Tasmanian Council of Social Service Inc.

TasCOSS submission to the Feasibility study for a second Tasmanian interconnector

October 2016

TasCOSS

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Introduction

The Tasmanian Council of Social Service (TasCOSS) welcomes the opportunity to respond to the *Feasibility of a second Tasmanian interconnector Preliminary Report*, and to put in writing our comments made verbally in a meeting with John Tamblyn and the study team (13/10/2016).

It is the view of TasCOSS that the proposal for a second interconnector across Bass Strait exists in an environment of substantial economic and policy uncertainty, and that the interests of the Tasmanian community – especially disadvantaged Tasmanians – have not been adequately considered in the *Preliminary Report*. TasCOSS believes that a much closer examination of the effects of the proposed interconnector on electricity prices is needed, as is careful and robust scrutiny into the risks involved were the Tasmanian Government, Hydro Tasmania and TasNetworks to contribute to funding the construction of a second interconnector, or to enter into a guaranteed commercial arrangement akin to that established with the owners of the existing Basslink cable.

Impact on electricity prices

Electricity bills have long been a major challenge for Tasmanian households living on low incomes, and this is true especially of the last decade, during which prices have increased significantly. The *Preliminary Report* makes numerous references to the network augmentation that would be necessary were a second interconnector to be built, and the effect this would have on network prices as determined by the Australian Energy Regulator (AER). The *Report* notes that regulated network costs as set by the AER comprise around 59 per cent of Tasmanian household electricity bills. In its draft determination released in September of this year, the AER set the nominal regulated asset base of TasNetworks for 2017 at a not-insignificant $1.63 billion.[1] The additional network infrastructure required to support a second interconnector, and to connect the substantial new renewable generation assets which are required to sustain these proposals, are likely to increase this asset base by tens of millions of dollars, if not more. These costs will be passed on to Tasmanian consumers, as TasNetworks will be permitted to recover its costs, as a well as a return on its capital base at a fixed rate as determined under present regulatory arrangements.

The *Preliminary Report* notes further that if a second interconnector is constructed as a regulated asset, the "proportion of costs recovered from consumers of each state or territory will be linked to the proportion of time that the flows are towards that region."[2] While the foremost intention appears to be for this proposed interconnector to export hydroelectricity and ancillary services from Tasmania, much the same could be said about Basslink as it was originally conceived. Despite this, Basslink did not see its balance of transfer tip in favour of exports until 2010-11, in the fifth year of its operation.[3] This experience must suggest that it is

[1] Australian Energy Regulator, 'Draft Decision: TasNetworks distribution determination 2017-18 to 2018-2019, Attachment 2– Regulatory asset base,' 2016. p. 6.
[2] *Preliminary Report*, p.33
[3] Electricity Supply Industry Expert Panel, 'Basslink: Decision making, expectations, and outcomes,' 2011. p. 36

possible that Tasmanian consumers will end up paying the bulk of such regulated charges were the connector to be built, especially in the absence of increased generation capacity in Tasmania, and notwithstanding the energy security benefits to the State.

Risk to the Tasmanian Government Budget

TasCOSS is also concerned about the risk to the Tasmanian Government Budget – both in direct costs and/or through poor returns to the Government as the owner of Hydro Tasmania.

In 2011 the Government's Electricity Supply Industry Expert Panel undertook an evaluation of the final business case for Basslink, measuring it against the cable's actual financial performance. The evaluation expressed, in the mildest of terms, that "Basslink's final performance is yet to fulfil the expectations contained in the final business case," and noted that the five-year average of annual benefits from the link accrued to Hydro Tasmania was less than half of the revenue benefits projected in the final business case, and undershot the annual costs of Hydro Tasmania's usage of the cable by more than 20 per cent.[4] These costs do not just include facility fees paid under the Basslink Services Agreement, but also a parallel financial arrangement undertaken by Hydro Tasmania to protect against rising interest rates, which has resulted in "hedge costs […] equivalent to around 43 per cent of the facility fee" in "one year over the period 2005-6 to 2010-11."[5] As an example to illustrate the risks involved with this proposal, the architects of Basslink wagered hundreds of millions of dollars of Tasmanian public money that interest rates would rise, and they lost.

While the *Preliminary Report* notes capital investment required for a second interconnector is estimated to be in the region of $800 million, we must again refer to history, as Basslink's construction costs jumped from initial estimates of $500 million to some $874 million by the time of the project's commencement.[6] The result of these misjudgements has been the commensurate reduction in the returns Hydro Tasmania can make to its owners: the State of Tasmania, and its people.

TasCOSS believes that these risks should not again be taken by the Tasmanian Government without very serious consideration, and without near certainty that positive net returns on public money can be realised from constructing a second interconnector.

A substantial part of the rationale for the second interconnector is the clear benefits of hydroelectricity when combined with intermittent renewables, especially given hydro's rapid ramping capacity and storage functions. While this is used to support Tasmania's further integration into the NEM, it seems evident that increased intermittent renewable capacity could be developed in Tasmania without an $800 million allocation to interconnection – and perhaps especially if that proposed funding were used elsewhere. Intermittent renewables

[4] Electricity Supply Industry Expert Panel, 'Basslink: Decision making, expectations, and outcomes,' 2011. p. 46
[5] Ibid. p. 45
[6] Electricity Supply Industry Expert Panel, 'Basslink: Decision making, expectations, and outcomes,' 2011. p. 6

such as wind, solar and wave energy can each be integrated into Tasmania's energy infrastructure with fewer drawbacks, given our hydro assets and concomitant storage potential. Energy storage and security could all be furthered by the development of our dams as the State's great batteries. It is not made clear in the *Preliminary Report* why these benefits cannot be realised without a second interconnector.

Above all else, the most compelling reason that TasCOSS advises caution with respect to this proposed investment is that we believe there are far more urgent infrastructure and other expenditure needs in Tasmania. The State's water and sewerage infrastructure is in a parlous state, while the needs of our schools and entrenched disadvantage in many communities all exist in more concrete and definite terms than do the speculative benefits of the proposed interconnector. TasCOSS does not support the gambling of public finances on this project in present circumstances; its commercial risks are substantial – especially in an environment of policy uncertainty, and almost inevitable change – and the *Preliminary Report* does not explore how Tasmania's energy security could be enhanced through more affordable means. As with the Basslink experience, were this project to fail to fulfil the terms of its business case, it is likely that the people of Tasmania will pay for it, through both their power bills and reduced dividends returned to the Tasmanian Government.

The poor use of Government funds represents the gravest risk for the most vulnerable communities in Tasmania, who are least able to bear the consequences of speculative investments of public money gone awry, and suffer the most from pressing infrastructure deficits elsewhere. Eight-hundred million dollars would go a long way towards making their lives more liveable, prosperous, and fulfilling.

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