energy solutions

erm power

8 February 2007

Mr. Robert Pullella
Executive Director, Competition, Markets and Electricity
Economic Regulation Authority
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Dear Mr Pullella

Western Power's Access Arrangement for the South West Interconnected Network

I refer to your Notice issued on 17 January 2007 in which you called for submissions in relation to Western Power's Access Arrangement for the South West Interconnected Network (SWIN). ERM Power submits the following comments and views.

General

ERM Power (ERM) is an energy solution specialist, electricity generation developer and wholesale electricity supplier with a proven track record in the deregulated electricity industry in Australia.

ERM is a joint owner of NewGen Power with global investment and advisory bank Babcock & Brown.

NewGen Power operates a portfolio of power stations under the "NewGen" banner and trades electricity in both the National Electricity Market (NEM) and Western Australian Electricity Market (WEM).

Apart from the 320MW Kwinana Power Station currently under construction, ERM is involved in bringing to fruition a number of other major power generation projects in Western Australia. In this context ERM continues to interact with Western Power Networks (WPN) in relation to transmission access at a number of potential power station locations in the State.

Mid West Power Station Project

One of these potential power station projects is located near Eneabba in the Mid West Region south of Geraldton. ERM is conducting a joint study with Aviva Corporation, the owner of a coal deposit at Eneabba, to examine the commercial and technical feasibility of a large scale coal-fired power station supplying power to the Mid West Region and to the SWIN. This power station would deliver the following benefits to the State:

- A billion dollar investment in the Mid West;

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- 400 construction jobs;
- 100 permanent jobs locally housed;
- Reliable and competitive power supply for the Mid West and the SWIN;
- Unlock the potential of the Mid West Region, particularly through development of its mineral resources; and
- Provide a large and stable source of power at the northern part of the SWIN with obvious network benefits.

An essential ingredient of this power station is a solid transmission connection to the SWIN. This requires an upgrade of the existing 132kV transmission system from Perth to the Mid West to at least 330kV.

The time frame in which additional power transmission capacity to the Mid West is needed, particularly to supply a number of iron ore projects, is from 2009 onwards.

In response to existing and potential demand in the Mid West, WPN is planning to construct a 330 kV line from Perth to Geraldton via Eneabba. ERM supports the intention of WPN to up-grade the line to accommodate increased demand.

Due to the enormous interest and potential loads for such a line WPN, after consultation with ERM and other developers, has recently brought forward the planned commissioning date for such a line from 2014 to 2010. This is welcomed by ERM, however, a number of large scale iron ore projects require the up-grade to be brought forward to 2009 to fit in with their project timetables.

In relation to this proposed new transmission line in particular and to our other power station developments in general, we have a number of matters we would like to bring to your attention. Some of these relate directly to the issues raised in ERA's discussion paper and some are additional, but they are all inter-related, because they centre on how users and potential users gain access to new capacity, and what rights they have in relation to that capacity.

Our comments are as follows:

Reduction in Contractual Capacity

ERM understands that WPN is proposing that contractual capacity granted under a transmission access contract can be withdrawn by WPN if that capacity is not being used.

On the surface this may seem to be a reasonable solution for a network which is constrained, and may enable capacity to be freed up without substantial investment in new infrastructure. However, at the same time, it causes some concerns particularly for new entrant generators such as ERM

which are seeking to finance projects based on certainty going forward and require firm access rights to network capacity.

It raises the issue of what rights a network user has in relation to that capacity. What is being proposed seems to limit those rights by putting in place a regime in which ownership of all capacity is essentially vested in WPN, and WPN then offers a "service" to users and potential users, with WPN also having the sole discretion to withdraw those rights under certain circumstances. Giving WPN those powers is of concern, because it has the potential to act in ways that may unilaterally and unfairly curtail a user's existing or future access to the network.

ERM agrees that there should be provisions to preclude hoarding of capacity which may prevent new entrants gaining access to the network, if capacity is in fact available and unused However, if it was decided to pursue that model of access, it may be better for an independent body to determine if capacity is available and if the holder of that capacity is behaving anti-competitively.

ERM notes that the existing provisions within section 115 of the Electricity Industry Act 2004 also deal with this issue.

An alternative model which could be considered is for users to have firm capacity rights which can be traded in whole or in part by that user. This model is used generally on gas pipelines and seems to offer users and asset owners a way of maximizing use of existing capacity and allow new entrants to gain access on a commercially negotiated basis. Access codes generally provide a framework or fall-back position for such negotiations, which are all subject to dispute resolution procedures and anti-competitive legislation.

Treatment of Capital Contributions and Headworks Charges

The network owner needs to ensure that the shared network meets the needs of all users. In relation to a connection application, WPN for example, needs to consider what augmentations (if any) are needed to the shared network in order to support the connection. If an augmentation is necessary then WPN will either:

- Apply a regulatory test to determine if the augmentation should be funded by all network users generally; or
- Require the applicant to fund the augmentation either through some form of additional charge or by way of capital contribution.

For example, an applicant may seek to connect a new mining load whose equipment generated unacceptable harmonics. This may require WPN to install network filters on the shared network which facilitate the connection as well as improve the quality of the shared system. However, the applicant gets the direct benefit of the installation of network filters through the Connection Agreement which licences the generation of otherwise excessive harmonics.

In the case where the shared network is capacity constrained, WPN may already have plans to develop and improve the network and relieve the capacity constraint as the demand grows.

However, if the applicant is prepared to bring forward the development through a capital investment, just as in the example above, the applicant should have the right to the benefit in the Connection Agreement – at least up until the time the augmentation would have otherwise occurred.

If the applicant's requirement would result in a quantum change to the shared network, then the capital contribution should be regarded as a form of headworks charge and in our view this should be developed on a commercial basis to serve the mutual interest of both parties.

Queuing Policy for Applications for Access

The queuing policy for applicants for access to WPN's system, or more particularly the application of that policy, can override commonsense commercial outcomes. An example of this is the proposed up-grade of the 132kV line from Perth to Geraldton to 330kV.

ERM and a number of mining companies have indicated a preparedness to either contribute to, or consider providing all of the funds for, or even build and transfer to WPN a new 330kv transmission line from Perth to the Mid West. The companies are willing to consider that investment because there is no spare capacity on the existing line and WPN's proposed timetable for the up-grade does not meet the project construction requirements of a number of the potential iron ore developments.

In return for making that investment, the companies would expect to gain certainty of long term access to the newly created spare capacity. However, the current position seems to be that the companies would still need to line up in the "queue" behind others who have put in earlier access applications but who may not be prepared to contribute in a similar manner to the required transmission line investment.

Consideration should be given to a queuing policy which only applies to spare capacity, and in fact that seems to be the intention of the Access Code. If there is no spare capacity and potential users are willing to make an investment to develop new capacity ahead of WPN's planned schedule, then the private investors should be able to gain firm capacity rights for making that investment – otherwise there would be no incentive for them to make it.

As governments are increasingly faced with having to make decisions about competing investment needs from a limited capital pool, they are looking more and more to the private sector to assist in making those investments, particularly in large scale infrastructure, or in partnering publicly owned utilities through public private partnerships or similar vehicles. However, for the private sector to be willing to invest there must be a framework in place to enable a commercial outcome to be achieved and for those willing to make that investment to gain certain rights.

This is not to deny all potential users the right to access capacity in a fair way. It simply says that where there is no spare capacity and the network owner is not prepared to make the investment required to provide capacity in a timeframe required by the potential user, and that user is willing to

invest capital to bring that schedule forward, then the user should be given firm capacity rights ahead of others who are not willing to invest.

The other aspect of the queuing policy which needs addressing is the ability of applicants to frustrate the process by taking up places in the queue without having a "real" project. In a sense, these applicants can game the system by simply using a place in the queue to either frustrate a competitor or obtain a monetary value simply by putting in a network access application, even though that project may not be viable.

Transmission Line Easements

In the example of network connections from Perth to the Mid West, WPN currently has 132kV transmission lines occupying what is effectively the only easement available at least up to Eneabba. In this respect it appears to ERM to be sensible to consider the long term development of the area, say at least 30 years, when making investment decisions on upgrading the transmission network.

This is because the transmission line easements themselves are in effect natural monopolies, and though by-pass is theoretically possible, it is not possible practically. Therefore, governments should look to the long term needs of the region and State.

Such long term considerations may involve the government, from a state development perspective, contributing directly to such investments to enable larger transmission capacity than would otherwise be determined by WPN alone.

Alternatively, private sector investors may be willing to fund additional capacity beyond what is required in the short term, but in doing so, they should be able to use that capacity either for their own purpose, or for on-trading. Again, this relates to the issue of relinquishment of "unused" capacity – if a user has invested directly in providing spare capacity, then that user should have a right to access that capacity in proportion to the investment made.

Thank you for the opportunity to comment on these issues and your discussion paper. I would be pleased to discuss any of these issues further.

Yours sincerely

Richard Harris
WA Director