the australian **PIPELINE** industry association Ltd

30 November 2006

Dr John Tamblyn
Chairman
Australian Energy Market Commission
PO Box H166
Australia Square NSW 1215

Dear Dr ~~Tamblyn~~ John

The Australian Pipeline Industry Association (APIA), as the industry representative body for the gas transmission pipeline industry in Australia, welcomes the opportunity to make a submission on the AEMC's Draft Rule Determination for the *Draft National Electricity Amendment (Pricing of Prescribed Transmission Services) Rule 2006.*

APIA would like to comment on the AEMC's proposed approach to the pricing of generators' connection to the transmission network. In particular, APIA is disappointed that the AEMC has determined to continue the existing approach whereby generators connecting to the transmission network are charged on the basis of 'shallow' connection charges. We believe that this approach fails to meet the basic economic principle of pricing according to cost reflectivity that is necessary to ensure efficient pricing signals are sent to market participants.

Where there is no obligation for generators to pay for the full costs imposed on the network by their connection, they will not take these costs into account when choosing where to build. APIA considers that a generator should be required to pay for any costs that can reasonably be attributed to that connection. Where connection prices are not a true reflection of connection costs, generators will face muted pricing signals, which can lead to an inefficient pattern of investment, both in terms of the location of generators and mix of energy sources.

This is of concern to the gas transmission industry as it potentially distorts investment decisions in a way that undermines a key competitive advantage enjoyed by gas-fired generators. Specifically, charging generators only for shallow connection reduces the competitive advantage that gas-fired generators have over coal-fired generators due to the lower transportation costs of shipping gas compared with shipping coal. This competitive advantage is reflected in greater locational flexibility, and it should not be undermined through a failure to price electricity transmission networks on a cost reflective basis.

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For example, coal haulage and electricity transmission costs may be significantly greater than gas transmission costs on a GJ/km basis. Accordingly, not requiring generators to pay deep connection costs means they are more likely to locate nearer to the fuel source rather than taking account of the full delivered electricity cost, including generation and transmission to demand centres.

The AEMC noted in its Draft Determination that it does not believe the introduction of deep connection charges, or requiring generators to contribute towards the recovery of shared network costs, would materially improve the efficiency of generator investment decisions regarding location. This assessment is made on the basis that regulatory and market arrangements already provide significant signals to generators and also that there is no evidence that generators can cause a TNSP to undertake downstream augmentation.

The AEMC's concerns that deep connection charges will deter new generation investment are misplaced. To the extent that generators pay a cost reflective connection price, this should not be regarded as a barrier to entry, as it reflects the true costs of connection. APIA believes that such costs should be taken into account in investment decisions as this is more likely to result in an economically efficient outcome. It may well be appropriate to consider that, where generators do pay deep connection charges, they should have firm access rights.

This issue is part of a broader issue of efficient investment. There are some concerns about the effectiveness of the regulatory test – an issue which is presently being addressed by ERIG. APIA believes these issues, including the issue of firm access rights, warrant co-ordinated consideration and response.

It is important that market participants receive appropriate investment signals which reflect the true costs of making those investments. Smearing of deep connection costs will distort investment decisions and is likely to undermine economic efficiency. APIA believes that cost reflectivity in pricing is implied by the NEM objective of economic efficiency and, as such, the AEMC should fully justify departing from this principle.

Yours sincerely

CHERYL CARTWRIGHT
Chief Executive