



INTERIM SUBMISSION

ECONOMIC REGULATION AUTHORITY

**PROPOSED REVISIONS TO THE
ACCESS ARRANGEMENT FOR THE
WESTERN POWER NETWORK**

DECEMBER 2011

*Western Australian Local Government Association
15 Altona Street WEST PERTH WA 6005
PO Box 1544 WEST PERTH WA 6872
Tel: +61-8-9321 5055
Fax: +61-8-9322 2611
info@walga.asn.au*

EXECUTIVE SUMMARY

Local governments in Western Australia have a strong interest in the outcomes and consequences of the Access Arrangement for the Western Power network. In this submission, the access arrangements proposed by Western Power have been considered by Local Governments from their perspective as:

1. a significant consumer of electricity, used to operate a wide range of municipal facilities including recreation centres and sports grounds, civic centres, administration offices, works depots, libraries and swimming pools;
2. a purchaser of street lighting services; and
3. a land developer or a proponent of land development in their jurisdiction.

Electricity Consumer

Issue	Submission
<p>4.1 Recovery of Deferred Revenue from AA2</p> <p><i>Submissions are invited from interested parties on the appropriate time period over which deferred revenue from AA2 should be recovered from network users.</i></p>	<p>Support the proposal that deferred revenue from AA2 be recovered over the life of the assets on the basis of the evidence provided by the ERA. Calculations show that Western Power's proposal would result in significantly higher annual price increases (recovery of \$242m v \$80m).</p>
<p>4.2.1 Benchmark Credit Rating</p> <p><i>Submissions are invited from interested parties on the most appropriate benchmark credit rating for electricity transmission and distribution service providers in Western Australia.</i></p>	<p>The appropriate benchmark credit rating should reflect the reality of the government ownership of Western Power and the risks faced by investors.</p>
<p>4.2.2 Credit Rating for Government-Owned Public Utilities in Western Australia</p> <p><i>Submissions are invited from interested parties on the most appropriate benchmark credit rating for electricity transmission and distribution service providers in Western Australia.</i></p>	<p>WALGA concurs with the view that the cost of debt be benchmarked on rates applicable to the WA Treasury Corporation.</p>
<p>4.2.5 Equity Raising Costs</p> <p><i>Submissions are invited from interested parties on whether equity raising costs should be included in Western Power's revenue requirement and if so what is the appropriate methodology for calculating these costs.</i></p>	<p>Unless it is proposed that Western Power be privatised, equity raising costs should reflect the reality of the way in which Western Power is funded.</p>

Issue	Submission
<p>4.3.1 Service Standards Adjustment Mechanism</p> <p><i>Submissions are invited from interested parties on proposed revisions to the access arrangement to allow adjustments to target revenue in the next access arrangement period for the service standard adjustment mechanism proposed by Western Power.</i></p>	<p>WALGA is of the view that service targets have been considerably eased and that incentive payments to Western Power increased. It is noted that street light repair times and customer service levels remain unchanged, although the measurement of these standards continues to be questioned by Local Governments.</p> <p>WALGA supports the continuation of service performance comparisons over time as these indicate whether the outcomes delivered are improving or deteriorating.</p>
<p>4.4 Calculation of Revenue Requirement Issues</p> <p><i>Submissions are invited from interested parties on Western Power's proposed mid-year timing assumption for new facilities investment (capital expenditure).</i></p>	<p>WALGA is of the view that there is no justification for this change which can only result in higher prices to users.</p>
<p>4.4.2 Tax on Capital Contributions</p> <p><i>Submissions are invited from interested parties on whether an amount for tax on capital contributions should be allowed to be recovered from all network users.</i></p>	<p>WALGA is of the view that it may be appropriate for Western Power to recover the present value of the difference between the tax payable and the depreciation credits obtained. The contemplated approach of a revenue levy across the board redistributes the cost away from the user who generates the tax liability and is therefore a hidden cross subsidy. This should be avoided.</p>
<p>4.4.3 Working Capital</p> <p><i>Submissions are invited from interested parties on the need to include an allowance for a return on working capital</i></p>	<p>WALGA is of the view that it is assumed that Western Power is being efficiently managed and therefore an allowance for a return on working capital would be an unacceptable tenet and so the current ERA position should not change.</p>
<p>4.5 Applications and Queuing Policy</p> <p><i>Submissions are invited from interested parties on</i></p> <ul style="list-style-type: none"> <i>• the operation of the applications and queuing policy in the current access arrangement;</i> <i>• the revisions proposed by Western Power; and</i> <i>• whether any further revisions to this policy are required to meet the requirements of the Access Code.</i> 	<p>WALGA is of the view that Western Power needs to be more responsive to customer needs and that changes that reduce red tape and simplify customer relations and shorten response times are what is required. Changes that do this are supported.</p>

Issues	Submission
<p>5.1.2.2 Operating Expenditure</p> <p><i>Submissions are invited from interested parties on the level of actual operating expenditure for AA2, and whether or not the actual costs are consistent with a service provider efficiently minimising costs.</i></p> <p><i>Submissions are also invited from interested parties on the forecast operating expenditure for AA3, the methods used by Western Power to derive its forecasts, whether the forecasts should include an amount for efficiency gains in base operating expenditure, and the adequacy of Western Power's supporting information for this forecast</i></p>	<p>The assumption made by Western Power that 2010/11 was an efficient base year should be challenged by the ERA. Furthermore it is noted that these costs have been maintained in real terms and no efficiency gains on base operating costs are included, despite significant capital investment.</p> <p>Western Power should have efficiency improvements targets given the progress being made in technology and management and contracting practices.</p>

The key issues from a Local Government perspective with respect to the provision of street lighting services are not fully addressed in the Western Power Access Arrangement submission. Although this represents only a small proportion of Western Power revenue, from a customer perspective there is need for clarity, certainty and efficiency in the way these services are provided. In particular there is a need to ensure optimal investment in renewal of street lighting infrastructure from a public perspective, rather than the perspective of the electricity distributor. WALGA encourages the ERA review to examine the efficiency with which street lighting services are delivered.

Practical implementation of the contributions policy continues to be perceived as a significant barrier to commercial and urban development in many areas, particularly in regional centres. Local Governments are concerned about the capacity of Western Power to provide additional infrastructure in a timely manner to support growth.

The proposed Access Arrangements do not appear to support undergrounding of electricity distribution infrastructure as part of the renewal of pole networks when they reach the end of their service life. This is in contrast to the Western Power policy that requires a developer or Local Government to underground the infrastructure (at their expense) if a development requires that infrastructure to be relocated. From a public benefit perspective, the most timely and efficient way to move to an underground distribution system is when the poles and associated infrastructure requires replacement and this should be included in the plans underpinning the proposed Access Arrangement.

ABOUT WALGA

The West Australian Local Government Association (WALGA) is the united voice of Local Government in Western Australia. The Association is an independent, membership-based group representing and supporting the work and interests of 139 Local Governments in Western Australia plus the Christmas Island and Cocos (Keeling) Island Councils.

The Association provides an essential voice for almost 1,400 elected members and over 12,000 employees of the Local Governments in Western Australia. The Association also provides professional advice and offers services that deliver financial benefits to the Local Governments and the communities they serve.

This Interim Submission on behalf of the Local Government sector has been prepared with limited consultation due to the tight time frames provided by the Economic Regulation Authority since the release of the Issues Paper on 7 November 2011.

The Association wishes to acknowledge the consultative approach adopted by Western Power in developing their proposed revisions to the Access Arrangements.

WESTERN POWER COSTS AND REVENUES

The Local Government sector is a substantial electricity consumer and electricity represents a small, but significant and rapidly growing operating cost. The proposed price path (CPI +16.4% in year 1 followed by CPI +11.1% to 11.5% in each of the following four years) would, if reflected in electricity tariffs, represent a further cost pressure incurred by Local Governments that would need to be recovered from ratepayers. For example, for a large, growing metropolitan Local Government, the proposed tariff path will result in more than 30% of every new rate dollar over the next five years being used to fund increased electricity costs. This would more than double the share of operating expenditure being paid to Synergy / Western Power over this period.

The Economic Regulation Authority's Issues Paper identifies and seeks comment on a number of specific issues that will impact across all tariffs. These are considered below.

Recovery of Deferred Revenue from AA2

The concerns regarding price shocks identified by the ERA during the development of AA2 remain at least as relevant today as then, despite significant increases in the prices faced by electricity consumers in the intervening period. For this reason, WALGA is of the view that a recovery of deferred revenue from AA2 should be over a period equal to the average life of the network assets. A more rapid recovery of this deferred revenue will result in significantly higher annual price increases faced by electricity consumers (\$242m versus \$80m).

Credit Rating and Equity Raising Costs

Western Power is currently a wholly government owned corporation and we are unaware of any proposals to fully privatise Western Power within the term of this Access Arrangement. This ownership structure brings advantages and disadvantages from an electricity consumer's perspective. It is the Association's view that the appropriate benchmark credit rating credit rating should reflect the reality of the ownership of Western Power and the way in which it sources funding.

Service Standards Adjustment Mechanism

It is noted that the proposed service targets have been considerably eased and incentive payments to Western Power for exceeding targets. While the broad intention of incentive payments has been outlined, it is not made clear how the proposed system incentivises Western Power to perform in a particular way. There need to be a clear and transparent link between the desired behaviours and any incentive system.

It appears that it is proposed that service performance comparisons over time be abandoned in the future. This change is not supported, as these comparisons indicate whether the performance is improving or deteriorating over time.

Asset Replacement

It is noted that more than 200,000 of Western Power's 630,000 wooden poles are over 40 years old. It is projected by Western Power that a sustained high level of investment is required over the coming 20 years, before a more stable situation is reached where the rate of reinvestment equals the rate at which poles require reinforcement or replacement. From a Local Government perspective this is a very long period of time during which communities remain exposed to significant risks, including from bushfires caused by failures in the transmission and distribution networks. The proposed replacement cost, over \$20,000 per pole on average also appears high, given the scale and on-going nature of the required works program. This review should pay particular attention to ensuring that the optimal investment timing and technical approaches are used to address this significant risk issue.

Base Costs

It appears that Western Power has assumed that 2010/11 was an efficient base year and has maintained these costs in real terms, without assuming any efficiency gains on base operating costs through capital investment and other mechanisms. It is recommended that Western Power include efficiency improvements, reflecting progress in technology, management and contracting practices.

STREET LIGHTING SERVICES

Transparency

Street lighting services and their cost are of major concern to local authorities. It is recommended that the ERA give specific and detailed consideration to street lighting services and costs. The lack of transparency in the components (operation, maintenance and renewal) of street lighting tariffs makes it difficult to assess the efficiency of Western Power's proposed investment and service delivery in this area. There is currently no competitive market for street lighting service provision. Over many years street lighting assets, purchased by Local Governments, have been vested in Western Power. In the pricing arrangement it needs to be clear that Western Power pricing does not include earning a return on street light assets gifted to Western Power.

The existing street lighting service model results in Local Governments being almost powerless to influence the level of service or the cost of existing networks. Householders and businesses are able to respond to changes in electricity tariffs by changing their consumption and / or patterns of use. In contrast, once installed, street lights are unable to be controlled by the local authority (photo sensitive cells control switching).

Public Good

Given the public good nature of street lighting, it is questioned whether the approach of seeking full cost recovery to a government owned corporation is appropriate. The share of cost recovery applied to other services such public transport, where the costs are shared between the users and the public are arguably a more equitable model for street lighting service delivery.

Asset Renewal

As part of the current arrangements between Western Power and Local Governments, Western Power maintains street lights vested in it and replaces them when no longer serviceable. The pricing model, which is not transparent, includes a component for renewal of street lighting assets when they reach the end of their service life. However, there does not appear to be a clear mechanism to ensure that the revenue derived from Local Governments for this purpose will be directed and managed to ensure this is able to occur. Given the backlog in asset renewal that are highlighted in the proposed changes to the Access Arrangements, Local Governments seek strong assurances that the revenue will be available to replace these assets in a timely fashion.

Street lighting technology is developing rapidly, offering significant energy efficiency and street lighting performance benefits. It is recommended that the Access Arrangement include investment in replacing old, inefficient street lighting technology in a planned and timely fashion. The investment timetable over this access period to upgrade 80 watt mercury vapour street lights that have reached the end of their service life with energy

efficient 42 watt CFL's or LED street lighting should be clearly set out in the Access Arrangements.

LAND DEVELOPMENTS

Timely availability of network capacity to support developments, particularly in regional areas, and the prices proposed by Western Power for network expansion / augmentation are of concern to local authorities.

Case Study

In 2009 the Shire of Lake Grace received approval from the Western Australian Planning Commission to subdivide a lot to provide for the creation of a new roadhouse, motel and aged persons unit site. Planning approval conditions included the requirement to provide an underground electricity supply service to the proposed new lot, to the specifications and satisfaction of Western Power.

In response to a design and quotation application, Western Power advised that the estimated cost of providing an electricity supply service to the new lot would be **\$162,420**, an amount that would likely have resulted in the proposed projects becoming unviable. Following negotiations between the Shire and Western Power, a revised quotation of **\$4,967** to undertake the necessary power supply works was received and subsequently paid.

The ability to be responsive to a dynamic property development market is important to a all land developers, including Local Governments.

State Underground Power Program

The proposed Access Arrangements clearly establish that due to their age and condition, strengthening and replacing wooden poles will require significant re-investment over the coming five years. The opportunity to leverage the investment of the State and Local Governments in the Underground Power Program to enhance the reliability and performance of the distribution network is not clearly addressed in the proposed changes to the Access Arrangement.

Western Power policy requires that developers and Local Governments requiring overhead distribution infrastructure to be moved or modified underground the cables. However, this policy does not apply as Western Power progressively replaces poles and associated infrastructure as it reaches the end of its service life, or fails.

From a public perspective, the most efficient opportunity to move to a more secure, underground power distribution network is when significant parts of the overhead system are being replaced. It is recommended that this be factored in as part of the planned investment by Western Power.