



INDEPENDENT
MARKET
OPERATOR



ERA Submission

GSI – Allowable Revenue and Forecast Capital Expenditure
Submission for the period 1 July 2015 to 30 June 2019

26 November 2015

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Executive Summary

In accordance with the Gas Services Information Rules (GSI Rules), this submission is made on behalf of the Independent Market Operator (IMO) seeking approval from the Economic Regulation Authority (ERA) for the Allowable Revenue and Forecast Capital Expenditure related to the functions of operating the Gas Services Information functions in Western Australia for the three year Review Period commencing on 1 July 2016.

On 30 September 2015, the Minister for Energy, the Honorable Dr Mike Nahan announced the transfer of most of the IMO functions related to the operation of the GSI to AEMO. The transfer of functions of the IMO to AEMO will take at 8am on Monday 30 November 2015, but will not include the transfer of certain aspects of the rule change administration or compliance functions which will remain with the IMO until a decision is made on where these functions will reside.

Due to the timing of the Minister's announcement, this submission has been prepared on a business as usual basis.

This constitutes the IMO's second Gas Services Information (GSI) Allowable Revenue and Forecast Capital Expenditure submission.

The IMO is seeking Allowable Revenue across the three-year Review Period of \$6.868 million, which represents a decrease of \$0.342 million or 4.7% on the approved Allowable Revenue for the current Review Period.

This compares to an effective indexation factor between the two Review Periods of 7.5%.

The IMO is seeking Forecast Capital Expenditure across the Review Period of \$0.614 million, which represents an increase of \$0.153 million or 33% on the approved Forecast Capital Expenditure for the current Review Period.

The IMO functions were expanded to include the Gas Services Information (GSI) activities in August 2013. The costs related to the WEM functions are subject to a separate joint Allowable Revenue and Forecast Capital Expenditure submission covering the same Review Period.

In summary, the IMO is seeking approval of its Allowable Revenue and Forecast Capital Expenditure across the three-year Review Period as set out below:

	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
ALLOWABLE REVENUE	\$2,362	\$2,454	\$2,053	\$6,869
FORECAST CAPITAL EXPENDITURE	\$214	\$189	\$211	\$614

1. Introduction

In accordance with rule 108 of the Gas Services Information (GSI) Rules, the Independent Market Operator (IMO) must seek approval of its Allowable Revenue and Forecast Capital Expenditure from the Economic Regulation Authority (ERA) for the three-year Review Period commencing on 1 July 2016.

The GSI Services for determination of Allowable Revenue by the ERA are set out under rule 107 of the GSI Rules:

- to establish, operate and maintain the Gas Bulletin Board (GBB);
- to register or deregister Registered Participants and Registered Facilities and to grant Exemptions;
- to prepare and publish the Gas Statement of Opportunities (GSOO);
- to make Amending Rules and Procedures, including the initial Rules made by the Minister under regulation 6 of the GSI Regulations;
- to facilitate the processes of the Gas Advisory Board;
- to monitor compliance and investigate breaches or possible breaches of the Rules or the Procedures;
- to take enforcement action under the GSI Regulations;
- to manage information gathering and disclosure functions under the GSI Regulations and the Rules; and
- services deriving from the exercise of any other functions conferred on the IMO under the GSI Act, the GSI Regulations or the Rules.

The IMO/AEMO budget is based on the costs that would be incurred by a prudent provider of the defined services, acting efficiently, whilst effectively promoting the GSI Objectives.

The purpose of this submission is to provide relevant information to the ERA for it to assess and approve the IMO/AEMO's Allowable Revenue and Forecast Capital Expenditure for the Review Period 1 July 2016 to 30 June 2019.

Allowable Revenue is defined as the revenue that may be recovered through fees to meet the costs of providing the IMO/AEMO's services to the market.

Forecast Capital Expenditure is defined as the predicted sum of capital expenditure required for a Review Period.

The ERA must determine the Allowable Revenue and Forecast Capital Expenditure of the IMO/AEMO for the Review Period by 31 March 2016.

1.1 Legislative Framework

In 2011, the Western Australian Government appointed the IMO to be the operator of a new GBB and GSOO. The IMO is a body corporate that was established on 1 December 2004 to administer and operate the Wholesale Electricity Market (WEM) of Western Australia.

The key roles and functions of the IMO in relation to the GBB and GSOO are set out in the following instruments:

- Gas Services Information Rules; and
- *Gas Services Information Regulations 2012*.

1.2 GSI Objectives and Primary Purpose

The *Gas Services Information Act 2012* sets out the objectives and primary purpose of the GBB and GSOO.

The Primary purpose of the GBB:

“The gas bulletin board is a website the primary purpose of which is to include information relating to short and near term natural gas supply and demand and natural gas transmission and storage capacity in the State.”

The Primary purpose of the GSOO:

“The gas statement of opportunities is a periodic statement the primary purpose of which is to include information and assessments relating to medium and long term natural gas supply and demand and natural gas transmission and storage capacity in the State.” (section 5(1) of the *Gas Services Information Act 2012*)

The Objectives of the GBB and GSOO:

“The objectives of the GBB and GSOO are to promote the long term interests of consumers of natural gas in relation to —

- a) the security, reliability and availability of the supply of natural gas in the State;
 - b) the efficient operation and use of natural gas services in the State;
 - c) the efficient investment in natural gas services in the State;
 - d) the facilitation of competition in the use of natural gas services in the State.”
- (section 6 of the *Gas Services Information Act 2012*)

1.3 Allowable Revenue and Forecast Capital Expenditure Approval Mechanisms

After the Allowable Revenue and Forecast Capital Expenditure for the Review Period is determined by the ERA, the IMO is required to prepare budgets annually that are consistent with the ERA determination.

The annual budgets are submitted to the Minister for Energy for approval as part of the IMO Annual Operational Plan and provide the basis for the calculation of GSI Fees.

If an annual IMO budget proposal is likely to result in revenue recovery (over the Review Period) of more than 15% of the ERA determination, the IMO is required to apply to the ERA for a reassessment

of its Allowable Revenue. On the basis of the amounts included in this submission, the 15% threshold equates to \$1.030 million.

Similarly, if an annual IMO Budget Proposal is likely to result in capital expenditure (over the Review Period) being 10% greater than the capital expenditure approved by the ERA, the IMO is required to apply to the ERA to approve the adjusted Forecast Capital Expenditure. On the basis of the amounts included in this submission, the 10% threshold equates to \$61,400.

These reassessment mechanisms exclude Declared Market Projects that involve major changes to the IMO's function or a major change to market systems. For the next Review Period, the threshold that would apply for a Declared Market Project is \$0.748 million.

Any Declared Market Project requires ERA approval before the project can commence.

1.4 Basis for this Submission

The IMO makes this submission on a business as usual basis. However, it is acknowledged that the business requirements of Market Participants and stakeholders have a heavy influence on the IMO's workload and subsequent expenditure.

The Minister for Energy's announcement on 30 September 2015 that the functions of the IMO will transfer to AEMO on 30 November 2015 may impact the future business requirements on which this submission has been prepared. If this is the case, the submission may be subject to review under the funding arrangements that are put in place for the transfer.

The GSI Rules place an obligation on the IMO to progress and administer proposed Rule Changes submitted within a prescriptive set of timeframes and while there is a degree of flexibility with regard to implementation timeframes, under normal circumstances the IMO is not in a position to delay the implementation of a Rule Change until the next Allowable Revenue period.

Consequently, while this Allowable Revenue and Forecast Capital Expenditure submission makes allowance for the operating and capital expenditure to support business as usual activity, it is possible that during the Review Period Gas Market Participants will request the IMO to undertake activity that was not budgeted in this submission.

Where this has occurred in the past in relation to its WEM functions, the IMO has separately identified and justified the activity as a special project and incorporated this into the IMO's annual Operational Plans for the Minister's consideration.

1.5 Allocation of costs across the IMO's electricity and gas functions

The IMO functions were expanded to include the Gas Services Information (GSI) activities in August 2013.

This submission is specific to the IMO's responsibilities under the GSI Rules.

The costs related to the IMO's WEM related functions are subject to a separate Allowable Revenue and Forecast Capital Expenditure submission covering the same Review Period.

While many costs are directly attributable to the IMO's functions under the GSI Rules (e.g. the cost of consultants preparing forecasts for the GSOO), some of the IMO's overheads are shared across both functions (e.g. accommodation). Where this occurs a detailed costing methodology has been used to apportion costs – a copy of this is contained in the detailed working papers.

2. Recurrent Budget 2016/17 – 2018/19

2.1 Budget Categories

Budgeted expenditure in this submission has been broken into the cost categories required by the Auditor General for the IMO's Financial Statements.

These cost categories are:

- *Employee Benefits Expense* – salaries, superannuation, payroll tax, fringe benefits tax and other staffing costs.
- *Supplies and Services* – includes IT expenditure, accounting, auditing, human resources, administrative costs, insurance, travel and training. In addition, consultant expenditure in support of service delivery.
- *Accommodation* – Portion of office rental, cleaning, electricity, maintenance and car parking.
- *Depreciation* – depreciation of fixed assets, including capital costs associated with the GSIP.
- *Borrowing* – interest expense.

2.2 Comparison: 2013/14 – 2015/16 Actual/Budget to 2016/17 – 2018/19 Submission

The budgeted expenditure for the current Review Period compared to the next Review Period is set out below:

Description	2013/14 - 2015/16 Actual/Budget	2016/17- 2018/19 Submission	Increase/ (Decrease)	
	(\$'000)	(\$'000)	(\$'000)	%
Employee Benefits Expense	\$2,401	\$2,912	\$512	21%
Accommodation Costs	\$276	\$317	\$41	15%
Supplies and Services	\$1,622	\$1,991	\$368	23%
Borrowing Costs	\$223	\$126	-\$98	-44%
Depreciation	\$1,582	\$1,522	-\$60	-4%
Total Expenditure	\$6,105	\$6,869	\$764	13%

More detailed information in respect of the comparison is provided at Appendix 1.

A simple comparison of financial performance between current review period and the submission for the next review period reflects an increase in net expenditure of \$0.763 million or 12.5%.

Explanations in respect of significant variations across the two periods are set out in below sections:

2.3 Cost Comparison: 2015/16 – 2018/19

The table below sets out the amounts budgeted for across the next Review Period compared to 2015/16 Budget:

	2015/16 (\$'000)	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
Employee Benefits Expense	\$824	\$946	\$972	\$994	\$2,912
Accommodation	\$96	\$101	\$106	\$110	\$317
Supplies and Services	\$705	\$637	\$672	\$682	\$1,991
Borrowing Costs	\$63	\$60	\$45	\$21	\$126
Depreciation	\$572	\$618	\$659	\$246	\$1,522
Total Expenditure	\$2,260	\$2,362	\$2,454	\$2,053	\$6,869

2.4 Annual Indexation

This submission incorporates annual indexation costs, which have been based on the Department of Treasury advice of 2.50% across the Review Period.

Excluded from this indexation are costs that are covered by fixed price contracts, where the IMO has received specific advice for a cost category and borrowing costs.

2.5 Employee Benefits

2.5.1 Approved positions

The IMO currently has 47 approved positions, corresponding to 45.7 FTE after adjusting for part-time positions.

The IMO has determined that no additional positions will be required to meet business needs in the next Review Period.

A detailed schedule showing the FTE split of all IMO staff between electricity and gas, together with a full reconciliation of all current approved positions to the positions approved in the previous ERA Determination is available as part of the detailed working papers which support this submission.

The detailed FTE split between gas and electricity is informed by a comprehensive costing methodology which allocates overheads between gas and electricity. This is also available as part of the detailed working papers.

The costing methodology identifies 40 FTE for WEM related responsibilities and 5.7 FTE for GSI related responsibilities.

The 5.7 FTE for GSI related responsibilities represents 12.1% of the total IMO approved FTE. The ERA Determination for the current Review Period approved 5.5 FTE out of a total of IMO FTE of 43 FTE – representing 12.8% of the IMO total. While the proportion of FTEs costs allocated to GSI is similar between the two periods, the increase in IMO FTE from 43 to 47.5 is a key factor in the increase in GSI employee costs between the two review periods.

2.5.2 Salary Increases

Employee Benefit Expenses is the IMO's biggest expenditure category, accounting for 42.4% of the total budgeted expenditure across the Review Period.

The IMO reviews staff performance and recommends salary increases commensurate with performance with effect from 1 April of each year.

Annual salary increases across the Review Period have been budgeted at 2.50% pa in line with Department of Treasury advice.

2.6 Accommodation Costs

Accommodation expenditure accounts for 4.6% of the total budgeted expenditure across the Review Period.

The IMO moved to new offices on Level 17 of 197 St Georges Terrace on 3 September 2012, which provides an area of 857m².

The rental rate for the new premises commenced at \$660/m² with 4% annual increases built into the lease agreement on the anniversary date of 1 October each year.

The current lease agreement is for 10 years with an option for the IMO to exit from the lease after 5 years. This submission has been prepared on the basis that the IMO remains in the current accommodation for the Review Period.

Accommodation costs increase by 4% per annum in line with the current lease agreement.

2.7 Supplies and Services

The IMO is a small, professionally-staffed organisation which is strongly reliant on the outsourcing of specialist services to ensure highest quality input at an efficient cost.

Supplies and Services accounts for 29.0% of the total budgeted expenditure across the Review Period.

	2015/16 (\$'000)	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
Corporate	\$158	\$149	\$150	\$168	\$467
Legal and Compliance	\$92	\$55	\$55	\$56	\$166
Development and Capacity	\$259	\$199	\$224	\$210	\$634
Operations and Technology	\$196	\$234	\$242	\$248	\$724
Total Expenditure	\$705	\$637	\$672	\$682	\$1,991

Corporate costs include the contribution to the IMO's accommodation, financial, human resources and other administration costs.

Legal and Compliance costs include the costs associated with the Annual Compliance Audit required under the GSI Rules, compliance investigations and dispute resolution.

Development & Capacity costs is the cost of specialist forecasting services for the annual GSOO, and administering the Gas Advisory Board meetings. This team also administers any rule changes to Gas Services Information Rules.

Operations & Technology incorporates the following costs:

- GBB system maintenance and support;
- datacentre hosting by specialist service providers;
- high speed fibre links between head office, production and backup datacentres;
- specialist database support;
- IT desktop and infrastructure support; and
- telecommunications and internet access costs.

Operations and Technology budgeted costs are impacted by additional desktop support built into the Review Period expenditure and additional software license costs.

Corporate costs include staffing related costs (e.g. staff training, recruitment), corporate governance matters (e.g. strategic planning, audit) and general administration expenses.

2.8 Depreciation

Depreciation accounts for 22.2% of the total budgeted expenditure across the Review Period.

Section 4 deals with the IMO's Forecast Capital Expenditure over the Review Period, which is predicated on the IMO's "Fourth IT Roadmap" for the period 2016 -2019.

A copy of the Fourth IT Roadmap, which encompasses the budgeted depreciation arrangements for the Review Period, is provided in the supporting documentation for this submission.

2.9 Borrowing Costs

Borrowing Costs accounts for 1.8% of the total budgeted expenditure across the Review Period.

All capital requirements over the Review Period are funded through fixed term loan funding arrangement provided by the Western Australian Treasury Corporation (WATC). Projected borrowing costs for the Review Period have taken into consideration existing loan facilities and the projected capital expenditure requirements of the Fourth IT Roadmap. Future loan facilities are based on projected borrowing interest rates provided by WATC.

3. Forecast Capital Expenditure 2016/17 – 2018/19

Forecast Capital Expenditure is the predicted sum of capital expenditure required for a Review Period.

The IMO has developed a key strategic IT planning document, culminating in the production of the Fourth IT Roadmap covering the Review Period 1 July 2016 to 30 June 2019.

The IT Roadmap is the primary strategic planning tool used to ensure that the planning, delivery, management and use of the IMO's IT systems optimally support the IMO's business requirements.

This IT Roadmap represents the fourth time the IMO has developed a technology roadmap and the second to consider the requirements of the GSI. It has been developed to support the IMO's Allowable Revenue and Forecast Capital Expenditure submission for the Review Period.

This submission seeks Forecast Capital Expenditure across the next Review Period as set out below:

	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
Forecast Capital Expenditure	\$214	\$189	\$211	\$614

The following categories have been used for the allocation of the Forecast Capital Expenditure in the Fourth IT Roadmap:

	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
GSI Rule Changes	\$88	\$90	\$92	\$270
GSI Enhancements	\$93	\$95	\$97	\$285
Corporate Support	\$33	\$4	\$22	\$59
Total	\$215	\$189	\$211	\$614

GSI Rule Changes and GSI Enhancements form the Gas Services Information activities outlined in the Fourth IT Roadmap with a focus on maintaining the current availability of the GBB whilst adopting evolutionary changes that are seen as valuable to its stakeholders.

Corporate Support relates to activities focused on maintaining systems and infrastructure that supports the IMO's non-core business functions.

A copy of the Fourth IT Roadmap, which encompasses the budgeted depreciation arrangements for the Review Period, is provided in the materials supporting this proposal. A comparison of the Forecast Capital Expenditure between the period 1 July 2013 to 30 June 2016 and 1 July 2016 to 30 June 2019 is provided as Appendix 2.

Appendix 1

Allowable Revenue

	Current Triennium - AR3				New Triennium			
	Actual/Projected				Budget			
	2013/14 ¹ (\$'000)	2014/15 ¹ (\$'000)	2015/16 ² (\$'000)	Total (\$'000)	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
Employees Benefit Expense	\$775	\$802	\$824	\$2,401	\$946	\$972	\$994	\$2,912
Accommodation Costs	\$89	\$91	\$96	\$276	\$101	\$106	\$110	\$317
Supplies and Services	\$422	\$495	\$705	\$1,622	\$637	\$672	\$682	\$1,991
Borrowing Costs	\$73	\$87	\$63	\$223	\$60	\$45	\$21	\$126
Depreciation	\$451	\$559	\$572	\$1,582	\$618	\$659	\$246	\$1,522
Total Expenditure	\$1,811	\$2,034	\$2,260	\$6,105	\$2,362	\$2,454	\$2,053	\$6,869

¹ Per audited results.

² Per 2015/16 Operational Plan submitted to the Minister for Energy

Appendix 2

Forecast Capital Expenditure

	Current Triennium - AR3				New Triennium			
	Actual/Projected				Budget			
	2013/14 (\$'000)	2014/15 (\$'000)	2015/16 (\$'000)	Total (\$'000)	2016/17 (\$'000)	2017/18 (\$'000)	2018/19 (\$'000)	Total (\$'000)
GSI Rule Changes	\$0	\$12	\$0	\$12	\$88	\$90	\$92	\$270
GSI Enhancements	\$23	\$98	\$142	\$263	\$93	\$95	\$97	\$285
Corporate Support	\$2	\$6	\$0	\$8	\$34	\$4	\$22	\$59
Total Expenditure	\$25	\$116	\$142	\$283	\$214	\$189	\$211	\$614