customers with a greater say over the future planning and operation of Basslink.

The proposed rule would commence on Thursday 18 September 2025, 12 months after the final determination is published. This is after the proposed commencement of Basslink's first five yearly revenue period on 1 July 2025. To ensure the proposed rule is as effective as possible, the AEMC should consider including transitional provisions a final rule that would allow a jurisdictional agreement to apply to Basslink from 1 July 2025.

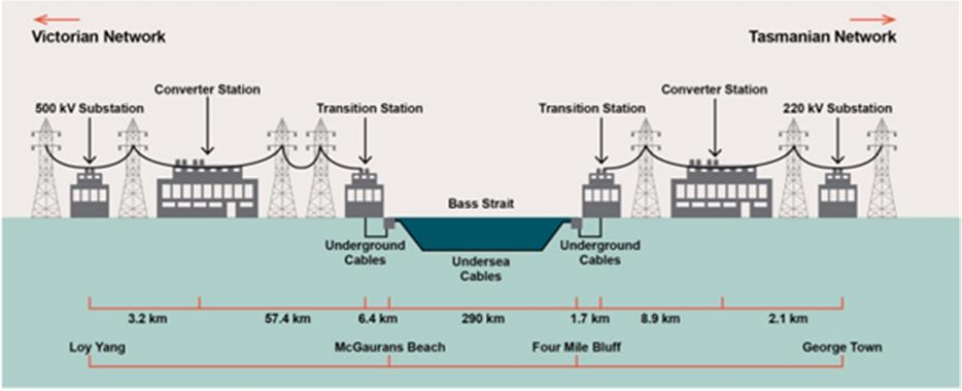
Extending the interconnection capacity between Tasmania and the mainland to allow variable electricity to move between jurisdictions is a critical part of creating a net zero future. Looking ahead, we encourage governments to investigate all options to deliver increased interconnection between Tasmania and the mainland. One option that could be investigated is augmenting Basslink to increase its current 500 MW capacity as a cost-effective means of increasing the supply of electricity between Tasmania and the mainland.

1.2 The importance of Basslink to Tasmanian and Victorian customers

Basslink is a 370 km long High Voltage Direct Current (HVDC) electricity interconnector between Victoria and Tasmania. Basslink starts at the Loy Yang switchyard in Gippsland (South-East Victoria) and travels by a 61 km high-voltage overhead transmission line until it is submerged. From there it travels for 290 km under Bass Straight at around 1.5 metres below the sea floor. It resurfaces again near George Town in Tasmania and travels another 11 km via a high-voltage overhead transmission line to the George Town substation.

National Grid was the developer of Basslink and the interconnector was commissioned in April 2006. The asset has a design life of 40 years.

Figure 2 – Assets that make up Basslink



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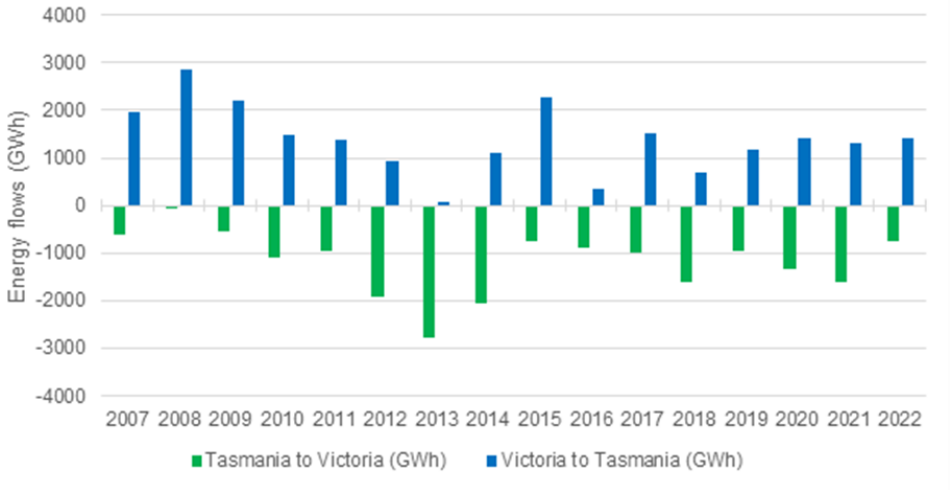
Basslink is currently the sole electricity interconnector between Tasmania and Victoria and plays a critical role in enhancing security of supply on both sides of Bass Strait.

Basslink remains the single largest alternative energy source for Tasmania after hydro-electric inflows and storages and is critical to meeting the State's energy security requirements. Basslink delivers reliable and diverse power supply to consumers and businesses in Tasmania and Victoria, to the benefit of both states. As shown in Figure 3, in an average year, energy flows from Tasmania to Victoria are about the same as from Victoria to Tasmania:

Figure 3 – Annual energy flows across Basslink



The Tasmanian energy crisis of 2015-16 highlighted the important role that Basslink plays in maintaining energy security and protecting Tasmanian customers from high electricity prices.

Following an outage in late 2015, which coincided with drought conditions, the Tasmanian electricity grid was islanded for a period of approximately six months. As shown in Figure 4, electricity prices spiked, and customers had to pay prices of up to $250/MWh, several times the normal rate at the time.

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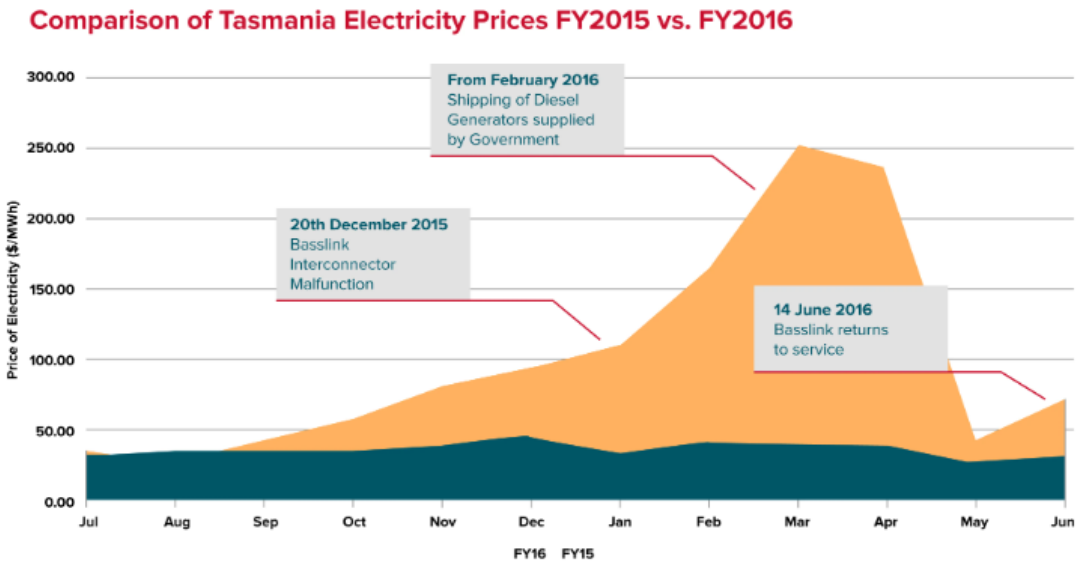
Figure 4 – inflated energy prices in Tasmania when Basslink was not operational



Basslink's important role was again demonstrated immediately following the Victorian coal power station, Loy Yang A, going off-line on 13 February this year.

Severe weather brought electricity lines down and tripped the state's biggest coal fired power stations. This left more than 500,000 homes in Victoria without power. Along with gas-fired power generation, hydro power from Tasmania stepped up to keep the lights on in Victoria by transporting excess power across Basslink, benefitting both states.

APA has shown its commitment to providing ongoing, reliable electricity by applying to the AER for Basslink's conversion to a regulated entity.

1.3 Why regulating Basslink better aligns the interests of APA and customers

APA is committed to delivering reliable and affordable energy for Tasmanian consumers and considers that the ongoing reliable operation of Basslink is critical to achieving this goal. As such, in September 2023 APA applied to the AER to convert Basslink from a MNSP to TNSP.

Put another way, APA is seeking to convert Basslink from being a merchant interconnector to a regulated interconnector.

While regulation is not always the right answer, APA is confident that converting Basslink to a regulated asset will ensure that it operates in an economically efficient manner as an 'open link' that maximises the energy transported between Victoria and Tasmania to the long-term benefit of customers.

In contrast to the current framework in place, regulation will better align the interests of APA and customers, provide greater certainty of costs and revenues, and allow customers to have a greater say in asset operation through the five-yearly regulatory process.

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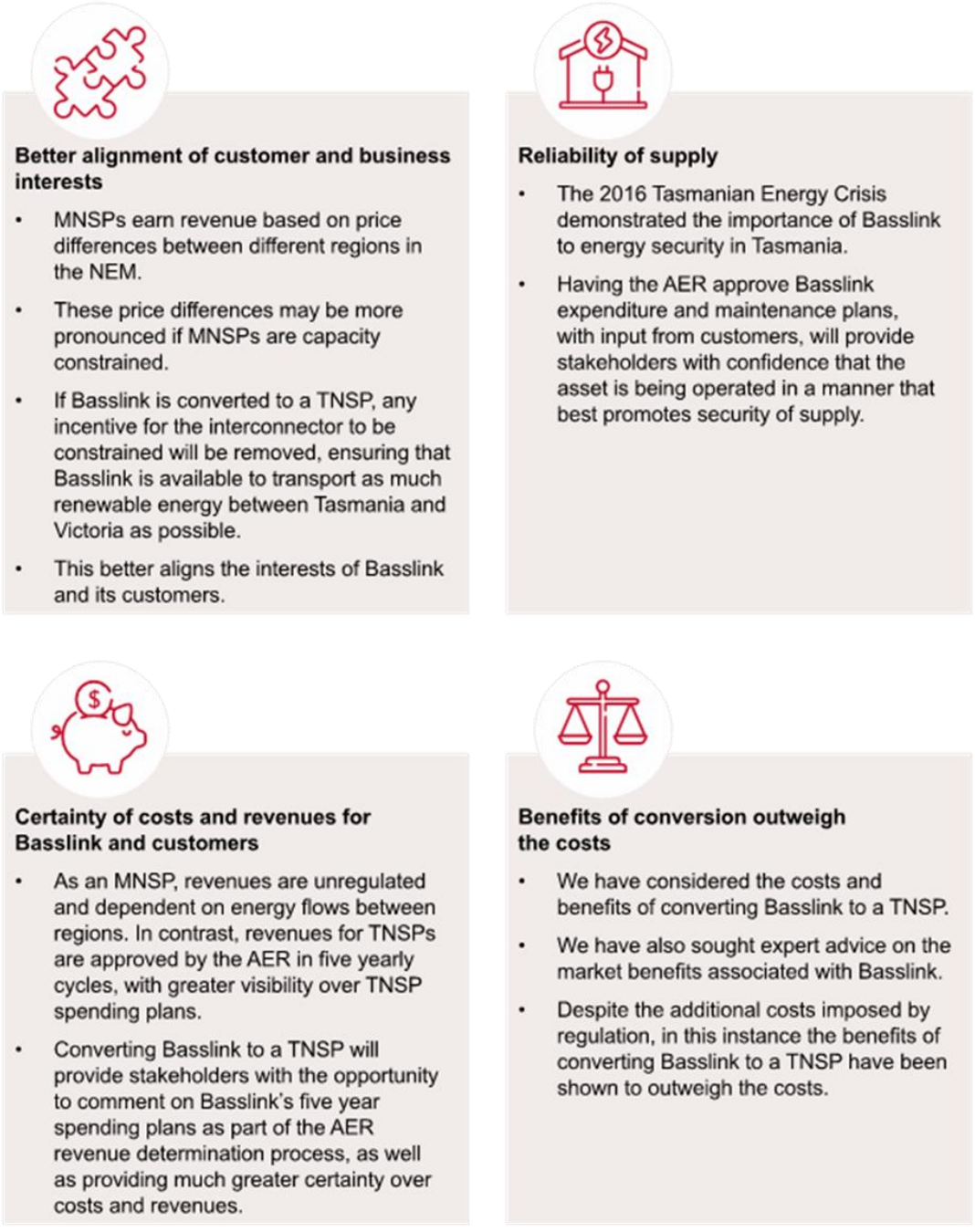
Australia's other two interconnectors, Murraylink and Directlink, have previously been converted to regulated assets in the same way.

There are four key reasons for APA's decision to seek full regulation for Basslink, as set out in Figure 5 below:

Figure 5: Reasons for regulating Basslink



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1.4 Allocation of Basslink costs

During the course of preparing Basslink's 2025-30 Revenue Proposal, we consulted widely about reliability and affordability matters. One of the key consultation topics was how costs would be shared between Tasmanian and Victorian customers.

The consultation process included:

- working closely with Tasmanian and Victorian representatives (representing large energy users, small business and residential consumers) and on our Regulatory Reference Group which guided APA 's approach to public consultation;
- online focus groups with Tasmanian and Victorian residents;
- four-hour workshops in Launceston and Melbourne with 93 participants; and
- an online survey of 1240 energy consumers from across Victoria and Tasmania.

Consistent with the views of stakeholders during the consultation process, our proposal to the AER was for cost allocation based on relative market size. Basslink's costs would be allocated based on the number of electricity connections in each state. Based on our initial proposal, the cost to consumers would remain low at around $8 a year for Tasmanian residential consumers and just under $11 a year for Victorian residential consumers.

The feedback we received was that of the options considered, the approach to cost sharing based on the size of the market was the fairest approach. Given customers in both states receive the benefits of Basslink, sharing the costs in this way was considered transparent and fair.

Further details on what we heard from Tasmanian energy consumers and how their feedback shaped our proposal, together with more details about the benefits of converting Basslink to a regulated asset are available in APA's revenue proposal, published on the AER's website: https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/basslink-determination-2025%E2%80%9330/proposal.

A fact sheet outlining the highlights of our 2025-30 Revenue Proposal to the AER can be found at Attachment A.

1.5 Application of the AEMC's draft determination to Basslink

The AEMC's draft rules, if made, will apply to qualifying interconnectors, which under draft rule 6A.29.4 would include an interconnector that satisfies this criteria:

> *(1) as at 12 September 2024, the network services provided by means of the interconnector were market network services*

As at 12 September 2024, Basslink will be providing market network services, and therefore if made, the draft rule could apply to Basslink, if an interconnector cost allocation agreement is entered into by relevant Ministers. APA would welcome such an agreement being entered into in relation to Basslink.

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However, the draft rule proposes that the rule would commence 12 months after the rule is made, which on current expected time frames is on Thursday 18 September 2025.[1]

APA is seeking to have Basslink become a fully regulated asset from 1 July 2025. The AEMC's draft rule, if made, would commence on 18 September 2025, which is after the proposed commencement of Basslink's 2025-30 revenue period.

While any final rule could apply to the second and subsequent years of the 2025-30 revenue period, the fact that it could not apply to the first year would create uncertainty for customers, Energy Ministers and Basslink.

For this reason, we suggest that the AEMC consider including transitional provisions in the draft rule that would allow an interconnector cost allocation agreement to apply to Basslink from 1 July 2025. Given the AEMC proposes making a final rule on 18 September 2024, which is over nine months prior to the commencement of Basslink's proposed revenue period, we consider that there is time for such transitional provisions to be implemented.

[1] AEMC, *Providing flexibility in the allocation of interconnector costs,* Draft rule determination, 20 June 2024, p16

At a glance
Basslink revenue proposal 2025-30

Basslink Pty Ltd has prepared its 2025-30 revenue proposal for Basslink which also includes an application to the Australian Energy Regulator (AER) to convert Basslink to a regulated transmission asset. If the conversion is approved, Basslink will earn revenues regulated by the AER instead of through market mechanisms. We undertook engagement with consumers and stakeholders to understand their views and ensure their preferences were reflected in our revenue proposal. We have focussed our stakeholder engagement on **five priority issues.**

Priority 1

Affordability

$8

Per year bill impact for Tasmanian residential consumers

$11

Per year bill impact for Victorian residential consumers

$831M

proposed opening regulatory asset base, significantly below alternative estimates. This helps lower the cost of Basslink to consumers over the long term

About Basslink

The Basslink Interconnector (Basslink) is a 370km cable which is mainly undersea and is currently the only electricity transmission link between Tasmania and the rest of Australia. Basslink stretches from George Town in northeast Tasmania across the Bass Strait and then connects to the Victorian transmission network near Traralgon. Basslink essentially operates like a two-way highway for electricity to be sent between Tasmania and Victoria.

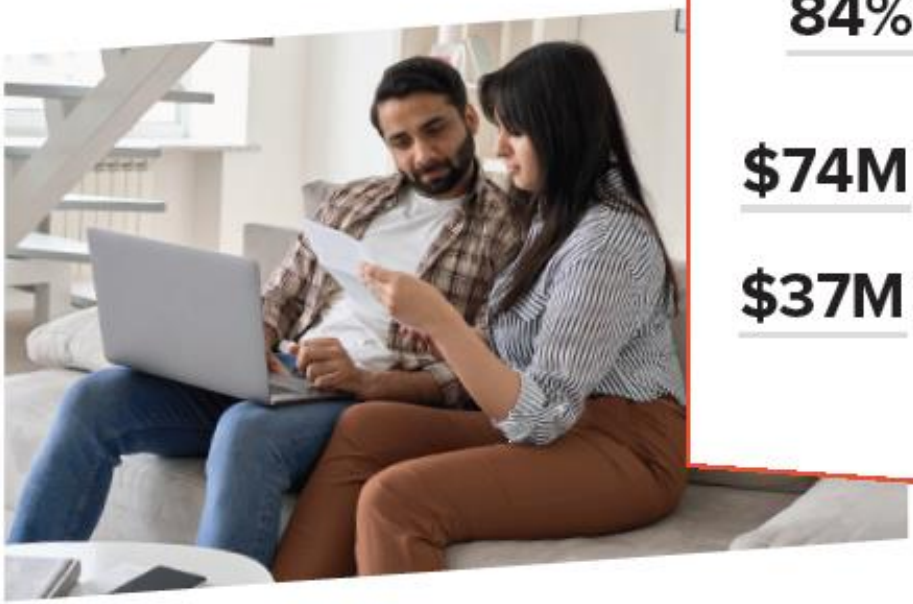
Priority 2

Reliability

84% Of surveyed consumers rated having greater reliability for the future as something they strongly support

$74M Capital expenditure over 2025 to 2030 to ensure high levels of reliability into the future

$37M Average operating expenditure per year to maintain the safety, security and reliability of Basslink



At a glance
Basslink revenue proposal 2025-30

Priority 3

Insurance

Higher
level of premium

Lower
level of risk to consumers

A higher premium, with lower risks to consumers, is proposed to avoid potential bill shocks to consumers in the future if damage occurs

Priority 4

Capital expenditure

~70%

Of consumers support the $44M replacement of the control and protection system in 2025-2030 to avoid the potential negative impacts of increased unreliability

Priority 5

Cost sharing

Consumers expressed a consistent preference for an approach to sharing the costs of Basslink based on the size of the market - mainly due to it being considered the fairest approach. This results in the most comparable bill impacts for Victorian and Tasmanian consumers.

Benefits of the revenue proposal

- Reliability and security of energy supply
- Supports the transition to a renewable energy future
- Certainty of costs and revenues and how they impact consumer bills
- Better alignment of consumer and business interests
- Regulatory conversion benefits outweigh costs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