Delta electricity

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14 May 2004

Mr James Cox
Acting Chairman
Independent Pricing and Regulatory Tribunal of NSW
PO Box Q290
QVB Post Office NSW 1230

Dear Mr Cox,

NSW ELECTRICITY REGULATED RETAIL TARIFFS 2004/05 TO 2006/07
SUBMISSION ON DRAFT REPORT AND DRAFT DETERMINATION, DATED APRIL 2004

Further to the Tribunal's invitation for submissions on this draft report and draft determination, and further to Delta Electricity's submission to IPART on Discussion paper DP70, I wish to offer comments in relation to:

- The representation in the draft report of Delta's submission to IPART on Discussion paper DP70, and in particular
- Delta's views in relation to the level of LRMC of purchased energy adopted by the Tribunal.

LRMC

Delta Electricity agrees that similarities in methodology mean that with similar assumptions, there would be close agreement of Delta's results with those from IES. Three important points of distinction however are the treatment of reserve plant, the load duration curve sampling methodology and the basis of reporting the range of modelling outcomes.

Reserve Plant

Following IPART's roundtable discussions on 4 March 2004, Delta had constructive discussions with IES on assumptions as to the future level of reserve plant. Delta concurred that a 10% reserve plant margin, while appropriate at present, would be excessive when the electricity supply system had doubled in approximately 25 years time. Delta's concurs with IES that in order to preserve a similar level of system reliability the quantum of reserve plant needs to grow at a compound rate of about 1.3%pa (on top of plant required to meet the expected energy).

IES have made an allowance for the cost of incremental reserve of approximately \$0.98/MWh. Delta believes this is on the low side and a mid range estimate is in the order of \$1.74/MWh.

Load Duration Curve sampling

It is understood that IES have used Calendar 2001 ETEF data and used the maximum demand in each sample period (refer exhibit 4-5 of the IES report). Calendar 2001 ETEF had a maximum demand of 5,974MW and a load factor of 49.4%. Calendar 2002 ETEF data had a maximum demand of 6,493MW and a load factor of 42.1%. These are materially different.

Using Calendar 2002 data instead results in a higher estimate of the median LRMC by approximately \$3.31/MWh over using the Calendar 2001 data. Selecting the appropriate dataset should not be arbitrary; it is not the case that either year's data sets are equally valid. Managing this volume volatility is part and parcel of the regulated tariffs and should be appropriately incorporated in the LRMC evaluation. To ignore this fact leaves the process open to questions of selective use of the available data.

Range of LRMC estimates

In Delta's submission to the Tribunal dated 2 February 2004, Delta had estimated the range of possible LRMC outcomes in terms of the 90% confidence levels as between "$49.80 to $55.20/MWh with a median figure of $52.20/MWh".

Based on the amended reserve assumptions above Delta would now revise down its estimate of LRMC which, with 90% confidence, should lie in the range $48.18 to $53.95 with a median figure of $51.03 /MWh.

The distinction Delta wishes to make is that reporting a low possible LRMC may be misleading as it attaches no probability to the likelihood of that cost actually being realised. In Delta's view the $47.00/MWh LRMC adopted by the Tribunal, while possible, has a probability of being realised of less than 5%.

Delta is disappointed that the Tribunal is proposing to apply a figure for the LRMC that is outside a credible range of estimates. The competitive outcomes of applying an inappropriately low LRMC are discussed in Delta's previous submission.

Plant mix

The generation technology capacity as reported in the Tribunal's draft report was included in Delta's submission to indicate the scale of new capacity increments on which the costs in Delta's modelling were based. A typical plant mix corresponding to Delta's median-cost estimate was 2,079 / 2,117 / 304 / 2,641 MW of OCGT-Fuel Oil / OCGT-NG / CCGT / Coal plant respectively to supply 6493MW (ETEF 2002 Max Demand) with a reserve plant margin declining over time from an initial 10%.

Conclusion

Delta submits that the Tribunal's proposed $47.00 regulated wholesale electricity purchase cost should increase as it is outside a reasonable range of estimates. It is noted that with a $3.31/MWh upwards adjustment (using the Calendar 2002 load dataset) and an additional $0.76/MWh adjustment for the cost of incremental reserve plant, the IES medium LRMC estimate of $47.84 would become $51.91MWh which is well within Delta's 90% confidence bounds for the LRMC.

Delta would be pleased to provide any clarification of the above or any further assistance required. In particular, we continue to be willing to share with you our range of assumptions and further details of our modelling of efficient new entrant costs and LRMC. If you would like to discuss these matters further please contact Phil Colebourn (02 9285 2751) or Frank Hutchinson (02 9285 2756).

Yours sincerely,

T.P. Baker

Tim Baker
General Manager Marketing

cc. Fiona Towers