

Decision on the Maximum Reserve  
Capacity price proposed by the  
Independent Market Operator for the  
2017/18 Reserve Capacity Year

30 January 2015

Economic Regulation Authority

WESTERN AUSTRALIA

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Economic Regulation Authority  
Perth, Western Australia  
Phone: (08) 6557 7900

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## Contents

<b>DECISION</b>	<b>1</b>
<b>REASONS</b>	<b>1</b>
Background	1
MRCP Market Procedure	2
Summary of input parameters and calculated values	2
1.1 Power station costs (PC)	4
1.2 Factor for legal, insurance, approvals, other costs and contingencies (margin M)	5
1.3 Transmission connection works (TC)	6
1.4 Fixed fuel costs (FFC)	7
1.5 Land costs (LC)	8
1.6 Fixed operating and maintenance costs (Annualised fixed O&M)	9
1.7 Weighted average cost of capital (WACC)	10
Public consultation process	11
<b>CONCLUSION</b>	<b>12</b>

## DECISION

1. On 16 December 2014, the Independent Market Operator (**IMO**) provided the Economic Regulation Authority (**Authority**) with its final report on the Maximum Reserve Capacity Price (**MRCP**) for the 2017/18 Capacity Year.<sup>1</sup> The Authority approves the revised value for the MRCP for the 2017/18 Capacity Year of \$164,800 per MW, as proposed in the IMO's Final Report.
2. This approval is granted pursuant to clause 2.26.1 of the *Wholesale Electricity Market Rules* (**Market Rules**). The approval is granted on the basis that:
  - the revised value for the MRCP proposed by the IMO reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules; and
  - the IMO has carried out an adequate public consultation process.

## REASONS

### Background

3. Clause 4.16.3 of the Market Rules requires the IMO to develop a Market Procedure documenting the methodology it uses and the process it follows in determining the MRCP (MRCP Market Procedure).<sup>2</sup> The IMO must follow the MRCP Market Procedure to review the MRCP for each Reserve Capacity Cycle. The IMO must propose a revised MRCP using the methodology described in the MRCP Market Procedure, and prepare a Draft Report describing how it has arrived at the proposed revised MRCP. Following a public consultation process, the IMO must propose a final MRCP to the Authority for approval.
4. Clause 2.26.1 of the Market Rules requires the Authority:
  - to review the report provided by the IMO, including all submissions received by the IMO in preparation of the report;
  - to make a decision as to whether or not to approve the revised value of the MRCP;
  - in making its decision, to only consider:
    - whether the proposed revised value for the MRCP reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules;
    - whether the IMO has carried out an adequate public consultation process; and
  - notify the IMO as to whether or not it has approved the revised value.

<sup>1</sup> See IMO website, Maximum Reserve Capacity Price web page, <http://www.imowa.com.au/mrcp>

<sup>2</sup> See IMO website, *Market Procedure: Maximum Reserve Capacity Price*, [http://www.imowa.com.au/docs/default-source/rules/imo-wem-procedures-and-other-documents/pc\\_2012\\_\\_08\\_final\\_amended\\_market\\_procedure\\_\\_clean\\_.pdf?sfvrsn=2](http://www.imowa.com.au/docs/default-source/rules/imo-wem-procedures-and-other-documents/pc_2012__08_final_amended_market_procedure__clean_.pdf?sfvrsn=2)

5. Clause 2.26.2 of the Market Rules provides that, where the Authority rejects a revised MRCP submitted by the IMO, it must give reasons and may direct the IMO to carry out all or part of the review process under clause 4.16 again, in accordance with any directions or recommendations of the Authority.

## MRCP Market Procedure

6. The MRCP Market Procedure sets out the principles to be applied and the steps to be taken by the IMO in order to develop and propose the MRCP.
7. The methodology for determining the MRCP, as specified in the Market Procedure, includes a technical costing of the following components:
- capital cost of an industry standard, liquid-fuelled open cycle gas turbine (**OCGT**), with a nominal nameplate capacity of 160 MW and an inlet cooling system, located within the South West Interconnected System (**SWIS**);
  - land cost associated with developing and constructing the power station;
  - costs associated with the development of liquid fuel storage and handling facilities;
  - costs associated with the connection of the power station to the bulk transmission system;
  - fixed operating and maintenance (**O&M**) costs for the power station, fuel handling facilities and the transmission connection components;
  - margin for legal, insurance, financing and environmental approval costs plus contingencies; and
  - Weighted Average Cost of Capital (**WACC**).
8. The calculation of the 2015 MRCP is based on a theoretical power station that would begin operating on 1 October 2017. In accordance with the MRCP Market Procedure, capital costs are escalated to 1 April 2017 and fixed O&M costs are escalated to 1 October 2017.

## Summary of input parameters and calculated values

9. The MRCP Market Procedure states that the IMO must use the following formulae to determine the MRCP.

$$\text{MRCP} = (\text{ANNUALISED\_FIXED\_O\&M}^3 + \text{ANNUALISED\_CAP\_COST}^4 / \text{CC}^5)$$

10. The value of CAP\_COST must be calculated as:

<sup>3</sup> Annualised fixed O&M cost is the annualised fixed operating and maintenance cost for a typical OCGT power station and any associated electricity transmission facilities determined in step 2.5 of the MRCP Market Procedure and expressed in Australian dollars, per MW per year.

<sup>4</sup> Capcost is the total capital cost estimated for an OCGT power station. Annualised capcost is the total capital cost, expressed in Australian dollars, annualised over a 15 year period, using a Weighted Average Cost of Capital (WACC), as determined in step 2.9 of the MRCP Market Procedure.

<sup>5</sup> CC is the expected Capacity Credit allocation determined in conjunction with power station costs in step 2.3.1(c) of the MRCP Market Procedure.

$$\text{CAP\_COST} = ((\text{PC}^6 \times (1+\text{M}^7) + \text{TC}^8) \times \text{CC} + \text{FFC}^9 + \text{LC}^{10}) \times (1 + \text{WACC}^{11})^{1/2}$$

11. A summary of the input parameters to the MRCP and their calculated values for the 2017/18 Reserve Capacity Year in the IMO's final report compared with the approved values for 2016/17 is provided in the table below.

	Proposed value 2017/18	Approved value 2016/17	Units	Market Procedure definition
Power station expected Capacity Credit allocation	150.5	150.5	MW	CC
Weighted Average Cost of Capital	5.81	7.01	%	WACC
Power station costs	865,835.57	878,792.83	\$/MW	PC
Factor for legal, financing, approvals, contingencies and other costs	19.97	20.10	%	M
Transmission connection works	161,194.00	141,910.00	\$/MW	TC
Fixed fuel costs	7,282,059.84	7,206,385.63	\$	FFC
Land costs	2,751,636.61	2,733,933.12	\$	LC
Total capital cost	196,083,111.85	196,690,722.71	\$	CAP_COST
<b>Annualised capital cost</b>	<b>19,938,595.51</b>	<b>21,607,991.70</b>	<b>\$/year</b>	<b>ANNUALISED_CAP_COST</b>
<b>Annualised fixed O&amp;M cost</b>	<b>32,307.02</b>	<b>33,238.01</b>	<b>\$/MW/year</b>	<b>ANNUALISED_FIXED_O&amp;M</b>
<b>MRCP (rounded)</b>	<b>164,800.00</b>	<b>176,800.00</b>	<b>\$/MW/year</b>	<b>MRCP</b>

The most significant changes since last year's review are as below.

- The WACC has decreased from 7.01% to 5.81% in this year's review, which has accounted for the majority of the decrease in the MRCP. This was predominantly driven by reductions in the debt risk premium (**DRP**) and the risk free rate.

<sup>6</sup> PC is the capital cost of an OCGT power station, expressed in Australian dollars per MW, as determined in step 2.3 of the MRCP Market Procedure for that location.

<sup>7</sup> M is a margin to cover legal, approval, financing and other costs and contingencies as detailed in step 2.8 of the MRCP Market Procedure.

<sup>8</sup> TC is the estimate of Total Transmission Costs as determined in step 2.4 of the MRCP Market Procedure.

<sup>9</sup> FFC is the Fixed Fuel Cost as determined in step 2.6 of the MRCP Market Procedure.

<sup>10</sup> LC is the Land Cost as determined in step 2.7 of the MRCP Market Procedure.

<sup>11</sup> WACC is the Weighted Average Cost of Capital as determined in step 2.9 of the MRCP Market Procedure.

- The increase in the power station cost is driven by a lower exchange rate between the Australian Dollar relative to the Euro.
  - The Transmission connection cost has increased by 13.6% since last year. The reasons for this are discussed in section 1.3 below.
  - Estimation of lower escalation factors over the period of cost escalation. In particular, lower escalation factors for power station capital costs, driven by lower commodity price forecasts, have contributed to a decrease in the MRCP.
12. The Authority has reviewed the IMO's Draft Report, the IMO's Final Report, the IMO's MRCP calculation spreadsheet and public submissions received by the IMO in response to its Draft Report. The Authority has also reviewed reports commissioned by the IMO in regard to input parameters for the MRCP, in order to assess that these reports reasonably reflect the application of the method and guiding principles described in clause 4.16 of the Market Rules.
  13. The Authority is satisfied that the IMO has calculated the MRCP according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.
  14. In particular, the Authority notes that the IMO has calculated the MRCP using the formula set out in section 2.10.1 of the MRCP Market Procedure.

## 1.1 Power station costs (PC)

15. Section 2.1.1 of the MRCP Market Procedure states that the power station upon which the MRCP is based must:
  - be representative of an industry standard liquid-fuelled OCGT power station;
  - have a nominal nameplate capacity of 160 MW prior to the addition of any inlet cooling system;
  - operate on distillate as its fuel source;
  - have a capacity factor of 2%;
  - include low Nitrous Oxide (NOx) burners or associated technologies, as would be required to demonstrate good practice in power station development;
  - include an inlet air cooling system and water receiveal and storage facilities to allow 14 hours of continuous operation, where in the opinion of the IMO this would be cost effective; and
  - include the minimum level of equipment or systems required to satisfy the Balancing Facility Requirements.
16. The MRCP Market Procedure states that the IMO must engage a consultant to provide:
  - an estimate of the costs associated with engineering, procurement and construction of the power station as at April in Year 3 of the Reserve Capacity Cycle;
  - a summary of any escalation factors used in the determination; and

- likely output at 41 degrees Celsius which will take into account available turbine and inlet cooling technology, likely humidity conditions and any other relevant factors, which represents the expected Capacity Credit allocation of the power station.
17. The IMO commissioned Jacobs to provide estimates of generation plant capital costs for a 160 MW OCGT power station located within the SWIS. Based on Jacobs' capital cost estimate, escalated forward to 1 April 2017 dollars as required by the MRCP Market Procedure, the IMO has proposed a value of \$865,835.57 per MW for the capital cost of an OCGT.
  18. Jacobs used the same methodology to calculate the power station capital costs as last year. In its report, Jacobs notes that there is now only one gas turbine make/model in production that is rated in close proximity to the 160MW nominal nameplate capacity required by the MRCP Market Procedure.<sup>12</sup> As the nameplate capacity of this machine is 173 MW, Jacobs has scaled the capital cost and expected Capacity Credit allocation to better represent a nominal 160 MW generator.
  19. The Authority notes that Jacobs has identified the components of the capital costs that are likely to be scalable with generator size and those components that are likely to be fixed, and has only adjusted the scalable costs in estimating the capital cost for a nominal 160 MW power station.
  20. Given that the MRCP Market Procedure requires that the capital cost of the notional power station be based on a 160 MW industry standard liquid-fuelled OCGT power station with inlet cooling, located within the SWIS, the Authority considers the scaling approach by Jacobs to be a reasonable application of the MRCP Market Procedure.
  21. The Authority is satisfied that the IMO has calculated the capital cost of an OCGT according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.

## 1.2 Factor for legal, insurance, approvals, other costs and contingencies (margin M)

22. Step 2.8 of the MRCP Market Procedure states that the IMO must engage a consultant to determine the value of margin M, which shall constitute the following costs associated with the development of the power station project:
  - a) legal costs associated with the design and construction of the power station.
  - b) financing costs associated with equity raising.
  - c) insurance costs associated with the project development phase.
  - d) approval costs including environmental consultancies and approvals, and local, state and federal licensing, planning and approval costs.
- a) other costs reasonably incurred in the design and management of the power

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<sup>12</sup> The Siemens SGT5-2000E power station.

station construction; and

- b) contingency costs.
23. The IMO commissioned Jacobs to provide an estimate of the above costs. Jacobs estimated these costs associated with recent comparable developments, excluding any abnormal costs that may be particular to certain projects. Jacobs has scaled the costs for a 160 MW power station where relevant. Jacobs proposed a margin of 19.97 per cent, which is added as a fixed percentage of the capital cost of developing the power station.
24. The Authority is satisfied that the IMO has calculated the margin for M according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.

### 1.3 Transmission connection works (TC)

25. Step 2.4 of the MRCP Market Procedure states that Western Power must provide an estimate of the total transmission costs, in accordance with the methodology in the Market Procedure to connect the generator and deliver the output to loads, consistent with the relevant planning criteria in the Technical Rules.<sup>13</sup>
26. The estimated total transmission costs must be derived from capital contributions either paid historically or expected to be paid to Western Power under Access Offers<sup>14</sup> and Western Power's Contribution Policy as approved by the Authority only for generators that are capable of being gas or liquid fuelled.<sup>15</sup>
27. According to the MRCP Market Procedure, the transmission connection cost is calculated by using actual connection costs for projects completed within a five-year window, and weights each connection cost according to the year that the facility commenced, or is expected to commence, operation.
28. For any year for which no actual project data is available, Western Power is required to estimate the shallow connection cost consistent with the MRCP Market Procedure.<sup>16</sup> Shallow connection cost refers to the cost that new generators have to pay that solely covers the direct infrastructure costs to connect their plant to the existing transmission system.
29. The Authority understands from the IMO that in this year's review, actual project data was only available for one year within the five-year window in which transmission connection costs calculations are based on. Therefore, the transmission connection costs for the other four years within the five-year window are based on shallow connection cost estimates. Western Power notes that the estimated shallow connection cost is higher than the actual capital contributions for facilities within the

<sup>13</sup> See Western Power website, *Technical Rules web page*, [http://www.westernpower.com.au/aboutus/accessArrangement/Technical\\_Rules.html](http://www.westernpower.com.au/aboutus/accessArrangement/Technical_Rules.html)

<sup>14</sup> Access Offers are made in accordance with the *Electricity Networks Access Code 2004* and Western Power's Capital Contribution Policy.

<sup>15</sup> Facilities excluded from the Access Offers calculation are stipulated in section 2.4.1 of the Market Procedure.

<sup>16</sup> Shallow connection cost refers to the cost that new generators have to pay that solely covers the direct infrastructure costs to connect their plant to the existing transmission system.

current five-year window which has led to an increase of 13.6% in total transmission connection costs compared to last year.<sup>17</sup>

30. In accordance with the requirement of the MRCP Market Procedure, Western Power has calculated the transmission connection cost estimate as part of its obligations under the MRCP Market Procedure, and has provided an audit report to the IMO verifying the data used in its calculation. Based on this, the IMO has proposed a value of \$161,194 per MW for transmission connection costs.
31. The Authority is satisfied that the IMO has calculated transmission connected costs according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.
32. The Authority notes that, prior to the 2012 Reserve Capacity Cycle, transmission costs were based on a high level indicative estimate of future costs. As a result of the IMO's five-yearly review of the MRCP Market Procedure, from the 2012 Reserve Capacity Cycle onwards a modified approach to calculating total transmission costs was adopted whereby the cost estimate is based on actual connection costs. This change was adopted because it was considered the previous approach could lead to inaccuracies and year-to-year volatility. The Authority notes that the current MRCP Market Procedure requires shallow connection costs to be estimated by Western Power in instances where no actual project data is available, which may also lead to inaccuracies in the calculation of total transmission connection costs for the determination of the MRCP. The Authority recommends that the IMO review the methodology in calculating transmission connection costs in the next five-yearly review of the MRCP Market Procedure.

## 1.4 Fixed fuel costs (FFC)

33. Step 2.6 of the MRCP Market Procedure states that the IMO must engage a consultant to determine an estimate of the costs for the liquid fuel storage and handling facilities of the power station. The costs should be those associated with a fuel tank of 1,000 tonne capacity, including foundations and spillage bund; facilities to receive fuel from road tankers; and all associated pipework, pumping and control equipment. The IMO commissioned Jacobs to estimate the fixed fuel costs.
34. Based on Jacobs' estimates, escalated to 1 April 2017 as required by the MRCP Market Procedure, the IMO has proposed a value of \$7.282 million for fixed fuel costs. This is slightly higher than the 2014 value of \$7.206 million, which is largely as a result of an increase in the cost of installing storage tanks.
35. The Authority is satisfied that the IMO has calculated fixed fuel costs according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.

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<sup>17</sup> In last year's review, Western Power reported no actual project data for the Latest Offer Year and its estimated shallow connection charge was included in the five-year weighted average calculation.

## 1.5 Land costs (LC)

36. The MRCP Market Procedure states that the IMO must retain Landgate under a consultancy agreement to provide valuations on parcels of industrial land. The regions in which the analysis is required to be conducted includes:
- a) Collie Region
  - b) Kemerton Industrial Park Region
  - c) Pinjar Region
  - d) Kwinana Region
  - e) North Country Region; and
  - f) Kalgoorlie Region
37. These areas represent the regions within the SWIS where generation projects are most likely to be proposed and should provide a broad cross-section of options. The IMO may include additional locations if it considers appropriate.
38. The MRCP Market Procedure states that the IMO will provide an indication as to the size of land required, which should be limited to:
- a three hectare parcel of land in an industrial area of a standard size, with consideration given to any requirements for a buffer zone in that specific location (where the minimum land size is greater than three hectares, the minimum available land size shall be used); and
  - the summation of multiple smaller parcels of land, as appropriate to meet these requirements.
39. The Authority notes that three hectare sites were used for all locations except Kemerton, for which the smallest available lot is five hectares. This approach is identical to that used in previous MRCP reviews. The Authority also notes that Landgate has provided its estimate of the cost of each land parcel as at 30 June 2014 excluding transfer duty, and that the IMO has added the applicable transfer duty to each land parcel cost, as in the last three MRCP reviews. The Authority recognises that the inclusion of the transfer duty is not explicitly specified in the MRCP Market Procedure but considers that it is appropriate to include the transfer duty as part of the land costs calculation, as has been the case in previous years.
40. Pursuant to the MRCP Market Procedure, the IMO has calculated the mean of the seven valuations, and has escalated the land cost to 1 April 2017 as required in the MRCP Market Procedure. The IMO has proposed a value of \$2.752 million for land costs. This price represents an increase of 1 per cent from the corresponding value for the 2014 MRCP, which is due to an increase in land prices for the Collie, Geraldton and Eneabba regions.
41. The Authority is satisfied that the IMO has calculated land costs according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.

## 1.6 Fixed operating and maintenance costs (Annualised fixed O&M)

42. The IMO must determine fixed O&M costs for the power station and the associated transmission connection works. Fixed O&M costs must also include:
  - fixed network access and/or ongoing charges, which are to be provided by Western Power; and
  - an estimate of annual insurance costs as at 1 October in Year 3 of the relevant Reserve Capacity Cycle, in respect of power station asset replacement, business interruption and public and products liability insurance, as required under network access arrangements with Western Power.
43. The IMO must determine the annualised fixed O&M costs in accordance with step 2.5 of the MRCP Market Procedure. The IMO may engage a consultant to assist in this process.
44. The IMO commissioned Jacobs to provide an estimate of fixed O&M costs for the power station and the associated transmission connection works.
45. The IMO has calculated the power station fixed O&M costs based on the annual generation fixed O&M costs determined by Jacobs which was converted to a present value using the WACC. This is escalated to 1 October 2017, providing an annualised value of \$16,106.60 per MW per year. The fixed O&M costs for transmission connection works include the switchyard and the transmission line O&M costs. The IMO has converted the annual transmission connection works O&M costs (determined by Jacobs) to a present value using the WACC. This is escalated to 1 October 2017, providing an annualised value of \$479.33 per MW per year.
46. The fixed network access charge is based on the relevant charge from Western Power's Price List. These charges are escalated to 1 October 2017 using the Consumer Price Index in accordance with the MRCP Market Procedure, providing an annualised value of \$11,997.91 per MW per year.
47. The IMO sought updated advice on insurance costs from an independent insurance broker. The insurance cost in the fixed O&M costs is escalated to 1 October 2017, providing an annualised value of \$4,736.74 per MW per year, compared with the 2014 value of \$5,804.67 per MW per year.
48. The Authority notes insurance costs have decreased by 22.5 per cent compared to last year. It is stated in the IMO's final report that this is a result of decreased insurance premiums for business interruption and asset replacement insurance, and also for public and products liability insurance. Insurance premiums decreased this year as a result of increased competition and lower risk, and fewer claims related to natural disasters. The IMO obtained this information from a quote received from an independent insurance broker.
49. Based on the cost estimates discussed above, the IMO has proposed a value for the total annualised fixed O&M costs of \$32,307 per MW per year.
50. The Authority is satisfied that the IMO has calculated fixed operating and maintenance costs according to a methodology that reasonably reflects the

application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.

## 1.7 Weighted average cost of capital (WACC)

51. Step 2.9 of the MRCP Market Procedure states that the IMO must determine the cost of capital to be applied to various cost components of the MRCP. The MRCP Market Procedure sets out the parameters and a formula for calculating the WACC in real pre-tax terms. The WACC parameters are classified into two categories in the MRCP Market Procedure, i.e., the annual components and the five-yearly components.
52. The MRCP Market Procedure states that in determining the WACC, the IMO must review and determine values for the annual components. It may also review and determine values for the five-yearly components that differ from those in step 2.9.8 of the procedure if, in the IMO's opinion, a significant economic event has occurred since undertaking the last five-yearly review of the MRCP, in accordance with clause 4.16.9 of the Market Rules.
53. The IMO commissioned PricewaterhouseCoopers (**PwC**) to calculate the DRP and calculated the remaining WACC components from publicly available information.
54. The IMO has calculated the WACC according to the pre-tax real Officer WACC formulation, with bond yields considered in both the costs of equity and debt. The nominal risk free rate is determined from observed yields of Commonwealth Government bonds, while the DRP is derived from observed yields of corporate bonds.
55. The MRCP Market Procedure provides that, in determining the WACC, the IMO must determine the methodology to estimate the DRP which, in the opinion of the IMO, is consistent with current Australian accepted regulatory practice. For the 2015 MRCP, the IMO calculated the DRP using the bond-yield approach developed by the Authority, which is consistent with the 2014 MRCP. This approach uses a sample of bonds issued in Australian dollars by Australian entities to estimate a DRP. The average remaining term to maturity (tenor) of past samples of bonds used to estimate the DRP has had a tendency to be around five years. The implication of this is that the DRP estimate reflects a term to maturity of around five years. The Authority notes that this methodology was appealed to the Australian Competition Tribunal and was upheld in June 2012.
56. Alinta Energy made a submission in response to the IMO's draft report on the issue of the bond sample average term to maturity. It made reference to PwC's advice to the IMO on the appropriate DRP, which highlights that the use of a DRP based on a sample of bonds with an average term to maturity of less than ten years is likely to underestimate the DRP.
57. The Authority notes it has recently adopted a modified bond yield approach to calculate the DRP in its Draft Decision on Proposed Revisions to the Access Arrangement for the Mid-West and South-West Gas Distribution System in October 2014.<sup>18</sup> This modified methodology uses a larger sample of bonds where the country associated risks primarily stem from Australia and allows for the inclusion of bonds

<sup>18</sup> Economic Regulation Authority, 'Draft Decision on Proposed Revisions to the Access Arrangement for the Mid-West and South-West Gas Distribution System', 14 October 2014, p.189, <http://www.erawa.com.au/cproot/12938/2/20141014%20D129552%20%20GDS%20-%20ATCO%20-%20AA4%20-%20Draft%20Decision%20-%20PUBLIC.pdf> (accessed 9 January 2015)

issued in local and foreign currencies. The larger sample has allowed the Authority to estimate a 'yield curve' across a range of tenors (as opposed to single DRP point estimate) so that a ten-year DRP can be estimated. The Authority is of the view that the modified approach overcomes the issue of the sample of bonds producing a DRP with an implied term to maturity of less than ten years.

58. However, the Authority acknowledges its Decision on Proposed Revisions to the Access Arrangement for the Mid-West and South-West Gas Distribution System in which the modified bond yield approach was used is still currently in draft form. For this reason, the Authority considers it reasonable for the IMO to continue to determine that previous methodology as representing current accepted Australian regulatory practice.
59. The Authority has also examined the other annual WACC components determined by the IMO. It notes an inconsistency in the IMO's calculations, whereby data used to derive the Risk Free Rate was based on a different date range than the period used to derive the Debt Risk Premium. The Authority has recalculated the WACC using consistent dates for both the Risk Free Rate and the Debt Risk Premium and notes the impact on the total MRCP is less than 0.5%. The Authority considers that the IMO has calculated the annual WACC components in line with the MRCP Market Procedure; however, best regulatory practice would be to calculate all annual WACC parameters using consistent date ranges. The Authority recommends that the IMO review this element of methodology in the next five-yearly review of the MRCP Market Procedure.
60. On balance, the Authority is satisfied that the IMO has calculated the real pre-tax WACC according to a methodology that reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure.

## Public consultation process

61. The IMO published a Draft Report in November 2014, which described how the IMO arrived at the proposed revised value for the MRCP and called for submissions by 5 December 2014. Rule Participants and other industry stakeholders were advised by the IMO that the Draft Report had been published. Announcements were also published in the Australian Financial Review newspaper and the West Australian newspaper. The Draft Report and supporting documents, including reports from Jacobs, PwC, Landgate and Western Power were published on the IMO's website.<sup>19</sup>
62. The IMO received two submissions through the public consultation process on the Draft Report from Alinta Energy and Community Electricity.
63. The IMO has summarised the comments it received from stakeholders and its responses to the comments in section 5 of the IMO's Final Report.
64. The Authority is satisfied with the public consultation process undertaken by the IMO. In the context of the application of the method and guiding principles described in clause 4.16 of the Market Rules and the MRCP Market Procedure, the Authority is of the opinion that the IMO has appropriately addressed the comments raised by stakeholders.

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<sup>19</sup> IMO website, *MRCP web page*, <http://www.imowa.com.au/mrcp>

## CONCLUSION

65. The Authority is satisfied that the IMO has met the requirements of the Market Rules in proposing the MRCP for the 2017/18 Reserve Capacity Year for the following reasons:
- the Authority is satisfied that the proposed revised value of the MRCP reasonably reflects the application of the method and guiding principles described in clause 4.16 of the Market Rules; and
  - the Authority is satisfied that the IMO has carried out an adequate public consultation process.
66. Based on the above assessment, the Authority approves the proposed revised value for the MRCP for the 2015 Reserve Capacity Cycle of \$164,800 per MW per year, effective from 1 October 2017 for the 2017/18 Reserve Capacity Year.