

Our Reference: 63570



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Dear Sirs

### **MID WEST ENERGY PROJECT (SOUTHERN SECTION)**

In light of the Authority's draft determination of 14 November 2011, Crosslands Resources Ltd (Crosslands) appreciates the opportunity to provide further comment on the new facilities investment test for Western Power's Mid West Energy Project (MWEP) (Southern Section).

Crosslands owns and operates the Jack Hills iron ore mine, located 380 kilometres north-east of Geraldton, and also owns 50% of Oakajee Port and Rail Pty Ltd (OPR). One of the largest tenement holders in the region, Crosslands is jointly owned by Murchison Metals Ltd and Mitsubishi Development Pty Ltd. It is currently operating the Stage 1 Jack Hills iron ore operation and conducting a bankable feasibility study for a major expansion with an expected mine life of 39 years.

On 24 November 2011 it was announced that Mitsubishi Development Pty Ltd has entered into a conditional purchase agreement with Murchison Metals Ltd in relation to all of the Murchison's interests in Crosslands and OPR. The transaction requires the approval of Murchison shareholders in February 2012.

Crosslands is currently evaluating power supply options for its Jack Hills Expansion Project (JHEP). The power demand for the expansion is currently projected to be 220MW for a two module magnetite processing facility but a subsequent third module is being considered which would increase the power demand. Reliable and economic supply of electricity is critical to Crosslands.

The feasibility study for the JHEP includes the development of a competitive, long-term power supply from generators in the South West Interconnected System (SWIS). The SWIS power supply includes two essential infrastructure components; (i) a high voltage direct current connection from Three Springs to Jack Hills, developed by Crosslands, and (ii) an access contract with Western Power at Three Springs with capacity for the JHEP and expandable to meet future demand growth.

**A GROWING  
AUSTRALIAN  
IRON ORE  
EXPORTER**

An access application (ref:SW110314A) was submitted by Crosslands to Western Power on 1 March 2011 and is currently being processed by Crosslands and Western Power.

Securing a SWIS power supply on the scale that is anticipated by Crosslands will materially benefit the network and existing customers. In addition to the incremental revenue that would result, other anticipated benefits would flow from the scale and the technology of a Crosslands connection such as more efficient use of regulated capital, increased redundancy and robustness of Western Power's transmission line to Three Springs, and operational benefits of a large scale direct current converter station at Three Springs.

The timely completion of the MWEP is a prerequisite for Crosslands securing a SWIS power supply. In order for Crosslands (and other customers) to plan effectively and to make efficient investment decisions it is critical that we understand the decision pathway as the nature of the Authority's draft determination provides considerable uncertainty in the following areas:

- Incremental revenue and net benefits;
- Natural growth concept;
- Objectives of the code;
- Negotiated contributions;
- Speculative fund;
- Quantum and threshold of NFIT risk; and
- An NFIT approval pathway.

Each of these concerns is dealt with in more detail below.

### **1) Incremental Revenue and Net Benefits**

In the draft determination the Authority provides discussion around its opinion that the incremental revenue and net benefits claimed by Western Power are overly optimistic. The discussion refers to proposed new mining loads and implies consideration was given only to the new mining loads that are known and was not given to foreseeable growth in generators and other mining loads over the 60 year life of the proposed asset. The NFIT test in the Electricity Network Access Code (Code) refers to the net benefit being over a reasonable period of time and the definition of a "reasonable time" should be judged in the context of the asset life. With this in mind, Crosslands believes that the Authority should not specifically be a judge of the certainty or uncertainty of individual generators or mining loads but is obliged by the Code instead to consider in a probabilistic or macro sense, all forecast growth in generation and mining loads in the region over the asset lifecycle. Given the current regulatory environment that supports renewable power development, the forecast demand for mineral resources and the amount of investment to date in developing the Mid West region, Crosslands' opinion is that it is highly probable and almost inevitable that the net benefit from the MWEP will exceed the new facility investment over a reasonable period of time as provided for in the Code.

## **2) Natural Growth Concept**

The statement in the draft determination that “a much lower cost solution could be adopted to accommodate natural load growth” appears not to be valid on its own, the Code does not define “natural growth” and the Code relates equally to generators and transporters of electricity. Specifically, the definition of “net benefit” in the Code refers to those who generate, transport or consume electricity so natural load growth is therefore too narrow a concept. The Code does not appear to contemplate a natural growth test but if it were applied then the Authority should consider a consensus view of what natural growth means (i.e. it should clearly include more than historic growth of small franchise loads, should somehow contemplate Western Power’s access queue and should consider the future natural drivers for growth such as underlying development investment, demand for minerals and drivers for renewable and other generation) and it should be inclusive of generation, transport and consumption of electricity. Given the very large volume of generation in the Western Power access queue, it seems that a lower cost solution would be unlikely to accommodate natural growth in generation, transport and consumption of electricity over a reasonable timeframe.

## **3) Objectives of the Code**

The stated objective in the Code is to promote economically efficient investment and operation of networks. Furthermore, the Code says that the Authority must have regard to the Code objective. Given the very long lifecycle of network assets, a long-term investment timeframe is implicit to the objective of the Code, whilst the short-term strategy that appears to underpin the draft determination, runs counter to the Code and the Authority’s obligations. There are examples in the SWIS (such as the most recent Mid West power line being developed at 132kV rather than 330kV) where a short-term investment timeframe has massively undermined efficient investment in a 60 year asset and the operation of the network.

## **4) Negotiated Contributions**

The Authority suggests that Western Power may obtain funding contributions from new loads by commercial negotiation which is theoretically possible but practically has proved to be unsuccessful for shared network services elsewhere. Each customer has its own timeframes and strategic interests and these must inevitably drive individual decision making. Network development in the Pilbara is evidence that even when there is considerable efficiency or savings to be achieved it is not likely to be possible to get a negotiated shared services outcome that approximates to what the Authority suggests. The objective of the Code seems largely intended to prevent the inefficiency that comes from this type of approach.

## **5) Speculative Fund**

The Authority also suggests that Western Power may place the asset in a speculative fund but there are inconsistencies with this approach too. Whether it is Western Power or a private sector entity, speculation is a risk versus reward proposition and it is not conceivable that a speculator (other than the state government) will be able to raise funds based upon the risk proposed by the Authority in return for a regulated return (the remainder of the consequential benefit of the new facility flowing to customers). Western Power effectively operates as a regulated monopoly and it seems inconsistent with the Code and with Western Power's mandate that it should manage a speculative fund, especially for the purpose of building a covered network.

## **6) Quantum and Threshold of NFIT Risk**

The draft determination contains only a partial finding in that it does not quantify the magnitude of the NFIT risk or provide guidance to what the test of certainty is for incremental revenue and net benefit. Understanding these points is essential for Crosslands and other potential customers in order to make informed and efficient decisions and the Authority is requested to address these points in its final determination. In paragraph 1) above, it is argued that the Authority should consider the incremental revenue and net benefit in a macro sense rather than being a judge of individual customers, if this approach is not followed then Crosslands particularly would like to know what the threshold is for the Authority to include in its assessment for Crosslands incremental revenue and net benefit.

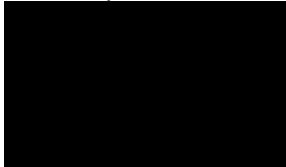
## **7) NFIT Approval Pathway**

To further support effective decision making of customers, if unconditional NFIT approval is not provided by the Authority, then Crosslands requests that the Authority provide a clear NFIT approval pathway. The preferred approach is for the Authority to firstly say what proportion of the new facility cost currently satisfies unconditional NFIT approval and does not present NFIT risk. Then for the balance of the new facility cost to say what conditions need to be met in order to satisfy NFIT, it would also help to know the threshold or test for achieving the respective conditions.

Crosslands continues to support the Mid West Energy Project proceeding and believes that it is an essential development in the efficient provision of network services. The capacity that Crosslands has applied for will specifically rely upon Western power's Mid West Energy Project. Please feel to follow up with myself or with Crosslands' Manager Power, Colin Stonehouse, who can be contacted at [cstonehouse@crosslands.com.au](mailto:cstonehouse@crosslands.com.au) or 0419 903 152.

We thank you for the opportunity to provide this submission.

Yours sincerely



**Andrew Caruso**  
**CHIEF EXECUTIVE OFFICER**