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The Inquiry Secretary
Legislative Council Sessional Committee - Government Administration 'A'
Inquiry into Energy Prices in Tasmania
Legislative Council
Parliament House
HOBART TAS 7000

Via Email: epr@parliament.tas.gov.au

Dear Sir or Madam,

RE: Inquiry into Energy Prices in Tasmania

Thank you for extending an invitation to the Tasmanian Minerals, Manufacturing and Energy Council (TMEC) to contribute to the inquiry into energy prices in Tasmania which we welcome.

TMEC's membership base represents an important wealth creating sector within the Tasmanian economy. The combined minerals and manufacturing sector employs 21,000 people and contributed $2.795B in exports as of the 12 months to June 2023. Most of our members are based in regional areas of Tasmania and therefore provide critical employment opportunities away from public funded employers. Minerals exports alone account for 62.9% of Tasmania's commercial exports and is the foundation stone of many regional communities with 5,200 direct jobs.

Background

The current method of determining the wholesale price of electricity in Tasmania is often presented as a "market or NEM based model" and therefore should not be interfered with. The reality is Tasmania's electricity prices are set by a formula which the Tasmania Government are responsible for. Yes, it uses references from the NEM, but only because the State Government has scripted the formula to do that.

Hydro Tasmania determines a myriad of inputs from both its internal measures as well as externally sourced measures and populates the formula each year. The Economic Regulator checks what Hydro Tasmania has submitted and out comes a result, which virtually every customer in Tasmania then pays for. The Government claims setting prices is at "arm's length" which is correct, what is not said it that is calculated to the formula the Parliament set in 2013.

It is important to know where the formula came from and why. The formula was created following a Parliamentary enquiry into the electricity supply monopoly which recognised in 2012 that the size of the Tasmanian electricity market was unlikely to ever attract a competitor for Hydro Tasmania. Therefore, the intent was to create a price determination method which linked Tasmania to what was probably, in 2012, the best of the competitive market features. At that time, Victoria had multiple generator businesses and linking the Tasmanian formulae to some of Victoria's variables gave some comfort Tasmania may be serviced by a monopoly provider (Hydro Tasmania), but the price it charged was as if they were a participant in a virtual competitive market.

Wind the calendar forward ten years and the evolution of the NEM means than many of the worst features of a disrupted market is now being factored into the formula. Tasmanian consumers pay for the broken market which exists in the eastern seaboard states. Tasmania pays for the privatisation of electricity generators and transmission companies of the eastern states – even though Tasmania owns the assets in Tasmania. Tasmania pays for thwarted attempts to decarbonise the NEM and yet Tasmania's electricity system is already decarbonised. Tasmania has the best class of assets in a decarbonised world but pays for the worst of a fossil fuelled market.

Claims of delinking the prices, price caps and energy dividends are effectively attempts to undo elements of how the formula works. Rather than apply band aids perhaps it is time to reset the formula, so it reflects Tasmania today and the Tasmania we are striving to be. Perhaps Tasmania needs a Parliament with the same appetite to look after electricity consumers as was the case in 2012-13.

TMEC has always advocated for the generation and transmission assets to remain in public ownership and for those entities to be able to earn a margin which flows back to the state as a dividend – which benefits all Tasmanians. The point of difference in TMEC's approach is for the State to do a better job of driving efficient GBE's.

TMECs input as per the terms of reference are:

1. ***Factors that impact energy prices for Tasmanian household and small and medium business customers, with particular reference to energy generation, distribution and retail costs;***

   Concern remains that Hydro Tasmania continue to reference the Victorian Market price in the National Electricity Market as the benchmark price for market pricing. It is unfair to all Tasmanian consumers of electricity when the electricity that is generated in Tasmania is not valued simply at the cost of generation plus the margin required to operate the business and provide the Tasmanian Government with an acceptable dividend.

   With reference to transmission and distribution the rules as set by the Australian Energy Regulator no longer work to incentivise TasNetworks low-cost investment and acceptable rates of return that are below the AER benchmarking. A clear example, the rules do not provide incentives if TasNetworks improves efficiencies through reduction of operating or capital costs then that saving is directly passed onto customers.

   The way retail pricing set by the Tasmanian Economic Regulator is questionable with the current energy mix in Tasmania. The model uses Victorian forward pricing as the reference and variable inputs from Hydro Tasmania to then set the wholesale contract price that can be charged. This mechanism has been in place since January 2014 and is outdated. The Tasmanian energy mix today has additional wind farms, and these are not part of the formula although onerous contracts have been entered into for this generation to be provided to Hydro Tasmania and Aurora Energy, again both Government owned businesses.

2. ***Opportunities and challenges for the State of Tasmania as owners of power generation and transmission infrastructure; and in relation to opportunities:***

   In addition to the charge of energy methodology outlined above, transparency on the cost of borrowing versus what is recovered from consumers should be explored. An example remains that TasNetworks borrows money at a lower cost of borrowing through Government agencies, yet the AER rules allow that recovery of that debt to be referenced to national interest rates.

With regards to TasNetworks 5-year regulatory review and dividend returned to the Government, the Government agencies like RecFIT could play more an active role in challenging the proposals in likes of cost of capital, contingent projects, operational costs and returns to Government in the form of dividends.

With respect to Hydro Tasmania, is being a firmer of energy in the best interests of Tasmania or is it in the best interests of Hydro Tasmania? What barriers are being created (unintentionally) which may be resulting in a reluctance to build new renewable projects? These projects are progressing across the nation, but not in Tasmania.

Has Parliament seen the modelling which shows the current approach being taken for new investments in renewables is the best option for Tasmania? Should the Government consider building new renewables (wind/solar) at least initially to break the nexus between new load needing supply, and new generators needing load.

3. Any other matters incidental thereto.

A common concern amongst the TMEC membership base (which includes a combination of retail, wholesale and direct connected customers) is the impact on transmission pricing going forward in relation to the following listed below:

a. **Basslink** – The change in ownership and importantly the change in how Basslink recovers its cost from consumers needs scrutiny to ensure Tasmanian consumers do not pay twice for the use of this asset. Under the planned regulation of Basslink, the owner will charge a transmission fee which will appear on all consumers bills. Up until Basslink becomes a regulated asset, Hydro Tasmania have paid a “facility fee” to use Basslink as a merchant link, which has been quoted publicly in the order of $70M per annum. It is vital LegCo confirms Hydro Tasmania will cease recovering the $70M fee from consumers. The nett effect of Basslink becoming a regulated asset for consumers should be ZERO DOLLARS. This will be evidenced by Hydro Tasmania showing a reduction in expenditure but a corresponding reduction in revenue.
b. **Marinus** – Marinus project will impose additional transmission charges to all consumers and to what order of magnitude is still unclear. None the less, another cost increase to consumers putting pressure on pricing.
c. **North West Transmission Development** – Project is to enable higher energy flows for Marinus Link and to enable new renewable generators to connect to the network. This project however, by the rules, will be funded by the existing transmission customers. Generators do not pay transmission fees yet are the main beneficiaries of this development.
d. **Contingent Projects – TasNetworks** – In Bell Bay there is a significant amount of capital allowed for transmission projects to support the development of hydrogen. This again, if triggered, will put increase on transmission costs to all consumers.

Summary and Future Risks

The importance of getting clarity and answers to how electricity pricing is determined in Tasmania is important and this review is a vital step in the process.

TMEC is acutely aware of the impending disruption which is almost inevitable as the capacity of the state's electricity system is increased by a further 100 percent, in line with the Government's aspiration.

TMEC understands the technical merit of why a boosted Tasmanian electricity system will bring technical benefit to both this state and the National Energy Market (NEM) with enhanced interconnection from Marinus Link.

While growth in new renewable electricity generation in Tasmania without Marinus Link is possible, having the cable provides more options and potentially a faster increase in capacity. Bringing more capacity online with interconnection will be a trigger for closure of coal fired power stations in the eastern states. A point not often considered by Tasmanian residents when they actively lobby and protest new wind farms and transmission lines being proposed in their locality.

The unresolved matter is the financial implications which is a consequence of solving the technical issue of a reliable dispatchable supply of electricity.

The installation costs for renewable electricity assets are increasing in Australia and globally. The recent announcement regarding Marinus Link being rescoped to a single cable is an example of the scale of cost implications. The cost estimate of a one cable project in 2023 is the same as a two-cable project was in 2020. CSIRO's collaboration with the AEMO to produce "GenCost 2022-23 Report" indicate wind and solar remains the lowest cost new build electricity generations sources, but wind farms investment costs have increased by 35 percent.

The claimed benefit of lower wholesale prices offsetting increased transmission costs is unlikely to be realised. This begs the question if consumers do not require additional capacity should they pay for it?

The infrastructure equivalent comes from roads in major cities. Addressing congestion is being done by installing new road networks and funding the investment by charging a toll for those who choose to use the toll road. Drivers who do not use the toll pay no additional cost.

Should this model be adopted for electricity in Tasmania? Existing electricity consumers whose needs are fully met by the existing capacity continue to pay what they pay for. New consumers, or existing consumers and users of the system with increased needs pay the "toll" for this investment. For example, a new generator funds their investment and the cost to transmit the electricity, a new consumer pays for the electricity and infrastructure they need to get the electricity to their site, Hydro Tasmania pays for the augmentation of infrastructure to enable the additional generation and they recoup this cost from the beneficiaries of the new capacity.

At present, the approved cost recovery models used by electricity utilities reward expenditure (the more you spend the more you earn) and allows the costs to be recouped from every consumer connected – even those who are not needing new capacity. This would be akin to asking all road users in the cities to pay for the toll roads, even if they do not use them.

Tasmania is home to arguably some of the best renewable electricity assets in the world. Yet the state choses to be saddled with systems which reflect some of the least attractive assets in the world. Tasmania needs to be bold and step away from convention and design and implement a model which creates greater wealth for this state while exporting renewable energy, in any form to enable other countries, states and companies to cease the use of fossil fuels.

TMEC appreciates the opportunity to contribute to the inquiry into energy prices in Tasmania. Please do not hesitate to contact me should you require further clarification of any of the points raised in this submission.

Yours sincerely,

Ray Mostogl
Chief Executive Officer