

31 May 2019

Economic Regulation Authority  
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Perth BC WA 6849

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

## **Submission to the Economic Regulation Authority's Draft Decision on the Australian Energy Market Operator's 2019-22 allowable revenue and forecast capital expenditure proposal**

Perth Energy submits this paper in response to the Economic Regulation Authority's (ERA) draft decision on the Australian Energy Market Operator's (AEMO) 2019-22 allowable revenue and forecast capital expenditure proposal.

Perth Energy welcomes the ERA's pragmatic approach to the determination of AEMO's allowable revenue and forecast capital expenditure. The ERA has adequately addressed the concerns raised in our submission.

We provide the following comments in response to the ERA's draft decision.

We welcome the additional information provided to Perth Energy in a confidential, draft copy of AEMO's intended response to the ERA's draft decision<sup>1</sup>. We understand that AEMO has provided an advanced draft submission to help inform stakeholder's submissions and in turn facilitate the ERA's final decision. We appreciate this step and encourage AEMO to maintain this transparent approach. However, we continue to hold the view that large portions of AEMO's forecast capital expenditure and associated allowable revenue do not meet the requirements of clause 2.22A.11(b) of the WEM Rules, which states:

*"the Allowable Revenue and Forecast Capital Expenditure must include only costs which would be incurred by a prudent service provider delivering those services... acting efficiently, seeking to achieve the lowest practicably sustainable cost of delivering those services...."*

In particular, Perth Energy remains concerned about forecast capital expenditure on WEM Reform and the Digital Roadmap.

Perth Energy reiterates its publicly stated view that the cost of the design and implementation of the State Government-driven reform agenda should be wholly funded by Government. To date, the benefits (and costs) of WEM reform have not been adequately quantified. It is inappropriate that market

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<sup>1</sup> Perth Energy received an email on Friday 24 May 2019 containing a confidential, draft copy of AEMO's submission to the ERA in response to its draft decision.



participants should pay for reforms that have not been reasonably demonstrated to deliver benefits or efficiencies. Perth Energy supports WEM reform in principle. However, we consider that a market participant should only be allocated reform costs based on the benefits it is expected to receive. At this time, neither the costs nor the benefits of the WEM reform program are clear, therefore it is unreasonable to expect market participants to fund it. In the absence of a formal and detailed assessment of the costs and benefits, we consider the costs should, at least in the short term be borne wholly by the Government.

Notwithstanding this, Perth Energy considers the ERA's draft decision to approve expenditure in stages to be a pragmatic approach given the continued uncertainty regarding the scope and timing of the reform agenda. However, we recommend each project within the program is also independently estimated justified.

We also consider the ERA's draft decision not to approve forecast expenditure related to the Digital Roadmap is prudent given the lack of information on the costs and benefits provided by AEMO. While we agree in principle that the integration of WA operations into AEMO is necessary to realise the cost efficiencies intended from the takeover of operations from the former Independent Market Operator and Western Power, to date market participants have seen little evidence of benefits to the WEM.

Perth Energy welcomes any efficiencies offered by AEMO. However, it has not to our knowledge quantified, or included any operating efficiencies for the WEM or capital expenditure reductions that it expects to result from the implementation of the Digital Roadmap. On this basis we struggle to see how this program can be approved under the WEM Rules.

As with WEM reform, Perth Energy is not opposed to AEMO undertaking work to improve its digital capabilities, however, AEMO must demonstrate what efficiencies and benefits will ultimately be delivered to the market participants that pay for it. Given the lack of detail and the magnitude of the proposed expenditure, Perth Energy recommends the Digital Roadmap is treated as a Declared Market Project and the necessary justification for the program is shared with the ERA and market participants prior to incurring expenditure.

We support the ERA's request for further information on the methodology used by AEMO to determine its proposed project contingencies. We do not believe a blanket top-down allocation of contingency, as was initially proposed by AEMO, to be appropriate. However, we cannot expect AEMO to be able to perfectly forecast project costs up to three years in advance, and so we recognise an allowance for contingency is a reasonable request. On this basis we share the ERA's view that any project contingency should be justified based on identified risks associated with each project. We highlight however, that not every project will require additional expenditure, as some projects will be below forecast.

We do not agree with the ERA's suggested alternative that project contingencies need not be justified and AEMO may simply use the provisions in clause 2.22A.9 of the WEM Rules instead. We believe this clause is intended to be used for unforeseen capital requirements that arise during the period. To use this mechanism to accommodate overspends on known projects is not prudent and may drive inefficient behaviour. It may also result in unnecessary complexity and unexpected in-period adjustments if unforeseen costs to emerge during the period and the 10 per cent allowance has already been exhausted on project contingencies that should have been budgeted for.



Instead, we recommend the ERA reviews the additional risk-based justification provided to it by AEMO and then allows a contingency amount it considers appropriate given the scope, expected cost and risks associated with the projects it decides to approve. Perth Energy also requests the ERA monitors the actual project costs AEMO incurs during the period and to the extent possible, holds AEMO to account for delivering projects within the project baseline amounts during its next allowable revenue review.

Should you have any questions in relation to this submission, please contact me on [REDACTED] or at [REDACTED].

Regards,

[REDACTED]

Elizabeth Aitken

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