
Response to the Draft Determination on the New Facilities Investment Test Application for a 132-66/11kV Medical Centre Zone Substation

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1 Background

On 19 November 2012, Western Power submitted an application to the Economic Regulation Authority (ERA) to determine if the forecast new facilities investment of \$27.21 million to construct a new 132-66/11 kV Medical Centre zone substation at the Queen Elizabeth II (QEII) Medical Centre in Nedlands is reasonably expected to meet the new facilities investment test (NFIT).

The NFIT requires Western Power to demonstrate that the proposed investment represents the most appropriate development option and that the project will be delivered efficiently.

Western Power submitted the application at the request of the Department of Health, which is funding a proportion of the investment.

On 22 April 2013, the ERA made a draft determination not to approve Western Power's application for \$27.21 million. The ERA considers only \$24.43 million is reasonably expected to meet the NFIT.

Although, the ERA considers that Western Power's proposed design and delivery of the project appear reasonable and efficient, they consider that:

- Costs of \$2.59 million in relation to risk allowances should be excluded, on the basis that it cannot be determined at this stage whether it is efficient expenditure. However, if actual costs exceed forecast costs, Western Power could re-submit its application. Alternatively, an "ex-post" review of all capital expenditure will be undertaken by the ERA at the end of the next access arrangement review. If this additional amount is proven to meet the NFIT, Western Power will be able to earn a return on the total investment.
- Costs of \$600,000 for a third transformer bund and switchroom should be excluded as they do not directly relate to the load increase requirements of the QEII Medical Centre.
- Costs of \$410,000 associated with customer requirements to bring forward the distribution shared works should be added to Western Power's costs. The ERA believes that the proposed investment addresses current risks to safety and reliability arising from poor asset condition and capacity issues in the area and will therefore meet the safety and reliability test as soon as the works are completed.

2 Western Power's response

Western Power accepts the ERA's draft determination that \$24.43 million meets the NFIT for the 132-66/11kV Medical Centre zone substation.

Western Power, however, notes the following:

Risk allowance

As part of its estimation process, Western Power includes an amount for forecast risk. The inclusion of risk in its NFIT costs for the Medical Centre is consistent with the previous NFIT determination for the Mid-West Energy Project (Southern Section).

However, Western Power accepts the ERA's determination that risk allowance of \$2.59 million should be excluded from the NFIT amount. Any costs incurred as a result of the identified risks materialising will be assessed for efficiency as part of Western Power's close-out documentation.

Western Power notes that the actual cost of the project may be assessed as part of an ex-post review as part of the access arrangement.

Costs associated with the third transformer

Western Power estimates project costs holistically. This means that works are combined where they can achieve economies of scale and scope, as with the Medical Centre project, the third transformer works were included as part of the total project cost. These costs are subsequently removed for purposes such as determining capital contributions.

In this case, while the costs associated with the third transformer itself were removed, the costs associated with the bund and switchroom were overlooked. As such, Western Power accepts that the \$600,000 should be excluded from the NFIT amount.

Bring forward costs

In the NFIT application, Western Power proposed that the \$410,000 associated with bringing forward the distribution works associated with the Medical Centre should be allocated to the QEII Medical Centre. This is because Western Power plans indicate that the project would not otherwise be undertaken until 2016.

In its draft determination, the ERA stated that the construction of the Medical Centre substation should be undertaken now rather than deferred and as such will meet the test for providing covered services.

Western Power accepts the ERA's decision to recover the \$410,000 of costs associated with bringing the project forward through tariffs rather than directly from the QEII Medical Centre. However, Western Power remains of the view that the proposed timing of 2016 is appropriate. This is because:

- **The requirements of the technical rules** – The existing Medical Centre and University substations will be compliant with the Technical Rules until 2016. If this project is completed before that time, the customers connected via Medical Centre and University substations will receive service performance above that required in the Technical Rules and therefore provided to other customers on the network. Furthermore, if the costs of bringing forward this work are considered to meet NFIT, the cost of the increased service performance will be recovered from the broader customer base rather than the QEII customer.
- **Prioritisation of the capital works program** – Western Power has considered the risks associated with the existing Medical Centre substation and requirements of the QEII Medical Centre in the context of its entire capital works program. Western

Power understands that assessment as part of the NFIT application process only allows the ERA to consider the costs and benefits of the project in isolation.

- **Management of existing assets** – The ERA notes that the probability of the failure of assets in the existing Medical Centre and University substations is significant and therefore the project should be undertaken now rather than deferred. Western Power supports its engineering judgement that the life of these assets can be extended through prudent management.