



Notice

9 September 2022

Western Power's fifth access arrangement review

Draft Decision

The Economic Regulation Authority has published a [draft decision](#) on Western Power's access arrangement proposal for the period 2022/23 to 2026/27.

The draft decision sets out the amendments Western Power must make before the ERA will approve the access arrangement.

The draft decision sets a target revenue of \$9 billion that Western Power can earn over the five-year period and forecast annual increases in network tariffs of between 7.5 to 8 per cent for the years 2023/24 to 2026/27.¹

The draft decision is higher than proposed by Western Power (target revenue of \$8 billion and a one-off increase of 3.7 per cent in network prices in 2023/24) due to significant increases in inflation and interest rates since Western Power prepared its proposal.

Western Power's network tariffs are charged to users of the network including electricity retailers (such as Synergy), generators and some very large industrial and mining companies connected to the transmission network. Electricity retailers decide how to pass on the network charges they incur to their customers. Most residential customers and business customers who use less than 50 MWh of electricity each year are supplied by Synergy and are on a regulated retail tariff set by the State Government. In the most recent State Budget, Government indicated electricity tariffs for residential and small business customers will increase in line with forecast inflation over the next three years.²

The access arrangement is required under the *Electricity Networks Access Code 2004*, and sets out the terms and conditions, including prices, for third parties seeking to access the Western Power network.

An [Overview](#) of the draft decision is attached to this notice.

Invitation for submissions

The ERA invites interested parties to make submissions on the draft decision.

Submissions close 4:00 pm (WST) Friday, 16 December 2022.

¹ Based on forecast inflation of 3 per cent each year.

² [State Budget 2022-23 Budget Paper No. 3 Economic and Fiscal Outlook](#) p. 329.

Submissions should be lodged online using the form on our website
www.erawa.com.au/consultation.

Public forum

The ERA is holding a public forum to explain the draft decision at 2:00 pm on Tuesday 27 September at the Four Points by Sheraton Perth, 707 Wellington Street. Further information and details on how to register for the forum can be found [here](#).

Further information

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Overview

Western Power's fifth access arrangement is being determined during a period of significant change in the energy sector. At the same time, financial conditions are uncertain with high inflation and rapidly rising interest rates.

Customers and businesses are changing their behaviour and demanding energy from cheaper, greener sources, as well as generating their own electricity from roof-top solar systems. Government and corporate policies to reduce carbon emissions are encouraging the development and ongoing increase in the number of storage systems and large-scale wind and solar farms looking to join the network. With the electricity supply chain traditionally designed around thermal baseload generation, the consequence is an electricity industry undergoing a once in a century transformation. The electricity network - the mechanism needed to transport a reliable supply of electricity between suppliers and customers – is caught in the middle of this disruption and needs to respond. Western Power faces the challenge of planning, costing and implementing rapidly evolving technologies and responding to more frequent and severe weather events from our changing climate. The scale of the changes underway require fundamental shifts in investment and the ongoing operation of the network.

Uncertainty in current financial and economic conditions influences the costs of financing and delivery of the essential investment needed in the network. Western Power's proposal was costed over a year ago. Since then, changing economic and financial conditions have seen significant increases in inflation and interest rates. Increases in interest rates are outside of the control of both Western Power and the ERA, yet these increases determine the Western Power's cost of capital and drive most of the change in revenue. If Western Power costed its proposal today, the revenue required over the regulatory period to 2027 to deliver its proposed projects, would be considerably higher (\$942 million or just under 12 per cent in nominal terms). Without smoothing, this is equivalent to a 19 per cent increase in network prices in 2023/24 after which prices remain flat. This contrasts with Western Power's initial submission for a one-off increase of 3.7 per cent in network prices in 2023/24.

The challenge to the ERA in considering Western Power's access arrangement is to ensure that customers are not exposed to excessive costs and risks from the ongoing uncertain conditions, while also enabling Western Power to fulfil its role in supporting the energy sector's transformation over the next few years.

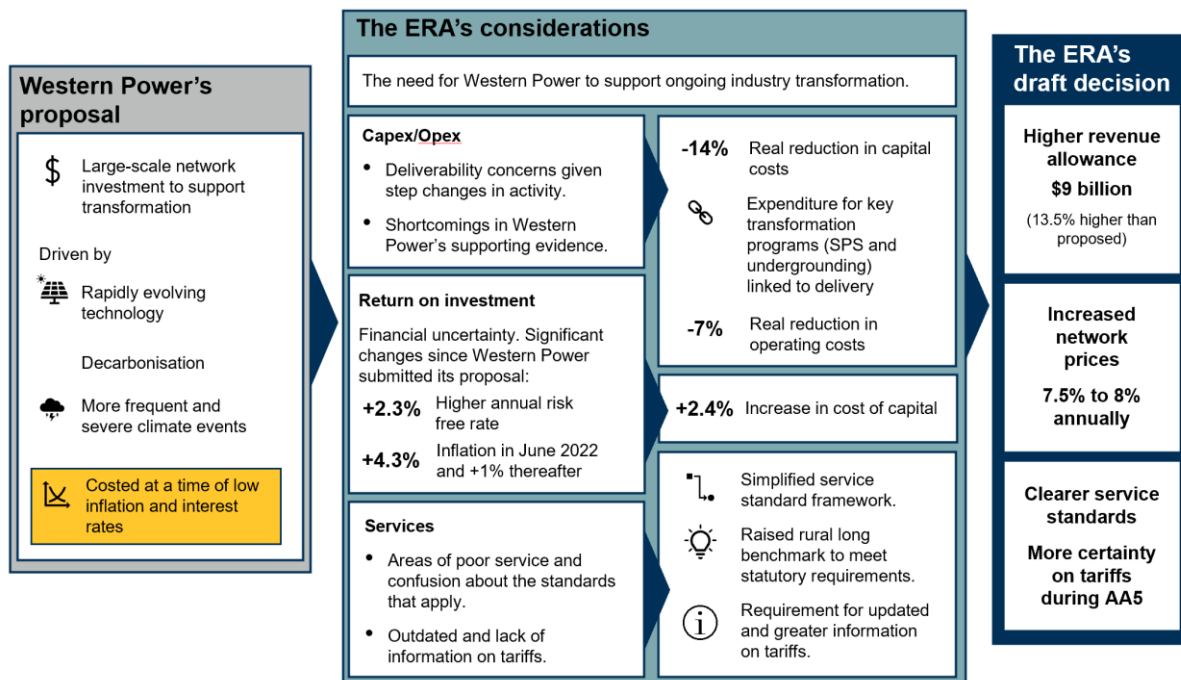
This draft decision enables Western Power to deliver energy transformation programs at a realistic pace, and ensures customers only pay for the network enhancements Western Power delivers.

In making its draft decision, the ERA has:

- Carefully considered Western Power's proposal and advice from the ERA's technical consultant on the proposal.
- Independently sought stakeholders' feedback on Western Power's proposal and Western Power's performance in providing reliable electricity to customers, particularly in the regions.
- Been mindful of the State Government's decarbonisation goals and projects such as advanced metering and standalone power systems, established to help achieve these goals.
- Incorporated current market interest rates and forecast inflation.
- Embedded in its draft decision recognition of the expanded Access Code objective that requires consideration of the environmental consequences of energy supply and consumption.

The draft decision results in target revenue of \$9 billion and forecast annual increases in network prices of between 7.5 to 8 per cent for the years 2023/24 to 2026/27. Key elements in the draft decision are summarised in Figure 1 below.

Figure 1: Draft decision summary



Overall, Western Power's proposal outlines project initiatives that are consistent with the transformation and ongoing care and maintenance of the network.

The ERA has approved increases to operating costs compared to the last access arrangement period (AA4) for the transformational change required over this access arrangement period (AA5).³ However, to encourage Western Power to seek efficiencies the ERA has included a 2 per cent productivity factor that requires Western Power to deliver operating efficiencies consistent with other network operators in Australia.

Western Power's advanced metering program is a key enabler of the transformation and the ERA has approved Western Power's proposed expenditure to complete the roll-out of the program over AA5.⁴ Approval of this expenditure in full in the ERA's final decision will require Western Power to fully detail and quantify the benefits of accelerating the advanced metering program and demonstrating it can be delivered in AA5.

The size of other capital programs and projects, such as undergrounding overhead power lines in urban areas and installing standalone power systems in regional areas, show large step-changes in the quantity of work Western Power expects to undertake in AA5. The activity proposed is well above the levels delivered in AA4 and the ERA has concerns about the scale and deliverability of these programs. Instead of approving the proposed expenditure in full, the ERA has included proposed costs for both programs in the Investment Adjustment Mechanism. This provides flexibility so that if Western Power over or under delivers against the activity and approved expenditure, the expenditure variation can be adjusted at the next access arrangement. This ensures that customers

³ AA4 covered the period from 2017/18 to 2021/22 and AA5 covers the period from 2022/23 to 2026/27.

⁴ Under a business-as-usual approach, the program would be completed in AA6. Western Power has proposed to accelerate the program to complete it in AA5.

are protected by only paying for what Western Power delivers, and also that Western Power is funded if it delivers the programs efficiently and more quickly.

Western Power's evidence supporting its proposed asset replacement costs and IT expenditure does not demonstrate that these costs are reasonable and efficient. The ERA has approved lower capital expenditure for these programs in the draft decision. However, the ERA has acknowledged the importance of Western Power's expenditure in cyber security which is necessary to protect the integrity of the network and consumers. Western Power will need to provide additional information to the ERA in support of any higher expenditure for cyber security in its response to the draft decision.

Further transmission investment may be required during AA5 so more renewable generation and new loads can connect to support decarbonisation and electrification of the economy. Western Power can reopen the access arrangement at any point during AA5 to request an increase in revenue to fund such investment.

The draft decision is made at a time when there is considerable uncertainty in financial markets. The ERA has accepted most of Western Power's proposed approach to calculating return on capital. The ERA's cost of capital calculation for the draft decision (7.1 per cent) reflects the current inflation forecasts and interest rates. The return on capital will change again for the final decision based on the market data sampled at the time.

The ERA opts to maintain the current approach to calculating the cost of debt. When compared to Western Power's proposed approach to debt, the current debt approach results in a higher cost of capital and raises the revenue requirement. The benefits of maintaining the current approach are that it accounts for efficient forward-looking financing costs and helps ensure more certain debt costs, and resulting network prices, over AA5. The ERA is open to stakeholder views on the value they place on price certainty in an environment of rapidly tightening financial conditions and highly volatile financial markets.

Historically, Western Power has provided a reliable supply of electricity to most customers but recent prolonged supply interruptions have focussed attention on outages. This focus, highlighted by the Independent Review of Christmas 2021 Power Outages shows that customers in some regions are receiving a poor level of service.

The ERA has spoken directly with regional customers experiencing poor service and what this means to them. Customers said, "Extended power outages for regional communities have multiple impacts, [including] heating and cooling of homes, schools, and businesses."

This engagement has also shown that the service standard incentive mechanism in the Access Code is difficult for customers to understand and is a blunt tool to address pockets of poor service.

The draft decision has addressed this and simplified the reliability benchmarks. The benchmark for rural long feeders has been raised to align with the standard prescribed in the *Electricity Industry (Network Quality and Reliability of Supply) Code 2005*. The ERA will also require Western Power to provide more detailed reports on its reliability performance in the regions and identify and cost options to improve reliability for those customers. Outside the access arrangement, the ERA will discuss other policy options to improve reliability with Energy Policy WA.

Next steps

The ERA invites submissions on the draft decision from interested stakeholders by 16 December 2022.

Western Power now has the opportunity to consider the draft decision and submit revisions to its proposal and supporting material by 14 November 2022.

The ERA anticipates it will publish its final decision by 31 March 2023.