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Attention: Mr P. Adams

Proposed change to Settlement Residue Auction Clause 3.6.5

NEMMCO has proposed a change to the Code which will have the effect of funding negative inter-regional settlement residues from the proceeds of the Settlement Residue Auctions rather than from auction fees, as at present.

The effect will be to transfer the direct risks associated with negative residues from those who choose to take on these risks by participating in the auctions to the customers who currently receive the SRA proceeds through reduction in transmission charges.

NEMMCO has argued that the net effect is the same. Customers already indirectly bear this risk on behalf of those who participate in the auctions, as reflected in the price paid for the auctioned SRA units. The simplest approach therefore is to place the risk more directly with the customers by funding negative residues from SRA proceeds.

This approach may be theoretically sound, but the experience to date is that SRA proceeds are on average about half the value of the residues. This suggests that recovery of negative residues from SRA proceeds will have a much greater effect on customers than recovery from positive residues or through auction fees.

TNSPs currently receive the SRA proceeds from NEMMCO and return those amounts to customers through specified changes to transmission prices. Each TNSP needs to estimate in advance the SRA proceeds which it will receive each quarter in the coming year and allow for those amounts in setting transmission prices. NEMMCO's proposal will add further uncertainty to those estimates, although if NEMMCO's estimate that annual negative residues total about \$800,000 remains correct, this is unlikely to be material.

The NEMMCO proposal will therefore add some small increased volatility to transmission charges from year to year. TransGrid's view is that this will not create major issues, provided it is generally recognised by transmission customers and regulators that this increased volatility may occur.

Yours sincerely

[Signed 16/3/2005]

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General Manager/Corporate Development