

16 October 2018

Economic Regulation Authority  
PO Box 8469  
Perth BC WA 6849

By email to [publicsubmissions@erawa.com.au](mailto:publicsubmissions@erawa.com.au)

## **Submission to the Economic Regulation Authority on the Australian Energy Market Operator's 2016-19 forecast capital expenditure adjustment proposal**

### **Overview**

Perth Energy submits this paper in response to the Economic Regulation Authority's (ERA) issues paper on the Australian Energy Market Operator's (AEMO) 2016-19 forecast capital expenditure adjustment proposal.

Perth Energy welcomes the opportunity to provide comment in relation to AEMO's proposed additional capital expenditure for the current allowable revenue period, ending 30 June 2019.

We highlight that AEMO's proposal is to increase its expenditure by \$19.5 million, rather than the \$11.2 million stated by AEMO and the ERA. The originally forecast and approved capital expenditure allowance is not an entitlement. The \$8.3 million underspend would otherwise have been passed-back through fee reductions. We therefore urge the ERA to consider AEMO's request as one for the total \$19.5 million, rather than the differential.

While we understand there is uncertainty in relation to the future of the Wholesale Electricity Market (WEM), we are concerned that this is the third adjustment to the three-year revenue requirement. Each proposal has resulted in increased WEM fees, and limited progress on the implementation of WEM reforms has been made.

Moreover, we highlight this increase in WEM fees is in the context of increases in the overall cost to serve customers (including for example, network charges and ancillary services costs), and is expected to be followed by further increases in WEM fees in the next allowable revenue period (AR5).

Perth Energy does not object to AEMO requiring more funds to undertake its market reform and market development activities. However, we believe \$19.5 million is significantly higher than what would be considered prudent and efficient to complete the works AEMO has set out in its proposal.



We consider the proposed implementation of the new energy management system (e-terra) and the upgrade of end-of-life IT infrastructure are urgent, and therefore, the additional capital expenditure of \$5.7 million is warranted. However, we question whether AEMO will require the full capital expenditure amount prior to 30 June 2019.

We also advise that the capital expenditure associated with the implementation of the two rule change proposals should be at the cost identified in the final rule change report. This is \$2.8 million not the \$3.6 million requested by AEMO.

The information provided by AEMO in its proposal is not sufficient for Perth Energy to support the recovery of \$10.2 million of costs associated with:

- eight months of a market reform program, which is being developed by the Public Utilities Office, and the implementation of which is well outside the current period; and
- the transfer of end-of-life System Management IT systems from Western Power to AEMO.

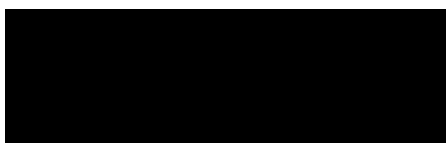
We note that in accordance with clause 2.22A.11 of the WEM Rules, the ERA can only approve costs which would be incurred by a **prudent service provider acting efficiently**, seeking to achieve the lowest practicably sustainable cost.

We do not consider AEMO has provided sufficient evidence to allow the ERA to approve additional capital expenditure of more than \$8.5 million.

Further comments on each of the AEMO's capital expenditure projects are provided at Attachment A.

Should you have any questions in relation to this submission prior to our attendance, please contact me on (08) 9420 0347 or at [e.aitken@perthenergy.com.au](mailto:e.aitken@perthenergy.com.au).

Regards,



Elizabeth Aitken

General Manager Operations



## Attachment A: Comments on specific capital expenditure items

**Issue 1: Interested parties are invited to make submission on the reasonableness of AEMO's estimate of the number and cost of the additional resources required to undertake market reform design and implementation activity in the remainder of the AR4 period.**

AEMO has not provided any information supporting its requirement for an additional 30 new staff members to implement the PUO's market reform work program.

This number of staff is similar to a medium sized stand-alone organisation and seems excessive given the support role AEMO is playing throughout the reform process, and the limited (eight-month) time left in the AR4 period.

We note that the ERA has requested further information from AEMO in relation to the increase in staff. We recommend that the ERA also satisfies itself that:

- the resource requirements relate to implementation activities, and not PUO design activities<sup>1</sup>;
- the entire increase is required to, and can be recruited in the remainder of the AR4 period; and
- the cost of the staff is able to be fully capitalised, rather than expensed.

**Issue 2: Interested parties are invited to make submissions of the reasonableness of AEMO's proposed capital expenditure for AR4 to enact the prudential exposure and notional meter rule changes by the required commencement dates.**

Perth Energy highlights that the final rule change report for the rule change proposal: Reduction of the prudential exposure in the Reserve Capacity Mechanism (RC\_2017\_06)<sup>2</sup> estimated the cost of the proposed changes was \$2.7 million.

AEMO's submission includes \$3.5 million to implement phase 1 of the IT changes necessary to implement the rule change proposal, with a further \$1.63 million in AR5. This is substantially higher than the estimate in the final rule change report.

AEMO has not provided any information supporting the increased costs. As such, we recommend that the ERA limits the total capital expenditure to \$2.7 million, and considers an appropriate apportionment over the project timeframe.

**Issue 3: Interested parties are invited to make submissions of the reasonableness of AEMO's proposed capital expenditure for AR4 to complete implementation of its energy management system.**

The current market and system operations systems were due to be updated or replaced from 2016/17. However, these plans were deferred with the intended outcome from the EMR being the adoption of the National Electricity Market (NEM) legislative framework and the associated systems and processes.

<sup>1</sup> An example of this duplication can be seen by the various industry working groups that aim to inform market participants of the reform process, including the Market Advisory Committee meetings (MAC) – an ERA meeting; the WA Electricity Consultative Forum (WAEFCF) – an AEMO meeting; and the various market reform industry forums – PUO led.

<sup>2</sup> See Appendix D, available at: [https://www.erawa.com.au/rule-change-panel/market-rule-changes/rule-change-rc\\_2017\\_06](https://www.erawa.com.au/rule-change-panel/market-rule-changes/rule-change-rc_2017_06).



We consider that, the timing of necessary upgrades of the market and system operations systems coupled with the timing of the proposed introduction of a constrained network access model provides the opportunity to introduce more appropriate IT systems, including a new energy management system.

We commend AEMO for expediting the implementation of e-terra, and support the capital expenditure of \$3.7 million being recovered from market participants.

**Issue 4: Interested parties are invited to make submissions of the reasonableness of AEMO's proposed:**

- a) Timing of the transfer of system management IT functionality to its own IT platform.**
- b) Forecast of the capital expenditure required to transfer the IT system functionality to its own platform.**

Perth Energy questions the need for AEMO to spend \$4.9 million to transfer end-of-life IT infrastructure from Western Power to AEMO.

As previously noted, WEM IT systems were due to be updated or replaced in 2016/17. Moreover, they will be largely redundant within 3-4 years as the re-designed WEM is proposed to be implemented by 2022. This will require new system operations systems to facilitate security constrained economic dispatch.

We note that AEMO has not provided the benefits or costs of any alternatives it states it has considered, including for example leaving the systems within Western Power's infrastructure. If one of the alternatives is more efficient than transitioning IT infrastructure now, the ERA should not approve the requested capital expenditure.

Furthermore, we recommend the ERA satisfies itself this investment has a pay-back period of less than 3 years, before approving the \$4.9 million in capital expenditure.

**Issue 5: Interested parties are invited to make submissions of the reasonableness of AEMO's proposed:**

- a) Timing of the transfer of market operation IT systems, currently hosted at the Malaga Data Centre, to its own cloud-based system.**
- b) Forecast of the capital expenditure required to transfer the IT systems to its own cloud-based system.**

Perth Energy has no objection to the movement of the market operations systems from the Malaga Data Centre to AEMO's private, cloud-based system as it is stated to be the lowest cost alternative

We recommend the ERA approves this expenditure.



**Issue 6: Interested parties are invited to make submissions of the reasonableness of:**

- a) The market reform and rule change activities AEMO has identified as being necessary in the remainder of AR4.**
- b) AEMO's forecast capital expenditure proposal for these activities for the remainder of AR4.**
- c) The anticipated increase in market fees in 2019/20.**

Perth Energy does not object to AEMO requiring more funds to undertake its market reform and market development activities. However, we believe \$19.5 million is significantly higher than what would be considered a prudent and efficient to complete the works AEMO has set out in its proposal.

Perth Energy is concerned the level of expenditure and resources required for market reform activities is excessive, and has not been supported by adequate information with respect to what will be achieved in the remaining eight months of the AR4 period.

Similarly, an explanation as to why the cost of implementing the prudential exposure rule change proposal has almost doubled since the final rule change report was published should be provided by AEMO prior to the ERA approving the proposed capital expenditure.

The information provided by AEMO in its submission is not sufficient for Perth Energy to support the transfer of end-of-life System Management IT systems from Western Power to AEMO.

We consider the proposed implementation of the new energy management system (e-terra) and the upgrade of end-of-life IT infrastructure are urgent, and therefore, the additional capital expenditure of \$5.7 million is warranted. However, we question whether AEMO will require the full capital expenditure amount prior to 30 June 2019.

We also support the capital expenditure associated with the implementation of the two rule change proposals at the cost identified in the final rule change report. This is \$2.8 million, rather than the \$3.6 million requested by AEMO.

As Perth Energy only supports \$8.5 million of the proposed \$19.5 million in capital expenditure proposed by AEMO, we would expect to see WEM fees adjusted accordingly.

We also highlight that this increase in WEM fees is in the context of increases in the overall cost to serve customers (including for example, network charges and ancillary services costs), and is expected to be followed by further increases in WEM fees in the next allowable revenue period (AR5).