Our ref : 6527853
Enquiries : Coan Harvey
Telephone : 08 9222 9259

Mr Robert Pullella
Executive Director Competition, Markets and
Electricity
Economic Regulation Authority
PO Box 8469
PERTH BC WA 6849

Dear Mr Pullella

CALL FOR SUBMISSIONS ON MATTERS RELATING TO WESTERN POWER'S REVISED PROPOSED ACCESS ARRANGEMENT

The Department of Treasury and Finance (DTF) is pleased to submit the following comments to assist the Economic Regulation Authority's (ERA's) examination of matters relating to the Network Access Arrangement proposed by Western Power (WP).

These comments focus on the issues of the treatment of capital contributions raised by the ERA and the proposal for a headworks charge proposed by the Office of Energy (OOE). The DTF understands the policy rationale for the changes and accepts that these could potentially help deliver more efficient investment in electricity network infrastructure. However, the DTF notes that there could be consequences of such changes for government's overall financial position, in particular the State's net debt to revenue ratio, which will need to be considered by government. At the end of the day these proposals have the potential to impact on the "shareholder" (whether private or public) which will need to be considered – shareholder capital, regardless of its source, is not free.

TREATMENT OF CAPITAL CONTRIBUTIONS

The ERA seeks views on an alternative treatment of capital contributions that spreads the deduction of capital contributions from the approved total revenue over an extended period, rather than adjusting the total contribution in the period in which the capital contribution is received. Such a treatment has some attraction from the perspective of setting regulated tariffs and avoiding price fluctuation caused by "lumpiness" in the receipt of revenue.

However, if this change in regulatory approach impacts on the way in which capital contributions are actually provided then this will impact on the current debt position of the network provider and its shareholder. This would depend on the manner in which capital contributions are paid to the service provider (eg "up front" versus time payments).

In the context of public ownership of the network provider any increase in government debt resulting from alternative arrangements would reduce capacity for delivery of public services.

HEADWORKS CHARGE

The OOE's proposal for a change in capital contribution policy stems from concerns that the current approach limits opportunities for network expansion by requiring a large capital contribution be made by a single, initial 'investment triggering' user. The new proposal submits that where network augmentations are triggered by one user, but would benefit future users in the region, a headworks charge would be levied across all the users to reflect the benefit of the investment received by each. This would in turn replace the single capital contribution currently charged to the triggering user.

The DTF is supportive of the introduction of a headworks charge and agrees with the benefits outlined by the OOE. Through the introduction of a regional average charge mechanism, capital contributions for the cost of augmentation can be spread on a more equitable basis across the infrastructure's present and future user base. This also preserves user pays principles by ensuring all users of the augmentation contribute to the cost.

However, there are two aspects to this proposed policy change that DTF wishes to highlight.

Firstly, the proposed headworks charge will impact the net debt to revenue ratio as a result of the network provider's need to cover the cost of the augmentation with a reduced start-up capital contribution. Even though the long term debt impact, assuming all expected head works charges are recovered, may be neutral the initial debt impact for the shareholder will need to considered in the context of the other demands for shareholder capital.

Secondly, the longer timeframe required in order for the network provider to regain its costs also creates uncertainty over the exact charges to be received in the future. This introduces a new "planning risk" for the network provider, and ultimately the shareholder, from "over-forecasting" new users. This could cause the network provider to bear all remaining uneconomic costs which will impact of its profit and long term viability. With the network provider under public ownership this is effectively transferring such planning risk to the tax payer. The ERA may wish to consider mechanisms that ensure that if "long term planning …vetted by the ERA in accordance with the Code" (as OOE propose) does not eventuate then lower than expected revenue from headworks charges can be recovered through higher system tariffs.

The ERA should also be aware that depending on the exact policy and model of implementation decided, there are potential impacts to net flows to Government through tax effects associated with these two proposals. Without further information on the model of implementation, however, it is difficult to gauge this impact.

I trust that these comments are of some assistance to the ERA in its deliberations.

Yours sincerely

David Smith
EXECUTIVE DIRECTOR
ECONOMIC

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