



11 December 2017

Ms Nicola Cusworth
Chair
Economic Regulation Authority
Level 4, Albert Facey House
469 Wellington Street
PERTH WA 6000

Dear Ms Cusworth

RE: Issues Paper on proposed revisions to the Western Power network access arrangement

Thank you for the opportunity to comment on the Issues Paper published by the Economic Regulation Authority in relation to proposed revisions to the Western Power network access arrangement covering the period from 1 July 2017 to 30 June 2022.

ATCO Australia recognises the importance of all 25 specific issues raised in the Economic Regulation Authority's Issues Paper, but has sought to address only those where we consider our experience and views are most relevant.

As a consequence, ATCO Australia's submission focuses on selected specific issues within two of the four areas of primary interest to the Economic Regulation Authority:

- investment in the network; and
- network charges and metering.

ATCO Australia also takes the opportunity to emphasise the importance of engaging with customers and stakeholders in developing regulatory proposals. This engagement is key contributor to developing access arrangement proposals that balance customer expectations with efficiency and other regulatory objectives.

Background

ATCO Australia is a customer focussed company that develops, builds, owns and operates a range of energy infrastructure assets, supporting residential, business and commercial consumers across Australia. The Australian business includes:

- ATCO Gas Australia, which owns and maintains the largest gas distribution network in Western Australia, connecting over 750,000 customers through more than 14,000 km of natural gas pipelines and associated infrastructure. ATCO Gas Australia is subject to economic regulation by the Economic Regulation Authority under the National Gas Law (NGL) and National Gas Rules (NGR) as applied in Western Australia;

ATCO Australia Services Pty Ltd

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- ATCO Power Australia, which owns and operates two power generation facilities in Australia (a joint-owned facility in Adelaide and a wholly-owned facility in Karratha) with a combined capacity of 266 MW; and
- ATCO Structures and Logistics, which has been operating in the Australian marketplace since 1961. Today, ATCO Structures & Logistics has two manufacturing facilities and eight offices across the country delivering modular solutions to a diverse group of customers.

The ATCO Australia Group is part of the worldwide ATCO Group of companies with approximately 7,000 employees and assets of \$21 billion. ATCO is engaged in pipelines and liquids (natural gas transmission, distribution and infrastructure development, energy storage, and industrial water solutions); electricity (electricity generation, transmission, and distribution); retail energy; and structures and logistics.

Issues paper

Drawing on ATCO Australia's experience in Western Australia, the National Electricity Market, and other deregulated gas and electricity markets, ATCO Australia makes the following observations:

- The rapid pace of technological change in the energy industry gives energy network businesses like Western Power the ability to improve the efficiency of their investment program by pursuing, on a default basis, non-network investment solutions, or alternative technologies, in a variety of network locations rather than just doing so for regional locations where traditional infrastructure options are difficult to justify on efficiency or cost grounds (Issue 1).
- The efficiency of Western Power's investment program could be enhanced by examining opportunities to work with other utilities and planning authorities to reduce the traffic congestion, noise, time and costs associated with infrastructure works (Issue 1).
- Consumers and market participants would likely benefit from a contestable approach to the rollout of advanced meters rather than implementing them via Western Power's access arrangement. Such an approach would drive innovation and encourage more competitive product and service offerings. It would also drive down costs and generate data that will inform and empower consumers and energy providers (Issue 4).
- Deferring transmission revenue to future access arrangement periods is not necessary as there are alternative price path options that would minimise 'price shock' without harming economic efficiency or compromising the Access Code's price control requirements (Issues 10 and 20).

The attached submission elaborates on these observations.

Involving customers in the development of access arrangement

ATCO Australia considers it is good practice for network businesses to engage with their customers and other stakeholders in developing access arrangements, even if this is not a specific regulatory requirement. In ATCO Australia's view, engaging with customers and stakeholders is critical to network businesses operating and investing in their network in a manner consistent with the long-term interests of consumers.



For this reason, ATCO Australia supports the engagement approach adopted by Western Power in developing its access arrangement, and commends the business for striving to balance consumer expectations with regulatory obligations.

Customer and stakeholder engagement will play a central role in the development of the next access arrangement (AA5) proposal being prepared by ATCO Gas Australia in relation to the Mid-West and South-West Gas Distribution network, which is due to be submitted to the Economic Regulation Authority on 1 September 2018 for the five-year period commencing on 1 January 2020.

If you have any questions or would like to discuss any of these issues further, please contact me or Matthew Cronin, General Manager Regulation ATCO Gas Australia.

Sincerely,

J.D. Patrick  Creaghan
Managing Director and Chief Operating Officer

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ATCO Australia submission on the Economic Regulation Authority's Issues Paper: Proposed revisions to Western Power's network access arrangement

Background

The Issues Paper published by the Economic Regulation Authority (ERA) on 31 October 2017 seeks submissions from interested parties on aspects of Western Power's proposed revisions, the review process, and some of the key issues to be addressed by the ERA in making a determination on the revisions. The Issues Paper is structured around 25 specific issues across four broad areas.

ATCO Australia recognises the importance of all 25 specific issues, but has sought to address only those where we consider our experience to be more relevant. As a consequence, ATCO Australia's submission focusses on a small number of specific issues within two of the broad areas of interest to the ERA:

- investment in the network; and
- network charges and metering.

The submission also provides general comments on matters ATCO Australia believes are important for the Economic Regulation Authority to be aware of when assessing Western Power's proposed revisions to its access arrangement.

Investment in the network (Issues Paper, Section 3.1)

Issue 1: Submissions are invited from interested parties on whether the approach Western Power has taken to developing its network investment plan for AA4, including its consideration of future uncertainties and possible effects of new technologies, and the expenditure it is proposing meet the Access Code objectives and new facility investment test requirements.

Technology advances are enabling rapid development of viable alternatives to traditional network infrastructure investment. At the same time, the way consumers are generating and using electricity is changing. These trends will continue and may evolve in ways that are not possible to contemplate today.

Given this context, energy network businesses like Western Power need to explore opportunities to improve the efficiency of their investment program by taking advantage of lower cost alternatives to traditional network infrastructure solutions.

One approach for Western Power to consider is to pursue, on a default basis, non-network investment solutions, or alternative technologies, rather than just doing so for low density regional locations where traditional infrastructure options are difficult to justify on efficiency or cost grounds. It is also possible these approaches could be viable in denser and connection-rich metropolitan locations.

Furthermore, it is probably not essential that non-network solutions or alternative technologies be delivered or owned by Western Power. A contestable approach to delivering non-traditional network investment would drive innovation, leverage market expertise, and incentivise the delivery of efficient and cost-effective solutions. It would also transfer financial and operational risks to the private sector, which could reduce Western Power's call on State debt funding and free up funding for other social and infrastructure priorities.

The Economic Regulation Authority could consider future uncertainties and possible effects of new technologies by:

- examining whether Western Power's proposed capital expenditure adequately accounts for changing consumer behaviour, the growing cost-effectiveness of non-network solutions, and the falling cost of alternative technologies;
- considering if Western Power should submit major augmentation proposals for the regulatory test as part of proposed revisions to the Access Arrangement (rather than outside of the Access Arrangement process) to give greater transparency of the opportunities for non-network investment solutions; and
- continuing to provide the D-factor in the Access Arrangement, which is a mechanism that provides for the recovery of operating expenditure incurred by Western Power as a result of deferring a capital expenditure project or for demand-management initiatives.

As well as pursuing non-network solutions and alternative technologies, there are opportunities for Western Power to improve the efficiency of its investment program by working with other utilities and planning authorities to reduce the traffic congestion, noise, time and costs associated with infrastructure works.

A practical example of the benefits of such collaboration is the recent joint effort of ATCO Gas Australia and the Water Corporation, as part of the Smarter Planning Perth initiative, to conduct joint trenching activities during the replacement of natural gas and water mains in Fremantle. This collaborative approach allowed for an efficient delivery of the mains replacement program for both businesses, lowered the costs associated with re-instatement, and reduced community disruption.

ATCO Gas Australia looks forward to continuing such alliances and would welcome new opportunities in the future. The projects to be completed as part of Round 6 of the State Underground Power Program, due to be rolled out from 2018, may provide such an opportunity for Western Power and ATCO Gas Australia to coordinate their infrastructure activities.

Network charges and metering (Issues Paper, Section 3.4)

Issue 4: Submissions are invited from interested parties on:

- *Western Power's proposal to install advanced meters, including whether the expenditure meets the Access Code objectives and new facilities investment test;*
- *the proposed new time of use and demand tariffs;*
- *the balance between fixed and variable charges; and*
- *any other tariff developments considered necessary to meet the Code requirements.*

ATCO Australia's comments on Issue 4 relate specifically to Western Power's proposal to install advanced meters under the access arrangement.

ATCO Australia considers that a broader rollout of advanced meters in the South West Interconnected System is critical to promoting efficient energy use, empowering consumers, and lowering the cost of providing energy services.

Based on our experience in other jurisdictions, ATCO Australia believes the rollout of advanced meters needs to be managed in a way that ensures metering services are delivered in an efficient, timely and competitive manner. A supportive regulatory framework is an essential element for achieving these objectives.

In the National Electricity Market, the regulatory framework supports a market-led approach to the deployment of advanced meters where consumers drive the uptake of technology through their choice of products and services. In making the final rule change determination introducing these regulatory arrangements, the Australian Energy Market Commission noted that:

“This competitive framework for metering services is designed to promote innovation and lead to investment in advanced meters that deliver the services valued by consumers at a price they are willing to pay.”¹

ATCO Australia acknowledges that the regulatory framework for metering services in Western Australia is different to the National Electricity Market framework, but believes Western Australian electricity consumers could benefit from a contestable and market-led approach to advanced meters. In our view, a contestable approach would benefit consumers by incentivising innovative and competitive product and service offerings. It would also drive down costs and provide consumers with informative and empowering data.

ATCO Australia is also mindful that a contestable approach to metering could be a way of limiting the risk that metering becomes a barrier to future policy and regulatory reforms or market development.

The Economic Regulation Authority could facilitate contestability in metering services over time by keeping options open for policy makers. This could be done by providing for the recovery of advanced metering costs via the Metering Code rather than through the Access Arrangement. The concurrent review of the Model Metering Service Level Agreement provides an opportunity to consider how this might be achieved.

¹ Page i, Australian Energy Market Commission, Rule Determination, *National Electricity Amendment (Expanding competition in metering and related services) Rule 2015 and National Energy Retail Amendment (Expanding competition in metering and related services) Rule 2015*, 26 November 2015.

Issue 10: Submissions are invited from interested parties on the following building blocks:

- *Return on working capital*
- *Taxation*
- *Investment adjustment mechanism*
- *Service standard adjustment mechanism*
- *Unforeseen events*
- *D-factor*
- *Gain sharing mechanism*
- *Deferred revenue*
- *Tariff equalisation contribution*
- *K-factor adjustment*

Issue 20: Submissions are invited from interested parties on Western Power's proposed updates to the deferred revenue that will be recovered in future access arrangement periods.

ATCO Australia's comments on Issue 10 relate specifically to deferred revenue.

ATCO Australia acknowledges Western Power is attempting to minimise 'price shock' to transmission customers by proposing to defer the recovery of \$234.1 million of AA4 target transmission revenue to future access arrangement periods and to increase transmission prices by 10 per cent each year instead of the 18 per cent that would be required in the absence of a revenue deferral. The approach proposed by Western Power is similar in structure and concept to the revenue deferral approved in AA2.

However, ATCO Australia has reservations about pursuing a similar approach for AA4 because:

- the special circumstances relating to the regulatory framework that supported revenue deferral in AA2, such as changes in the regulatory treatment of capital contributions, are not a relevant consideration for AA4;
- transmission tariffs will be below efficient costs for the duration of AA4, which is not conducive to promoting efficient investment in and use of the network (as required under the Access Code objective) – existing customers will 'overuse' transmission services, new customers will need to make higher capital contributions to offset their artificially lower incremental revenue, and Western Power may not receive clear investment signals;
- there is a clear expectation in the regulatory framework that network businesses should seek to align their required revenue with the forward-looking and efficient cost of providing regulated services during the access arrangement period – if revenue is deferred, then the business is pushing the burden of cost recovery for current services onto future users of the network; and
- it does not address the underlying gap between transmission revenue and the cost of service at the end of the AA4 period. If this approach is adopted Western Power is likely to be faced with a similar need to defer revenue in its AA5 submission.

In addition, ATCO Australia believes there are viable alternatives to the proposed price path that would address 'price shock' for transmission customers, in this and the next access arrangement period, without compromising economic efficiency objectives. Western Power explored some of these options in Attachment 10.8 of their submission.

In determining the best price path option for transmission customers the Economic Regulation Authority may wish to consider the issues highlighted by the Queensland Competition Authority in an information paper discussing price smoothing². A key conclusion of the paper is that:

“material changes in prices between one regulatory period and the next, resulting from specific regulatory arrangements, should be avoided where there is no reasonable economic rationale to support them and they are in effect an arbitrary outcome of the specific regulatory arrangements”.

It is important that the Economic Regulation Authority ensures that there is an appropriate balance between the longer term interests of consumers and minimising short term price shocks. In evaluating the best way of smoothing Western Power’s transmission revenue over the AA4 period, ATCO Australia suggests that the Economic Regulation Authority has regard to the following principles:

- Unsmoothed and smoothed revenue should be equalised in net present value terms;
- Proposed tariffs should reflect their underlying efficient costs;
- There should be minimal tariff variability from the final year of the current access arrangement and within the access arrangement period; and
- It is important to minimise the likelihood of variability in tariffs at the start of the next access arrangement period.³

ATCO Australia considers that the price path option most consistent with these guiding principles, and most likely to deliver an efficient outcome, is Option 3 in Western Power’s *Transmission Price Path* paper (Attachment 10.8).

Under this option, there would be a substantial increase in year one, followed by smaller increases in following years. In ATCO Australia’s view, this option provides transmission customers with pricing stability over the longer term and allows transmission prices to provide more effective signals to promote the economically efficient investment in and operation and use of the Western Power network by transmission users and Western Power.

² Page 31, *Financial Capital Maintenance and Price Smoothing*, Information Paper, Queensland Competition Authority, February 2014.

³ ATCO Australia notes that the Australian Energy Regulator typically targets keeping the divergence between the smoothed and unsmoothed revenues for the last year of the access arrangement period within a target range of 3 per cent.