



## Extension Hill Pty Ltd

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Our Ref: 10-500-PO-LET-0004

Access Arrangements Review  
Electricity Access  
Economic Regulation Authority  
PO Box 8469  
Perth BC WA 6849

Dear Sir/Ms

### **Re; Draft Decision on Western Power's proposed Access Arrangement Provisions**

The central theme of our submission relates to the inadequate level of information provided by WPC in the development of significant connections at the transmission level. These projects are important to the state and involve much more expenditure than the connection cost.

The provision of services is characterised by a "take it or leave it, all care, no responsibility" basis and needs to be addressed.

Manifestation of the above shows in the lack of certainty WPC provides with respect to the supply of any service, either in the provision of costing and technical issues or in the final delivery time and cost of the connection. At all steps WPC accepts no risk for time or cost and leaves the customer to assume this risk with no influence over them.

There is a significant body of intellectual property on how large projects are developed from the first stages of screening to the final investment decision. WPC provision of services has to be structure to provide the appropriate level of service to suit the staged development of large projects.

WPC has commenced industry discussion on addressing the queuing system and we are hopeful that this will provide an opportunity to address these issues.

I apologise for the lateness of the submission but hope that you will consider our input.

Thank you for the opportunity to make this submission.

Yours sincerely,  
EXTENSION HILL PTY LTD

**MATT DUXBURY**

**Manager Infrastructure Service  
Extension Hill Pty Ltd  
Submission to the Economic Regulator of Western Australia**

on the

**Draft Decision on the proposed Revisions to Access Arrangement for  
the South West Interconnected Network**

**Introduction**

In our contact with Western Power Corporation (“WPC”), the organisation has generally not demonstrated the commercial acumen or customer focus expected of a contemporary enterprise. We believe it would better service the needs of large industrial clients such as Extension Hill Pty Ltd (“EHPL”) by demonstrating a better understanding of the commercial framework under which we operate and by demonstrating a more constructive, collaborative and cooperative approach to the provision of network access.

The central principle in this submission is that WPC should have greater accountability to its existing and potential customers on an ongoing basis for the commercial consequences of its performance when dealing with new customers’ connection processes. The twin forces of ERA oversight and constant commercial accountability from customers are more likely to act together to facilitate change than relying solely upon the relatively blunt tool of regulatory oversight alone.

This submission focuses on WPC’s,

- Customer Solutions Group’s services failing to meet generally acceptable project management standards or to provide detailed scopes, costs and schedules in their proposals, (The group can only be as good as the back room support, so this a whole of organisation issue),
- Unwillingness to effectively collaborate with large customers to optimize outcomes,
- Failure to properly resource and manage large project connections proposal services, and
- Failure to accept any risk or commercial sanctions for cost or schedule of asset creation projects to effect a new connection.

While we make some suggestions about processes and approaches to address these issues, they are simply options. There will be no doubt be other options which may address these issues more elegantly than those we have suggested.

**COSTING**

**Introduction to Issue**

In our experience, WPC generally displays monopolistic behaviour in its approach to the creation of connections assets,

The manifestation of this behaviour shows in inadequate provision of,

- Work scope,
- Cost breakdown information,
- Schedule,
- Reporting against schedule and scope, and
- Acceptance of any risk.

With this approach, the stage is set for the client to be forced to accept WPC’s poor performance in all respects. It must be said that performance is not all poor, but when it occurs there is no recourse or alternative.

The comments noted at paragraph 564 of the ERA’s draft decision on the Access Arrangements summarise the tenure of our submission very well in all respects and is consistent with our direct experience. Paragraph 564 is reproduced below for convenience of reference.

564. In considering the planning and procurement processes for new facilities investment, the Authority obtained advice from Geoff Brown & Associates.<sup>247</sup> This advice indicates that the planning and procurement processes applied during the first access arrangement period, and particularly early in this period, were deficient in a number of respects, including:

- poor processes of cost estimation, resulting in an absence of a sound basis for cost control in the execution of capital projects and programs;
- a possibility that specifications for products and services may differ from industry standards, resulting in a potential for less competition between suppliers and higher costs;
- over-specification of some assets;
- a low level of rigour in analysis of options for large capital projects;
- a lack of integration in planning for the transmission and distribution networks resulting in potential for inefficient investment, particularly in zone substation assets;
- poor processes of contract management with suppliers, resulting in potential for significant over-charging by suppliers; and
- inclusion of excessive contingency provisions in funding increases for projects, approved late in project implementation.

One example, typical of our experience of the above with WPC's overall approach was experienced as follows,

### Indicative Budget Estimate

Three Springs Land Acquisition for Terminal Switchyard

Customer Driven: Asia Iron- Extension Hill Mine Site

ITEM	COST
Land acquisition cost (ex GST)	\$75,000
Valuation	\$500
Stamp duty	\$1,500
Conveyancing	\$1,000
Administration costs	\$30,000
Legal costs	\$2,000
Landscaping - tree planting	\$20,000
Fencing	\$2,000
Access Gates	\$4,000
Overheads	\$17,880
Total excl. GST	\$153,880
GST	\$15,368
Total incl. GST	\$169,048

No explanation was given for the cost make up, either when we were first informed or when we asked for justification. By any objective assessment this is grossly inflated.

A further element of WPC's performance is its failure to commit to schedule in a meaningful way. Failure to meet schedule will cause most clients substantial costs. At this time WPC bears no responsibility or negative consequences for failure to meet schedule. This gives clients great cause for concern.

### Current Situation

It is our understanding the Customer Solutions Branch is being reorganized in an attempt to address this issue. However, simple reorganisation is unlikely to be a solution.

It can be accepted that WPC needs to recover the cost of providing connection services, but it needs to be accountable for the quality, cost and timeliness of such services. At the moment WPC essentially provides a “take it or leave it, all care, no responsibility” service. Basic service attributes of commitments to scope, deliverables, cost and schedule need to be provided and, in particular, a much greater level of commercial accountability has to be accepted.

At the moment WPC is undoubtedly receiving many requests for generation connections each year by parties looking to secure connections as part of the generation licence process run by the Independent Market Operator (IMO).

WPC appears to be having difficulties with securing or allowing for sufficient resources to provide timely and effective connection proposals and costing services.

Given that WPC charges the actual cost of providing connection proposals, it is difficult to see why it is unable to schedule resources to provide proposals to an acceptable detail on a timely basis.

### **A Way Forward**

The principle WPC could adopt for its connection services (Customer Solutions) is one of accountability - there has to be some consequence to WPC for failing to deliver on undertakings. WPC should provide more detailed, negotiated scopes of work; provide reliable cost estimates, clearly define deliverables and a commit to and report against budget and schedule. In the event there are indeterminate cost elements, they need to be identified and costed as best able with reference to experience and the available information. The item then can be excluded from the fixed cost element of the proposal and the basis of exceeding an agreed cost recorded in the proposal. If it arises it can then be managed in an open fashion.

The external equivalent situation for this service provided by WPC is the consultancy industry. A quick comparison of the service provide by WPC will reveal a service that falls well short of the services provided by any good consultancy. We recommend that WPC establish a consultancy type approach, maybe within an internal, standalone business unit. WPC can propose charge out rates and ERA can approve or amend them proportionally against similar, publically available consultancy rates. Further, the unit can engage external consultancies to augment its resources as required.

Under this approach WPC can develop a standard agreement for these services, again a mechanism easily regulated by ERA.

At the moment WPC advises that it does not have to provide connection services until a party has entered into an Interconnection Works Contract (IWC). So it positions itself to be helpful in providing a contract called an Early Undertakings Contract (EUC) to provide preliminary services. A review of the EUC will clearly demonstrate that WPC's approach to this service is monopolistic.

If the project development process set out in the Queuing and Stages of Development section below is reviewed, it is clearly evident that a significant amount of work is required before a project is well enough defined to enter into a construction contract. The IWC is a final commitment and so should be at the end of the development process. At this point WPC only has the EUC, with no ERA oversight, as its mechanism to provide these early services.

Further, the poorly developed nature of the project at the time the IWC is expected to be executed makes it difficult for WPC to commit to firm outcomes. As long as it does not have a process to determine the scope, cost, and schedule of the asset under an IWC, WPC will continue to argue for no risk whatsoever to WPC agreements.

The above proposition that the connection services group be restructured into an independent internal business unit within WPC and overseen by the ERA will go some way addressing these concerns. The group will have to hold its internal suppliers accountable for their inputs. At the moment there is no evidence that this happens.

## MAJOR CONNECTION CAPITAL

### Cost

The above sentiment flows through to clients for capital connection asset costs. It is again monopolistic and is characterised by, “take it or leave it”. WPC openly state that the client will pay whatever the cost is, regardless of the cost estimate. In our case we expect WPC to have to build in the order \$70m transmission works.

With the above culture we will not be happy with having a cost, such as this, being open ended and being unable to influence the outcome.

In the section below on the queuing policy, we set out the stages of development of a project and the level of certainty for a project increasing as it nears final commitment. At the very least WPC should work with clients to identify the risks in their connection assets project and agree to their allocation and management. For instance, we may prefer to spend money on geotechnical drilling, as opposed to assuming ground conditions risk in the construction contract. Contractors may accept such a risk, but will charge a healthy margin to mitigate the risk, which may or may not be needed.

Further, WPC’s latest demonstration of capital cost estimates in the North Country 330kV transmission line project leaves us without confidence that WPC can deliver a “value for money” extension.

From our own costings and review of WPC’s approach, there is again evidence of the monopoly behaviour. Design is conservative; engineering is internal and detailed and fails to accept external standard designs. An analogy of this approach is that if one specifies all the components of a car to produce the equivalent of a Holden or a Ford and then puts it together, it will be far more expensive, time consuming and risky than simply buying the standard product with a few modifications.

The consequences of these approaches are contrasted below,

<b>Design from scratch approach</b>	<b>Off the shelf Approach</b>
Significant design calculations	Mostly already done and proven
Specification of all items	Specify a few large items, maybe more performance based
Detailed procurement of many small items	Buy a few large items
Large number of one off detailed drawings to show how all the disparate parts go together	Receive pre-prepared standard drawings with a few specials
Increased installation costs as the parts have to be physically put together	Delivered to site prefabricated, reducing site construction and installation
Higher risk	Lower risk
The on site commissioning has to be very detailed	Reduced on site commissioning as elements are commission at the factory in controlled, standard settings.

There are many more contrasts that can be made, but the flavour of the two approaches is evident.

The issue is that clients needing connections are faced with WPC’s approach to asset creation with no alternative.

## Schedule

Schedule is a major concern to clients of WPC. WPC again openly states that it accepts no schedule risk, it is “all care and no responsibility”. At this time WPC suffers no sanction or loss, due to failure to meet schedule. The client wears all the risk to their project and has no influence over WPC’s work schedule. WPC should wear completion costs up to a percentage of connection project value. WPC can back to back this with their main contractor, which is standard construction contracting practice.

To put this in perspective, The Extension Hill Magnetite Project Stage 1 at full production will generate revenue in the order of \$75,000,000 per month. Given a significant portion of these costs are fixed, especially at start up, the loss to EHPL is significant for failure to receive grid connection on time. Anyone would feel exposed, knowing that they only have WPC’s good graces to rely upon!

## Asset Ownership

The position of WPC is demonstrated with its response to our written request to own our element of the WPC connection for the Extension Hill Magnetite Project, the 70km Eneabba to Three Springs 330kV transmission line. In this case there may or may not have been a second user of the asset. We are willing to own a significant portion of the line, with WPC gaining some equity due to the provision of an easement and the dismantling of an existing 132kV line and possibly the element to supply the other miner. The proposition was that WPC retain operating and maintenance control of the assets. The unequivocal response to our request from WPC’s executives, was no.

We believe that we should be given the option of owning our portion of these assets. The risk profile adopted by WPC results in EHPL taking ownership type risks with out the benefits of ownership. Clearly the trade off for EHPL ownership would be to assume its share of the ongoing operation and maintenance cost and the risks associated with ownership. Open access is a well proven commercial mechanism that should be available to users in the creation of significant transmission assets.

## Discussion

There are three issues here,

- Asset ownership,
- Asset creation, and
- Completion risk

The issue is again how to get some accountability into these elements of the asset creation for connection service WPC provides.

Firstly, we consider asset ownership. EHPL contends that the transmission line represents an asset that is amenable to partial ownership by EHPL. Given contractual agreement to allow WPC to retain operation and maintenance control of the assets, there can be no concern about EHPL’s ownership impacting other WPC clients. This is then a simple, commercial arrangement. WPC’s only driver for retaining ownership appears to be to increase its assets base and grow its business. EHPL contends that this is an unreasonable position to take and is largely monopolistic behaviour.

Secondly, EHPL intends to design, build and own its own 140km 330kV transmission line from Three Springs to the mine site. The evidence to date as discussed above in **Major Connection Capital** is that WPC’s ability to competitively price and deliver to a budget is questionable.

It is unlikely that a party, such as EHPL, would be able to build the shared asset for a lower cost as WPC is likely to demand significant, detailed technical say in the design and this is likely to negate any advantage we may have.

However, WPC should be required to itemise the cost build up and agree to a third party review of the price and project approach.

Further, WPC should be required to provide fixed price elements and clearly identify the variables of unknown elements that may increase the final cost.

Finally, turning to completion risk, WPC should be required to provide bank guarantees, along the lines of normal industry practice, for connection projects above a minimum value to the clients, such as to the value of 10% of the connection project value and provide costs for failure to meet project schedule up to a cap.

## **Summary**

### **Share Ownership of Connection Assets**

- WPC to develop a shared asset policy option for connection assets above a certain value.
- This can be monitored and approved by the ERA

### **Capital Cost of Connection Assets**

- WPC to provide detailed budget cost breakdowns, scope and schedule,
- At the client's sole discretion and cost, WPC's connection asset project may undergo due diligence review. WPC will be required to provide detailed information and take part in the process. ERA could attend as an observer.
- WPC to provide as much as possible fixed prices for its connection works and to explicitly identify the variable areas for exclusion, but provide the basis for the uncertainty.
- For large projects WPC should be required to run risk assessments with the client to enable the client to make informed decisions about the management of risk and to be assured that WPC is managing risks.

### **Completion risk**

- The new IWC should include provisions similar to normal supply contracts that provide financial sanctions on WPC for failure to meet schedule.

## **QUEUING AND STAGES OF DEVELOPMENT**

### **Introduction**

WPC's management of connection requests does not make distinction between

- the scale, large or small, and
- the staged and progressive development of the certainty of proceeding.

The scale of a project very often dictates the development time line and WPC needs to amend its policies and approach to recognize the characteristics of various project development processes and time lines. We will focus on large projects as that is where our experience lies.

It might be added here that it is highly probably that large projects require multiple connections, both very large (50MW plus) and large by normal connection standards, (1MW to 20MW). These have to be managed by the same WPC representative to ensure consistency.

Major projects usually have some or all of the following distinguishing features,

1. The full project investment is significant, \$100s of millions and possibly billions of dollars, in our case \$1.8 - \$2 billion,
2. The development process takes a long time and involves a number of investment decision points, leading to commitments to the next stage, prior to full financial commitment. The final feasibility study can cost many tens of millions of dollars,
3. The development process involves a number of environmental and regulatory approval steps before full financial commitment,
4. The energy consumption is sufficiently high to warrant connection at the Transmission level, in our case 100MW plus,

5. The load is potentially significant to the local transmission and generation supply and security,
6. The project is significant to the state economic and local social development, and
7. There are only a relatively small number of such projects in the pipeline at any time.

The comments in this section of our submission relate to our experience with a project that fills all of the above criteria and for which WPC's processes are ill matched.

Our experience is that WPC does not allocated sufficiently experienced or authoritative personnel to manage projects of this scale. All WPC's short comings discussed above apply here.

### **Queuing Policy**

The queuing policy becomes arbitrary when considering significant projects. The simple act of making an application for connection at an early time can secure an unreasonable advantage or unreasonably prejudice another project, regardless of the real status of the project. At the highest conceptual level, our State is best served by facilitating as much as possible those projects with the best prospect of proceeding. It is then sensible to look for some way to provide WPC with the tools to make objective determinations of competing projects' position in any queue.

By their nature large projects have long gestation times and a great deal of uncertainty as to weather they will proceed often persists until major environmental approvals are obtained and a financial commitment is made. Further, all off site major infrastructure needs to be addressed in the assessment; for instance if a rail line is needed it has its own project approval and development time line, or maybe significant water is needed and it may also have a significant approval and development timeline. The likelihood of a connection proceeding improves over a considerable time period, often up to several years.

Project development generally proceeds through a number of steps before financial commitment. Each step increases the knowledge of critical elements of the project until it can be assessed as "bankable". In our parlance, bankable means sufficient detail has been developed and collated to enable prudent owners and lenders to make full financial commitments to the project.

All projects go through the same process, but as projects get bigger the steps become more defined and detailed.

Each stage of development addresses some or all of the following elements, the detail and certainty increasing at each stage,

1. Narrowing down options to the preferred project configuration,
2. Developing budgets
3. Engineering and technical
  - a. Process and manufacturing systems
  - b. Technology selection
4. Identification and scoping of the major approvals, such as
  - a. Environmental approvals,
  - b. Community,
  - c. Native Title,
  - d. Heritage,
  - e. Land tenure,
5. Risk identification, mitigation and allocation
6. Construction and procurement
  - a. Contracting strategy
  - b. Critical items procurement strategy
7. Critical inputs
  - a. Water supply,
  - b. Energy; power, liquids, gas,
  - c. Labour resources
  - d. Logistics; roads, rail, ports, pipelines, power lines,



- e. Waste disposal
- 8. Determination of financing and commercial issues
  - a. Markets and off takers
  - b. Financing debt and equity
  - c. Revenue and operations costs
- 9. Operations
- 10. Initial development time line with the major milestones identified through to financial commitment.
- 11. Project implementation and construction schedule

The stages for project development are arbitrary, but can be roughly presented as follows,

Stage 1 – Scoping Study, i.e. screening options

Stage 2 – Pre-feasibility study,

Stage 3 – Feasibility Study, or Investment Decision Quality,

Stage 4 – Execution Phase or Definitive Estimate

WPC must be able to provide commensurate connection proposal options to suit the needs of each stage of development and time line. The level of cost accuracy needs to be stated and appropriate to the stage of development i.e. stage one may need multiple options costed at +/- 30% accuracy, while stage 3 may need one option costed at +/-10% and Stage 4 needs a fixed cost proposal.

Generally, a large project will have major supply agreements negotiated and ready to execute at the end of Stage 3, and the IWC is one of these.

In the above development process there are a few key mile stones that could be used as the basis to determine if the queue order should be changed,

- EPA approval though the State Ministerial Statement and if applicable Commonwealth EPBC Act approval,
- Environmental Management Plans required under the Ministerial Statement,
- Native Title agreements,
- Land and service corridor tenure,
- Off taker commitments, and
- Funding commitments, equity and debt.

EHPL suggests that one possible approach is that WPC establish a framework to use such elements to determine if a change in the queue is warranted. It may be that a project cannot be put in the queue until it has achieved a minimum set of criteria. Such evidence is readily provided by proponents and is evidence of progress of a project from an “entrepreneurial idea” to fact. At this point in time an “entrepreneurial idea” with little real prospect of getting up can clog up the queue to the detriment of more prospective projects. WPC cannot be put in the position of having to assess project prospectively in the absence of clearly defined and objective criteria. While still unlikely to please everyone, it does put some pressure on project proponents to advance their projects in a timely fashion.

Development of the criteria and the process will need project proponent input to assist WPC to develop a workable system.

We note that at the time of writing this WPC had commenced a process to review the queuing arrangements.

**Summary**

- WPC establish, in consultation with clients, a set of criteria to use to objectively determine the prospectively of a project proceeding.
- WPC implement a process to manage queue order change based on objective criteria.