

Enquiries: Peter Mattner  
Telephone: 9326 4556



**Western Power**

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Mr Alistair Butcher  
A/Director – Electricity Access  
Economic Regulation Authority  
PO Box 8469  
Perth Business Centre  
PERTH WA 6000

Dear Alistair

**Economic Regulation Authority Issues Paper  
Western Power's Proposed Access Arrangement for the South West Interconnected  
Network**

Western Power is pleased to provide a response to the "Issues Paper" published by the Economic Regulation Authority on 16 September 2005. In doing so, Western Power considers it appropriate to limit its comments to inaccuracies and matters of interpretation which could possibly mis-inform other respondents about Western Power's proposed Access Arrangement or might lead to the ERA making an error in its assessment of submissions.

Western Power would like to provide a brief response on the following matters:

- Clarification of the purpose of "Qualifying Capital Expenditure Projects" (Appendix 8 of the Access Arrangement);
- Relevance of the NFIT and Regulatory Test to capex forecasts;
- Definition of Trigger Events;
- Gain Sharing Mechanism;
- Price List Information; and
- The separate Network Advisory Services report on Service Standards.

**1. Clarification of the purpose of "Qualifying Capital Expenditure Projects"**

The interpretation of Appendix 8 ("Qualifying Capital Expenditure Projects") in the Issues Paper differs from Western Power's intended position.

In section 4.2 (page 14) of the Issues Paper, the ERA states:

Section 5.26(c) of Western Power's proposed Access Arrangement refers to Appendix 8 as listing "qualifying capital expenditure forecasts." Western Power proposes these projects be assessed for inclusion in the allowed capex and tariff price controls.

To clarify, the purpose of Section 5.26 of Western Power's proposed Access Arrangement is to define the projects that will be included in the operation of the Investment Adjustment Mechanism.

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The purpose of Appendix 8 (“Qualifying Capital Expenditure Projects”) is to list the projects that Western Power is currently aware of that may become candidates for inclusion into the Investment Adjustment Mechanism. The projects listed in Appendix 8 relate to development announcements by proponents but for which, as at 1 August 2005, no firm start commitment had been given. Western Power, acting as a prudent and efficient network operator, has not included these projects in the capex forecasts in the proposed Access Arrangement for revenue and pricing purposes but is listing these projects for inclusion in the operation of the Investment Adjustment Mechanism.

As required by section 6.17(a) of the Code, Appendix 8 provides sufficient detail for the Authority to apply the Investment Adjustment Mechanism at the next access arrangement review.

## **2. Relevance of the NFIT and Regulatory Test to capex forecasts**

The interpretation of the application of the New Facilities Investment Test (NFIT) and Regulatory Test to forecast capital expenditure (capex) in the Issues Paper differs from the requirements of the Code.

In sections 4.2.1 (page 15) and 4.2.2 (page 16) of the Issues Paper, the ERA states:

For capex forecasts to be included in the network valuation, Western Power is required to provide sufficient supporting information to demonstrate that the proposed investments satisfy the relevant Access Code tests:

- New Facilities Investment Test (section 6.52); and
- Regulatory Test (chapter 9).

To clarify, under section 6.51 of the Code, Western Power may include capex forecasts that are “reasonably expected to meet the new facilities investment test” in its forecast revenues. It is Western Power’s clear view that its capex proposals satisfy the NFIT criteria.

Similarly, under chapter 9 of the Code, there is no requirement for major projects in the capex forecasts to have passed the Regulatory Test, noting that Western Power must not subsequently commit to a “major augmentation” without Regulatory Test determination. This does not preclude Western Power from forecasting capex that includes projects that may be subject to the Regulatory Test.

Western Power’s approach is explained in further detail in the Access Arrangement Information Appendix 7, pages 27 and 28.

## **3. Definition of Trigger Events**

The Issues Paper raises a new criterion (“clear, focused and specific”) to be used in assessing the trigger events in the proposed Access Arrangement. However, this new criterion is inconsistent with the definition of trigger events in the Code and section 5.36 in particular.

In section 6.9 (page 52) of the Issues Paper, the ERA states:

The Authority is conscious of the need for both service providers and users to efficiently allocate resources to the assessment process and to provide for regulatory certainty through the access arrangement period. In this regard, the Authority is focused on ensuring that any trigger events are not easily breached and are limited to those necessary to meet the Access Code objective.<sup>63</sup> For this purpose, trigger events should be clear, focused and specific, identifying only those potential events the occurrence of which is necessary to trigger the reassessment of an access arrangement in its entirety.

To clarify, under the definition of a trigger event in the Code, there is no need for a trigger event to be specific or identify potential specific events. The definition states: “trigger event is a set of one or more circumstances specified in an access arrangement...”. Given the definition, a single trigger event can cover a range of circumstances rather than a specific event.

Section 5.36 of the Code details what the ERA must consider before determining if a trigger event meets the objectives of the Code. Section 5.36 does not include the criterion of “clear, focused and specific” outlined in the Issues Paper.

Western Power encourages the ERA to assess the trigger events in the proposed Access Arrangement against section 5.36 of the Code and the definition of a trigger event in the Code.

#### **4. Gain Sharing Mechanism**

The interpretation of the reasons for not including a gain sharing mechanism in the Issues Paper differs from Western Power’s intended position. To clarify the reasons for not including a gain sharing mechanism at this time, Western Power provides the following further explanation.

In section 4.7 (page 31) of the Issues Paper, the ERA states:

Western Power proposes that a gain sharing mechanism is not appropriate at this time, arguing that the inclusion of one would be “counter-productive” and “over-emphasise the importance of under-spending”<sup>47</sup> during the first regulatory period.

The gain sharing mechanism has not been included for a number of reasons, including:

- There are no established “innovation and efficiency” benchmarks consistent with the requirements of section 5.26 of the Code, against which to operate a gain sharing mechanism. If the benchmarks were established at this time they would be developed in an environment of significant change in which it would be very difficult to determine appropriate parameters;
- The need to “substantially increase network investment and operating expenditure to deliver the level service that customers rightly expect” (Access Arrangement Information page 158);
- It is “more appropriate to introduce a gain-sharing mechanism once expenditure levels reach a ‘steady-state’” (Access Arrangement Information page 159); and
- “The disaggregation of Western Power into four independent business units is likely to create cost uncertainty and change-management challenges in the forthcoming access arrangement period” (Access Arrangement Information page 159).

Western Power has undertaken to develop efficiency and innovation benchmarks during the first access arrangement period, which would apply from the start of the second period (Access Arrangement Information page 160).

## **5. Price List Information**

Western Power considers it has complied with the Code requirements for provision of Price List Information.

Price List Information is defined in the Code as:

“a document which sets out information which would reasonably be required to enable the Authority, users and applicants to:

- (a) understand how the service provider derived the elements of the proposed price list; and
- (b) assess the compliance of the proposed price list with the access arrangement.”

Section 8.1 of the Code leaves the service provider with discretion as to whether or not to propose that its access arrangement contains a requirement for the service provider to submit price lists for approval each year. Western Power does not propose that its access arrangement will require it to submit price lists for approval. Accordingly, section 8.7 of the Code is applicable, requiring Western Power to submit price list information to the Authority for each pricing year except for the first pricing year.

Western Power has inferred that this provision was drafted in recognition of the fact that the Access Arrangement Information would provide a description of the pricing methods applied, and would thereby set out the kind of explanatory information that would enable stakeholders to understand how the elements of the proposed price list have been derived (thus meeting the requirements of paragraph (a) in the Code’s definition of price list information, for the first pricing year). On this basis, the description of the pricing methods contained in the Access Arrangement Information effectively provides price list information enabling stakeholders to understand the elements of the “current price list” (that is, the price list for the first year) in the access arrangement.

The relevant information is contained in:

- Part D Section 5 of the Access Arrangement Information – “Pricing methods”;
- Appendix 7 of the proposed Access Arrangement – “Explanatory paper presenting details of Western Power’s price control and supporting calculations”; and
- Appendix 6 of the Access Arrangement Information – “Pricing Structure for the Transmission and Distribution Network Businesses”.

## **6. NAS Report on Service Standards**

These brief comments are deliberately limited to identifying what are believed to be factual errors in the report relevant to the ERA’s consideration of public responses, rather than a response to particular issues raised by NAS *per se*.

6.1 On page 4 of the report, last paragraph, NAS states:

“Western Power has not included average reliability performance standards in its proposed Access Arrangement ... nor is it committing to achieve the service standard benchmarks that it has proposed ...”

These statements are incorrect and misleading. The proposed service standard benchmarks (average reliability) and service standard adjustment mechanism relating to reliability are clearly articulated in the Access Arrangement submission. In particular, the benchmarks are "committed" outcomes which underpin the relevant parts of the forecast expenditures designed to achieve these service standards. Western Power faces financial penalties under the service standard adjustment mechanism if the company fails to deliver on performance.

Likewise, Recommendation 2 on Page 75 of the NAS Report incorrectly implies that average reliability performance standards have not been included in Western Power's proposals.

6.2 Definitional Issues:

The essential principles in comparing any reliability figures are the detailed definition of the particular reliability measures (including specified event exclusions) and the integrity/accuracy of the reporting systems. These principles are not adequately reflected in the NAS report and consequently, some comparisons are not made on an "apples with apples" basis.

Western Power's proposals and supporting information are clearly described in Part A, Section 5.3 of the Access Arrangement Information.

Western Power anticipates that the Authority will give due consideration to the above issues in the publication of the draft decision on the proposed Access Arrangement. We continue to look forward to working with the Authority over the coming months to attain an approved Access Arrangement by mid 2006.

Yours sincerely



**PHIL SOUTHWELL**  
**MANAGER STRATEGY & REGULATION**