

NOTICE

Final Decision on Western Power's Revised Proposed Access Arrangement

The Economic Regulation Authority today issued its Final Decision on Western Power's revised proposed access arrangement for the South West Interconnected Network (SWIN).

The Authority's Final Decision is to not approve the revised proposed access arrangement.

The detailed reasons for this decision are set out in the Final Decision document, together with the amendments that the Authority requires before approving Western Power's access arrangement. This access arrangement, once approved, will apply until 30 June 2009.

Western Power submitted its proposed access arrangement to the Authority on 24 August 2005. On 21 March 2006, the Authority issued a Draft Decision to not approve the proposed access arrangement on the grounds that it did not satisfy the requirements of the *Electricity Networks Access Code 2004* (Access Code).

On 19 May 2006, Western Power submitted a revised proposed access arrangement, which is the subject of the Authority's Final Decision. The issuing of the Authority's Final Decision follows a period of extensive public consultation, including consultation undertaken as a result of amendments being made to the Access Code under which the revised proposed access arrangement is assessed.

Under section 4.19 of the Access Code, Western Power may submit an amended proposed access arrangement to the Authority within 20 business days of this Final Decision. The Authority is then required under section 4.21 of the Access Code to issue a Further Final Decision that either approves the amended access arrangement or does not approve the amended proposed access arrangement (in which case the Authority is required to draft and approve its own access arrangement).

BACKGROUND

The Authority is responsible for regulating third party access to regulated or 'covered' electricity networks in Western Australia under the framework of the Access Code.

At the commencement of the Access Code in November 2004, the only regulated network in Western Australia was Western Power's SWIN, which is located within the South West Interconnected System (SWIS).

The SWIS is the interconnected transmission and distribution system, which is located in the South West of the State and extends between Kalbarri, Albany and Kalgoorlie.

During the review of its revised proposed access arrangement, Western Power provided revised forecasts of an additional \$63.7 million of new facilities investment and \$23.7 million of non-capital costs between 2006/07 and 2008/09. The revised forecasts also included a proposal to amend the operation of the investment adjustment mechanism.

The Authority invited submissions from interested parties on Western Power's revised expenditure forecasts and its proposal to amend the operation of the investment adjustment mechanism. The Authority considered the five submissions received. The revised forecasts have been considered by the Authority in assessing the revised proposed access arrangement.

KEY ASPECTS OF THE FINAL DECISION

Capital Base

Under its proposed access arrangement, Western Power proposed a regulatory asset value (capital base) for the SWIN of \$2,932 million. This value incorporated some forecasts of new facilities investment for the 2005/06 year. After submitting the revised proposed access arrangement, Western Power further updated the value of the capital base to reflect actual new facilities investment up to 30 June 2006. This updated value was \$2,981 million.

The Authority is satisfied that this value meets the requirements of the Access Code.

Weighted Average Cost of Capital

Under its proposed access arrangement, Western Power proposed a rate of return (weighted average cost of capital or WACC) of 7.3 per cent (real pre-tax). This was revised to 6.76 per cent in its revised proposed access arrangement.

The Authority has determined that the revised WACC value of 6.76 per cent lies within a range of WACC values that may be reasonably estimated for Western Power's networks business and therefore meets the requirements of the Access Code.

Forecast Non-Capital Costs

In determining its target revenue under its proposed access arrangement, Western Power applied a forecast of non-capital costs of approximately \$734 million over the access arrangement period from 1 July 2006 to 30 June 2009. Western Power subsequently revised this forecast to \$827.2 million.

The Authority is satisfied the revised forecast meets the requirements of the Access Code to include only those costs that would be incurred by a service provider efficiently minimising costs.

Forecast New Facilities Investment

In determining its target revenue under its proposed access arrangement, Western Power forecast new facilities investment of approximately \$1,282 million over the access arrangement period, for which capital contributions would be made of approximately \$295 million. Western Power subsequently revised the forecast to \$1,585 million with \$399 million of capital contributions.

The Authority is satisfied that the revised forecast of capital expenditure is appropriately incorporated in the determination of target revenue by virtue of being reasonably expected to pass the new facilities investment test under section 6.52 of the Access Code or the test under section 6.56 of the Access Code.

Western Power has indicated to the Authority that it expects new facilities investment to exceed the forecasts applied in determining the target revenue for the first access arrangement period. If this is the case, the Authority is satisfied that an investment adjustment mechanism in the access arrangement will allow the target revenue for the second access arrangement period to be adjusted. Such adjustment of the target revenue

would arise if the amount, nature and timing of new facilities investment is different to that forecast for that period (where such investment meets either the New Facilities Investment test under section 6.52 or 6.56 of the Access Code).

Price control

Western Power has specified a revenue-cap form of price control in the revised proposed access arrangement. Under this form of price control, reference tariffs are set for 2006/07 on the basis of an amount of required revenue for the period, and in 2007/08 and 2008/09 on the basis of an amount of required revenue plus corrections for under or over recovery of required revenue for both years.

The Authority is satisfied that the revenue-cap price control proposed by Western Power is consistent with the requirements of the Access Code, with the exception of a provision to exclude certain costs and revenues from consideration in revenue requirements and the revenue cap. The Authority requires this provision to be removed.

Western Power is able to alter reference tariffs from year to year subject to meeting the constraint of the revenue cap and a "side-constraint" on tariff changes. Western Power has proposed a side constraint on year-to-year tariff changes of CPI + 5 per cent. This side constraint is greater than that initially proposed by Western Power (CPI + 2 per cent). The Authority is satisfied, however, that the less stringent side constraint is necessary to accommodate expected changes in tariffs for network services over the medium-term and is consistent with the requirements of the Access Code.

Price Lists

Taking into account the price lists proposed by Western Power to date, if Western Power submits an amended proposed access arrangement that is approved by the Authority the Authority envisages that the reference tariffs to be implemented under that access arrangement will result in increases in bundled transmission and distribution charges for small electricity customers that are in the order of 7 to 12 per cent over 2005/06 tariffs, depending upon the applicable reference service. This increase in transmission and distribution tariffs will not, however, affect retail electricity prices for these customers while retail electricity prices remain regulated under the *Energy Operators (Powers) Act 1979* and *Energy Operators (Electricity Retail Corporation) (Charges) By-laws 2006*.

Changes in transmission and distribution tariffs applicable to other than small electricity customers will depend upon the reference services applicable to these customers and the particular characteristics of the customers in terms of their electricity consumption.

Standard access contract and proposed policies

Western Power's revised proposed access arrangement includes a standard access contract for reference services, an applications and queuing policy, a capital contributions policy and a transfer and relocation policy.

Generally, these contracts and policies are based on a model standard access contract and model policies in the Access Code. However, the Authority has determined that there are some material additions, omissions and variations from these models that are inconsistent with requirements of the Access Code and that should be amended to ensure compliance with the Access Code.

Further information

The Final Decision is available on the Authority's [web site](#). Printed copies of the Final Decision are available on request at a cost of \$25.00 each.

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