Design Consultation Paper – Regulatory Framework for the Pilbara electricity networks

Alinta Energy

Submission

9 March 2018

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1 Introduction

Alinta Sales Pty Ltd (**Alinta**) welcomes the opportunity to provide a submission to the Public Utilities Office (**PUO**) on the *Regulatory framework for the Pilbara electricity networks - Design Consultation Paper* (**Design Consultation Paper**) relating to the regulatory framework for the Pilbara electricity networks.

Alinta supports the Government's decision to implement a light handed regulatory regime, including the development of an Independent System Operator (**ISO**), in the NWIS. A light-handed regime will provide a suitable balance between reducing the potential for resource misallocation and inefficiencies created in markets with unregulated monopoly assets; while avoiding the costs and potential market failure caused by significant regulatory burden.

The key beneficiaries of competition facilitated by the light-handed regime will be electricity customers connected to Horizon Power's Port Hedland and Karratha distribution network. These customers have been missing out on the benefits of competition, including lower electricity prices, for many years despite the NWIS having all the physical characteristics required for competition to thrive.

Alinta looks forward to the light-handed regime being operational as soon as possible and believes all industry participants, including government, must work together in good faith to ensure its swift and effective implementation so customers can start to realise the benefits unlocked by competition.

1.1 Background

The NWIS is comprised of interconnected electricity generation, transmission and distribution assets in the Pilbara region of Western Australia, including the major towns of Port Hedland and Karratha. The NWIS is made up of assets owned by many different parties, under both private and public ownership.

The NWIS is not currently centrally planned and operated and has developed in an ad hoc manner over several decades, as resources and energy companies made individual investments in generation capacity and network infrastructure to meet their own needs.

The Pilbara region is a significant economic driver for Western Australia, yet the electricity system supporting the region is fragmented and uncompetitive. The ad-hoc evolution of the market has at times led to sub optimal outcomes.

Despite its size and importance to the State, currently Horizon Power (Horizon) is the sole electricity retailer to almost all the customers connected to the NWIS.

Alinta is one of a number of electricity retailers seeking to enter the market to supply competitively priced electricity to customers connected to the Horizon Network.

Several customers with significant sized loads connected to the Horizon Network have indicated to Alinta a strong interest in the opportunities that competition delivers: price differentiation,

innovative and focussed product offers and enhanced customer service. The only barrier to Alinta's entry to the NWIS is gaining access to the Horizon Network to deliver energy and other tailored offerings to customers.

Alinta has sought to gain access under various mechanisms and approaches to the Horizon Network since April 2014 and has been continually frustrated and delayed at every stage.

Alinta's access attempts have included initial access discussions, an application for coverage in 2014 (which was subsequently withdrawn), and following a request from the Minister for Energy for Horizon to commence negotiations with Alinta, negotiations under a Memorandum of Understanding embodying a mutual objective to negotiate an Electricity Transfer and Access Contract (**ETAC**) that would apply on a reciprocal basis and commence prior to 30 June 2016.

Following protracted access discussions between Alinta and Horizon, and absent any formal framework as to process, in August 2017 Alinta applied under section 3.8 of the Code to the Minister for Energy for coverage of the Horizon Network to facilitate Alinta's entry into the market to supply electricity to customers connected to the Horizon Network under its Electricity Integrated Regional Licence (**EIRL**)[1]. The Minister made a Final Determination to grant coverage of the Horizon Network from January 2020[2].

Access to the Horizon Network will unlock significant benefits to Pilbara customers and the region more broadly. However, open access along with the establishment of a light-handed regulatory framework and ISO will further enhance benefits by improving the efficiency of the entire NWIS.

1.2 Structure of this submission

To assist the PUO in its consideration of Alinta's coverage application this submission is structured as follows:

- Section 2 – NWIS regulatory reform implementation timeline
- Section 3 - Proposed third party access framework
- Section 4 – Establishing an Independent System Operator
- Section 5 - Conclusion

2 NWIS regulatory reform implementation timeline

Alinta notes the PUO's timetable for implementing the light-handed regime is as follows:

[1] EIRL8, dated 12 August 2014, available: https://www.erawa.com.au/electricity/electricity-licensing/licence-holders
[2] Final Coverage decision, 2 February 2018, available: http://www.treasury.wa.gov.au/Public-Utilities-Office/Open-consultations-reviews/Electricity-Networks-Access-Code-Coverage-Application/

Table 1: Proposed Implementation Timetable

Implementation timetable	
March 2018	Design and implementation plan finalised
Apr-Dec 2018	Legislation, detailed regulatory framework finalised, transition plan developed
Jan-Jun 2019	Execute transition plan and stakeholder engagement
July 2019	New regime commences
July 2020	Post implementation review

Alinta welcomes the above timeframes which will provide NWIS customers with the benefits of competition as soon as practicable – noting that Alinta has sought to gain access since early 2014.

However, it is recognised that given the number of complex issues yet to be resolved it will be imperative on all stakeholders in government and industry to continue to actively participate in the regime's development and prompt resolution of issues.

To achieve the above timetable, it will be necessary to deal with many issues concurrently, using expedited processes. For example:

- expert working groups from industry and government should be established to resolve issues and draft the regulatory framework;
- proposed legislation, regulations and rules should be adapted from current and well-established regimes where possible – for example, the Western Power Technical Rules, the Wholesale Electricity Market Rules and various aspects of the National Gas Law and National Gas Rules; and
- the open access framework is likely to be completed prior to the ISO model given the precedents that exist and the issues being less complex. Accordingly, once the open access framework is complete, it is imperative that access processes and negotiations should be allowed to commence with a view to contracts being executed and operational immediately upon the implementation of the ISO.

Alinta looks forward to actively participating in the development of the NWIS light-handed regime.

3 Proposed third party access framework

Alinta is broadly supportive of the third-party access framework, particularly relying on existing frameworks where appropriate, for example the non-scheme pipeline arrangements. However, as noted in its response to the PUO's issues paper, it is important that a thorough assessment of the appropriateness of this regime for the NWIS context is undertaken.

3.1 Access framework objectives and design criteria

Alinta is supportive of providing for a NWIS regulatory framework that delivers efficiencies in all aspects of the market. As such, Alinta agrees with the PUO's objective of introducing third party access through a light handed regulatory framework for the NWIS as a more effective and efficient alternative to the current regulatory framework in the Electricity Networks Access Code 2004 (**Access Code**).

As outlined in its submission to the Issues Paper, Alinta considers that using an efficiency objective as an overarching guide should ensure that a regulatory model is designed such that it meets the needs of the NWIS while making the best use of resources and ensuring low costs (both implementation and ongoing) for all stakeholders.

Alinta is supportive of the PUO's design criteria outlined in the Design Consultation Paper[3] of:

- clear delineation of rights and responsibilities for current and future participants, including the ISO;
- recognising existing property rights;
- a pro-competitive bias providing a level playing field for new entrants and minimising network owners favouring their own generation or supplies to customers; and
- a bias in favour of low-cost regulatory requirements that do not impose a regulatory burden.

Noting this support, Alinta considers that there is some benefit in also embodying the following guiding principles from the PUO's Issues Paper into the design criteria:

- contractual and regulatory certainty; and
- safety of the network and security of existing supply arrangements.

3.2 Coverage

A key issue for the development of an access regime is the assessment and decision as to what assets should be covered by such a regime.

In the Design Consultation Paper, the PUO notes that it:

> "*considers that including the Alinta DEWAP interconnected network assets at the commencement of the light handed third party access regime supports the NWIS access regime objectives and is consistent with the design criteria*" [4]

Alinta supports coverage of networks where there are clear net benefits of doing so. Alinta is committed to doing what it can to ensure the light-handed framework is established in the NWIS in a

[3] Section 2.1, Design Consultation Paper.
[4] Section 2.2.1, Design Consultation Paper.

timely manner and, in that respect, is open to including its infrastructure. That being said, Alinta is not convinced that including the Alinta DEWAP interconnected network at the commencement of the light handed third-party access regime is in line with one of the PUO's design criteria being:

> *"a bias in favour of low-cost regulatory requirements that do not impose a regulatory burden on networks in advance of and disproportionate to any reasonable network connection and access requirements*." [5]

Alinta has a concern that including its DEWAP network into the regime at commencement could impose a disproportionate regulatory burden on Alinta in advance of any bona fide network connection and access requirements. Further detail supporting this position is contained in section 3.2.1.

3.2.1 Alinta's response to the coverage design elements

Alinta believes the Government should focus on the areas where there are clear net benefits that will result from implementation of a light-handed regime. Currently this is in Port Hedland and Karratha (the Horizon Network) which has the largest load by customer numbers and volume and where the savings from competition will drive the largest economic benefits.

Alinta's response to each of the design elements relating to coverage in the third-party access framework are outlined below.

Design Element 1

The following interconnected networks in the Coastal Region of the NWIS will be covered at commencement of the light handed third-party access regime in the NWIS:

- the Horizon Power interconnected network; and
- the Alinta DEWAP interconnected network.

Under the Electricity Network Access Code, there are three criteria which must be satisfied before coverage of a network is granted. These are:

a) Promotion of competition, that is would coverage result in a material increase in competition in at least one market?

b) Would it be uneconomic for another party to develop another network to provide the covered services provided?

c) Would access be contrary to the public interest?

For the assessment of Alinta's application of coverage of the Horizon Power NWIS network, it was demonstrably shown that all the criteria were met, and the Minister for Energy, subsequently decided to declare the Horizon Power network covered.

In its Design Consultation Paper, the PUO states that:

[5] Section 2.1, Design Consultation Paper.

*"In order to achieve the **maximum economic benefits** of competition at commencement of the light handed third party access regime in the NWIS, while not jeopardising the integrated nature of the mining operations (**particularly in the absence of any bona fide user applications for coverage**), the Public Utilities Office is of the view that coverage at commencement should apply to the following interconnected networks in the Coastal Region:*

- *the Horizon Power interconnected network; and*
- *the Alinta DEWAP interconnected network."* [6]

[Alinta emphasis added]

While the PUO considers coverage of the Alinta DEWAP network will lead to maximum economic benefit, Alinta notes that there has never been any analysis as to whether coverage of the Alinta DEWAP network would meet the necessary criteria and therefore result in the net economic benefits.

If such an analysis were undertaken Alinta questions whether a coverage application for the Alinta network would meet the Access Code criteria and at this stage, provide any material net benefit. Alinta explores these issues below.

1. Coverage of the Alinta DEWAP network will not promote competition

Alinta is not certain that coverage of its Alinta DEWAP network will result in a material increase in competition for the reasons outlined below.

1.1. There have been no formal requests for access to the Alinta DEWAP network

There is no evidence that access to Alinta's DEWAP network will promote competition as no party has ever lodged a bona fide formal request to access its network[7]. Given this, Alinta has no reason to believe there are any genuine access seekers for its network.

While Horizon Power has indicated it would like access to Alinta DEWAP's network, it has never formally requested access to a network connection and Alinta has never had discussions with it about its ability to make access available.

Without access seekers competing for the retail or wholesale supply of electricity off the Alinta DEWAP network, Alinta is not convinced about whether there are any benefits of increased competition.

1.2. The Alinta DEWAP network is connected to customers with significant countervailing power

The only customers that exist on the Alinta DEWAP network are BHP and Fortescue Metals Group (**FMG**), both of which are subject to long term supply contracts.

[6] Section 2.2.1, Design Consultation Paper.

[7] Other than Horizon Power lodging a competing coverage application in direct response to Alinta's initial coverage application.

BHP and FMG are two of the largest electricity customers in Australia. Like most established mining companies, they have significant countervailing power when negotiating with generators for electricity supply.

Their countervailing power is bought about by the materiality of their electricity supply contract and the numerous options open to them to limit the costs of their supply. The options include to bypass the Alinta DEWAP network by building their own network connections and/or building their own generation.

This countervailing power was demonstrated in 2011 when BHP decided to build its own on-site generation rather than contract with Alinta's existing Newman power station which was adjacent to the BHP operations.

The existence of countervailing power mitigates market power ordinarily possessed by a network operator, lessening any material promotion of competition bought about by open access.

1.3. The Alinta DEWAP network is fully contracted on a firm basis

The ability for new loads to connect to the Alinta DEWAP network is limited because:

- The transmission line is currently fully contracted on a firm basis and therefore there is no firm access available. However, there is scope for access on an interruptible basis.
- No additional capacity is available for new loads on an n-1 basis unless significant transmission infrastructure investment is made.

Therefore, there are limited opportunities to materially improve competition due to users gaining access to the Alinta DEWAP network given it is currently constrained.

2. Is it uneconomic to duplicate the network?

Alinta agrees that it would be uneconomic to duplicate the entire Alinta DEWAP network to supply commercial and industrial customers in Port Hedland.

However, for large mining customers whose electricity supply contracts are material and long term in nature, Alinta believes it would be economic to duplicate its network.

The economics test was demonstrated when Alinta won a tender to supply electricity through the construction of a 120km transmission line from its Newman power station to the Roy Hill mine. It won the tender over other electricity supply solutions, including onsite generation.

3. Would access be contrary to the public interest?

An important part of assessing whether coverage meets the public interest criteria is to assess whether the potential benefits outweigh the potential costs.

3.1. *There are material regulatory costs of open access*

As recognised by both Horizon Power and the Public Utilities Office, there are material costs involved for a network owner to comply with an open access regime. Horizon Power estimated its regulatory costs as $1 million per annum. Alinta agrees this estimate is consistent with what its own costs would be.

The costs to manage an access process include:

- drafting an ETAC and supporting documentation, including developing an appropriate pricing model;
- undertaking negotiations with access seekers and any subsequent arbitration process; and
- Managing on-going information disclosure requirements and compliance.

3.2. There are material costs and business disruption caused by the ring-fencing requirements

In addition to the above regulatory costs there are significant costs and business disruption from implementing appropriate ring fencing arrangements. While Alinta has not been able to undertake a detailed cost analysis in the short timeframe that it has had to respond to this Design Consultation Paper, Alinta expects these costs to also be in the order of $1 million per annum.

Alinta operates an efficient vertically integrated business which supplies two customers in the NWIS. The Alinta staff who manage the Port Hedland operations have broad responsibility and expertise across all areas of the business. This includes oversight of its power generation operations, transmission network and management of supply to its two major customers. In addition, system and processes are generally shared and visible to all relevant Alinta staff.

The requirement to ringfence the network part of Alinta's Port Hedland operations would be significant and would require:

- An increase in staff to ensure no overlap of network management functions with other functions; and
- Duplication of systems and processes to avoid information sharing.

In addition, Alinta expects ringfencing will result in material business disruption as the new processes, procedures and compliance requirements are bedded down.

3.3. *The costs of coverage may not be outweighed by the benefits*

As stated, the only customers on the Alinta DEWAP network have significant countervailing power and therefore open access is unlikely to result in further competition benefits to those customers.

Therefore, without any new retail customers on the Alinta DEWAP network (of which could not occur unless there is significant transmission investment) there are limited net benefits of open access.

4. Conclusion on coverage of the Alinta DEWAP network

Alinta is committed to doing what it can to ensure the light-handed framework is established in the NWIS in a timely manner and, in that respect, is open to including its DEWAP infrastructure. That being said, Alinta is not convinced that there is a clear net benefit from doing so.

Given this, coverage of the Alinta DEWAP network should not occur until:

- A genuine access seeker makes a specific and bona fide request for access to the network; and
- The PUO undertakes an assessment of whether coverage of the Alinta DEWAP network would in fact meet all the coverage criteria, specifically would coverage result in a material increase in competition in at least one market.

Design Element 2

Uncovered NWIS Interconnected Networks can 'opt-in' to the light handed regulatory regime at any time.

Alinta agrees with this design element.

Design Element 3

Coverage will be extended in the future to networks not covered at commencement by application of the existing Access Code coverage test.

An assessment for coverage is triggered by a coverage application that must be assessed by the Minister for Energy in accordance with current coverage criteria.

If a network is found to meet the coverage criteria, then the Minister will be required to make an additional decision as to whether the network should be subject to the light handed or full regulation, using principles similar to those in the National Gas Law.

Alinta supports the further inclusion of networks under the light-handed access regime where the coverage criteria is met.

As noted above, the Alinta DEWAP network should be assessed against the coverage criteria before a decision is made about whether it must participate in the light-handed regime upon its commencement.

3.3 Light handed access framework

It has been rightly recognised that the form of economic regulation that is available under the Access Code would be unnecessarily burdensome for the size, composition and maturity of the NWIS. In place of the 'heavy-handed' form of regulation currently under the Access Code, Alinta is of the view that a commercially fit-for-purpose 'light-handed' regulatory regime will balance the need for facilitating open access to the NWIS while minimising the regulatory burden and costs imposed on market participants.

Alinta is supportive of the overarching objective of the light-handed framework being:

> *"to facilitate access on reasonable terms to services provided by covered networks – which for the purposes of the framework, will be taken to mean at prices and on terms and conditions that so far as practical reflect the outcomes of a workably competitive market."*

Further, Alinta supports, at a high level, a regime that includes:

- a framework for access pricing, including pricing principles to guide price setting and that the arbitrator must have regard to when determining access disputes;
- a process for dealing with connection and access requests;
- requirements for the publication and exchange of information to facilitate timely and effective commercial negotiations in relation to access to covered networks;
- a negotiation framework; and

- a commercially-orientated binding arbitration process to resolve access disputes in a cost-effective and efficient manner.

Alinta's response to each of these design elements are outlined below.

3.3.1 Alinta's response to the light handed access framework design elements

Access Pricing

Design Element 4

Pricing principles will be developed to guide price setting and dispute arbitration.

Broadly, in terms of access pricing, Alinta believes that if the principles for negotiation include efficient pricing principles, and an effective and binding dispute resolution process is in place, then price regulation, including price oversight is unnecessary.

Noting this, Alinta supports pricing principles being developed to guide price setting and dispute arbitration. These principles should be detailed enough to provide sufficient guidance to the negotiating parties to ensure efficient network access prices are set to achieve tariffs that reflect the forward-looking efficient costs of providing the services.

Alinta notes that if pricing principles are too broad they are open to interpretation and therefore material disagreement may potentially arise between the parties. Alinta notes it had concerns with the pricing methodology adopted by Horizon Power in its previous access negotiations despite the existence of reasonable pricing principles. Alinta's concerns included those outlined in its submission to the PUO's Issues Paper on the coverage of the Horizon NWIS network[8].

[8] Alinta Energy Submission to the PUO's Issues Paper – Coverage of Horizon Power Electricity Network in the North West Interconnected System, Appendix 4, 16 October 2017.

While further work needs to be done by the PUO and industry jointly to determine the most appropriate principles to be used in the NWIS, Alinta has provided some high-level comments on the proposed pricing principles in the table below.

Table 2: Proposed Pricing Principles – Alinta's initial comments

#	PUO proposal	Alinta initial comment
1.	Prices are to signal the economic costs of service provision, by:	
	- being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), except where subsidies arise from compliance with legislation and/or other regulation;	Alinta notes that this is another way of saying that the price must sit within the lower – upper bound pricing range, which Alinta accepts. Alinta is concerned that the principle does not go anywhere near far enough and notes that pricing should be subject to economic scrutiny from an efficiency pricing perspective, not at just below the standalone cost.
	- having regard, to the extent practicable, to the level of available service capacity;	Alinta requires additional information about what the PUO is proposing, and questions whether this is a form of scarcity pricing.
	- signalling, to the extent practicable, the impact of additional usage on future investment costs.	Alinta accepts this principle, and notes that this is similar to long run marginal cost pricing (and somewhat linked to a scarcity pricing approach).

#	PUO proposal	Alinta initial comment
2.	Provided that prices satisfy (1) above, prices should be responsive to the requirements and circumstances of stakeholders in order to:	
	- discourage uneconomic bypass;	Alinta agrees, provided that consideration is given to available capacity.
	- allow for negotiation to better reflect the economic value of services and enable stakeholders to make price/quality trade-offs or non-standard arrangements for services;	Alinta broadly agrees but notes its concerns with Horizon's previous pricing models.
	- where network economics warrant, and to the extent practicable, encourage investment in transmission and distribution alternatives (e.g. distributed generation or demand response) and technology innovation.	Alinta broadly agrees, noting that this is achieved through cost reflective pricing.
3.	A covered network service provider should be provided with a reasonable opportunity to recover at least the efficient costs it incurs in: - providing covered network services; and - Regulatory Framework for the Pilbara Electricity Networks – Design Consultation Paper - complying with a regulatory obligation, other obligations or requirements for making a regulatory payment.	Alinta considers that this principle should be redrafted as follows: A covered network service provider should be provided with a reasonable opportunity to recover ~~at least~~ **[only]** the efficient costs it incurs in: …
4.	Regard should be had to the economic costs and risks of the potential for under and over investment by a covered network service provider in, as the case requires, a distribution system or transmission system with which the operator provides covered network services	Alinta broadly agrees and notes that in setting the initial capital base (i.e. the starting RAB) should adopt Depreciated Optimised Replacement Cost (DORC) methods or NFIT tests. Investments in assets that are not prudent and efficient should be struck out from the ICB.
5.	Regard should be had to the economic costs and risks of the potential for under and over utilisation of a distribution system or	Alinta broadly agrees.

#	PUO proposal	Alinta initial comment
	transmission system with which a covered network service provider provides covered network services	
6.	Regard should be had to the regulatory asset base with respect to a distribution system or transmission system, with an accepted method being used for the initial valuation and for rolling forward that valuation to future years.	See Alinta's comments to point 4 above.
7.	When applying the above principles to a network service that when used affects the capacity of the covered network available for other network services and is priced at a premium or a discount to the price for a firm service on the relevant covered network – the premium or discount must: - take into account any opportunity cost or benefit to the network service provider of providing the network service, having regard to any effect on the cost of providing firm services or the capacity of the covered network; and - be consistent with the price for the network service providing a reasonable contribution to joint and common costs.	Alinta broadly agrees but notes that this needs to be underpinned by a proper economic rationale.
8.	A covered network service provider should be provided with effective incentives in order to promote economic efficiency with respect to covered network services the operator provides. The economic efficiency that should be promoted includes: - efficient investment in a distribution system or transmission system with which the operator provides covered network services; - the efficient provision of electricity network services; and - the efficient use of the distribution system or transmission system with which the operator provides covered network services.	Alinta broadly agrees. However, Alinta notes that there are alternative approaches like Efficiency Carry-Over Mechanisms which can achieve this, noting this, consideration would need to be given as to how these concepts could be implemented in a 'light handed' approach to price regulation.

#	PUO proposal	Alinta initial comment
9.	Development of prices should be transparent, promote price stability and certainty for stakeholders, and changes to prices should have regard to the impact on stakeholders.	Alinta considers that this principle needs to include a reference to "efficient". Further, Alinta considers that there needs to be greater detail to guide / define where prices should be set at.
10.	Development of prices should have regard to the impact of transaction costs on retailers, consumers and other stakeholders and should be economically equivalent across retailers	Alinta broadly agrees.

Alinta notes that the proposed pricing principles above do not include corporate costs and overheads. Alinta considers that it is appropriate that a robust process for the allocation of corporate costs and overheads should be applied such as causal allocation methods.

Design Element 5

The onus will be on networks to develop, negotiate and defend their pricing methodologies in accordance with the Pricing Principles.

Design Element 6

In setting Reference Tariffs, the covered network businesses will be required to demonstrate that (a) they meet the Pricing Principles, and (as the case may be) to attest that they have applied the pricing guidelines or (b) to otherwise describe the methodology and key assumptions they have used in developing their Reference Tariffs.

Alinta agrees with Design Elements 5 and 6.

However, it's important that timely information is disclosed to access seekers so they can determine whether prices are consistent with the pricing principles. Alinta supports clear timeframes around when network operators must reply to requests for information.

Design Element 7

By mutual agreement, an access applicant and the relevant network could agree on a Non-Reference Tariff.

Alinta agrees that flexibility should exist for parties to negotiate bespoke terms to an access agreement.

However, its important the network operator assesses all access requests equally and does not discriminate against access seekers who may present a competitive threat to other parts of their business.

Connection and access policies

Design Element 8

Network access in the NWIS will be designed as a 'market carriage' regime.

The NWIS effectively operates as a contract carriage regime today. The shift to a market carriage model may be required in the future to allow electricity to be pooled and flow to various customers in the network in real time, particularly in the case of emergencies.

Alinta is not concerned by the shift to a market carriage model as long as:

- The contractual rights of existing generators are recognised and grandfathered where required;
- The change to a market carriage model in no way impacts existing contractual rights and responsibilities under current electricity supply contracts in the NWIS.

Design Element 9

Generators connected to the NWIS networks at the commencement of the new regime will continue to receive access that is unconstrained, or not constrained to a greater extent than at regime commencement. These grandfathered requirements will be codified in a set of 'NWIS Rules' relating to scheduling and dispatch and relating to any new connections and expansions of existing generators and loads.

Alinta agrees that grandfathering existing access rights is essential in the NWIS.

Design Element 10

New generators or expanded capacity of existing generators will be allowed network access on a constrained basis, with such generators being appraised (without guarantee) of the likely extent of constraints and the options for relieving those constraints. Generators would be liable for the cost of any options they choose to relieve constraints.

Alinta agrees that where constraints exist, access for new access seekers should be provided on a constrained basis.

However, Alinta believes the design should allow for:

- An independent assessment of network constraints by the ISO;
- effective ringfencing of network operator and generator functions; and
- the ability for an independent assessment/arbitration of costs to relieve constraints, given the inherent conflict of interest with vertically integrated network operators and generators.

Noting this, it would be reasonable to expect that a new generator/customer should not be expected to pay to fix a problem which existed prior to their connection.

Design Element 11

Loads will be provided with access at default security levels to be defined, but with provision for specific loads to request bespoke access and connection point security criteria to apply to them.

Design Element 11 appears reasonable, including consideration being given to grandfathering existing security levels.

Design Element 12

The networks will be responsible for managing the connection process, including specifying connection asset requirements and commercial terms for the provision of such assets.

Alinta supports Design Element 12 given network owners are the most appropriate people to manage the process of connecting customers to their network.

However, given the unique conflict of interests that currently exist in the NWIS, the design should provide for access seekers being able to seek an independent assessment or arbitration of the access requirements and commercial terms required.

Design Element 13

The ISO will be responsible for dealing with the 'electricity transfer and access' aspects of new connections and applications for expanded capacity, including the matters described in Design Element 10. The ISO will also design any changes to scheduling and dispatch resulting from constraints to new or expanded generators, in accordance with the NWIS Rules, and will accordingly manage constrained dispatch where required.

Alinta supports Design Element 13.

Requirements for publication of information

Alinta considers that an appropriate information disclosure regime should provide prospective access seekers with sufficient information to reduce the imbalance in bargaining power they may face when negotiating with service providers. This could include relevant standardised financial information, released on an annual or as required basis, for use in assessing the reasonableness of offered prices.

Design Element 14

Information disclosure requirements will be developed as part of the NWIS access framework. These will be developed in consultation with stakeholders and will specify the information that must be published by covered networks and the timetable for publication.

The disclosure of information is essential for assisting in the negotiation of access to natural monopoly infrastructure. It's important that any information disclosure requirements also have timeframes around when the information should be disclosed.

However, for smaller networks with less than 3-5 customers like the Alinta DEWAP network, there would be significant confidentiality concerns with the disclosure of some of the information outlined in Appendix B of the design consultation paper. Such disclosure could put the network in breach of their supply contracts.

For example, confidentiality concerns arise because customers on the network could back calculate other customers' usage if certain information is publicly disclosed. Electricity usage information is sensitive as it can be directly related to a customer's downstream output.

Alinta has concerns about the publication of the following information for its Alinta DEWAP network, given there are only two customers supplied on that network:

- A description of the service and any locational limitations on availability;
- The priority ranking of the service in relation to the other network services including when scheduling and in the event of curtailment;
- Monthly usage (kWh) and peak demand (MW); and
- Information about matters expected to affect the capacity of the network (including any planned expansions of the capacity) for each month in the following 12-month period.

Therefore, Alinta does not believe information which could be commercially sensitive should be required to be published by networks with less than 5 customers.

Negotiation framework

To facilitate timely access to a covered network, a robust and clear negotiation framework with well-defined time periods for each step is required.

Design Element 15

A negotiation framework will be developed as part of the NWIS Regime, setting out requirements for each covered network to produce and publish:

- a user access guideline;
- the process for making an access request;
- the process for making access offers, and
- the process for negotiating access, pricing, and access terms and conditions.

Alinta supports the application of the existing gas frameworks to negotiating access in the NWIS and, subject to Alinta's detailed comments below, considers that the requirements for each covered network to produce and publish the list above is appropriate.

In addition to the non-scheme pipeline arbitration mechanism, we refer the PUO to the latest paper from the Australian Energy Market Commission "*Draft Report: Review into the scope of economic regulation applied to covered pipelines,* 27 February 2018" which contains some applicable recommendations aimed at improving the existing negotiation and dispute resolution within the current gas framework.

In particular, Alinta supports a framework which has regard to:

- good faith negotiations, based on full and timely disclosure of information;
- clear guidelines regarding timeframes for negotiations; and
- a process which allows access seekers to notify of an access dispute after the timely conclusion of good faith negotiations.

Alinta looks forward to working with the PUO and the industry on the detailed design of the negotiation and dispute process.

Specific comments on the detailed negotiation framework are below (note Alinta has not commented on each and every aspect of the proposed negotiation framework, instead it has only provided comment on those areas that need additional clarification/review):

Table 3: Negotiation Framework – Alinta's initial comments

PUO proposal	Alinta initial comment
User Access Guide	
It is proposed that the network service provider for a covered network must publish the user access guide for the covered network no later than 20 business days after the application date for the covered network.	Alinta assumes that the reference to "application date for the covered network" for the Network Service Providers subject to initial coverage under this regime is the commencement date of the regime (and likewise, for new network operators covered after the regime commencement, this requirement will be 20 business days from the decision that they are included in the scheme).
Access requests	
The network service provider must notify the prospective user if the service provider needs to undertake further investigations in relation to the prospective user's access request. The notice must be given within 10 business days after receipt of the access request or, if applicable, after receipt of the further information requested.	For clarity, Alinta suggests that this be reworded as follows: The notice must be given within 10 business days after receipt of the access request or, if applicable, within 10 business days after receipt of the further information requested.
A network service provider must: – only undertake further investigations in relation to an access request when and to the extent reasonably necessary; and – carry out further investigations expeditiously.	Alinta considers that there should be a specific timeframe within which the further investigations should be undertaken, and suggests 30 business days (as a maximum).

Dispute resolution

Alinta considers that one of the key features required for a light handed regulatory regime to achieve the objective in the NWIS is the need for a robust dispute resolution framework which is both binding and clear in providing guidance to an arbitrator.

Design Element 16

A dispute resolution framework will be developed, that is clear and binding, based on the non-scheme pipeline arbitration mechanism in the National Gas Rules modified as outlined in this Design Consultation Paper for the specific circumstances of the NWIS. It will be administered by the ERA.

Alinta supports the application of the existing non-scheme pipeline arbitration mechanism in the National Gas Rules, modified as appropriate for the specific circumstances of the NWIS.

Noting this support, Alinta is concerned that dispute processes under the current non-scheme pipeline arbitration approach can take a very long time to progress.

The AEMC noted[9] that for non-scheme pipelines the arbitration process can take up to 65 business days, or up to 105 business days upon agreement of the parties (NB: the periods for provision of information by parties or for experts to consider matters are discounted). The AEMC in the same paper recommended that a fast-tracked dispute resolution process of 50 business days be provided for under specified circumstances.

Alinta supports the PUO considering a fast-track dispute arrangement for the NWIS.

Alinta supports the ERA being appointed as the scheme administrator, with the responsibilities outlined in the Design Consultation Paper.

3.4 Structure and markets

The importance of structural separation was highlighted in the development of Australia's National Competition Policy which recommended that all Australian Governments adopt a set of principles aimed at ensuring that, as part of reforms to introduce competition to a market traditionally dominated by a public monopoly, the public monopoly be subject to appropriate restructuring. The principles deal with:

- the separation of regulatory and commercial functions of public monopolies;
- the separation of natural monopoly and potentially competitive activities; and
- the separation of potentially competitive activities into a number of smaller, independent business units.

Alinta believes that such structural separation of Horizon is essential for an open access regime in the NWIS to work effectively. In noting this, Alinta agrees with the Design Consultation Paper that:

> *"separation of regulated and competitive activities in the NWIS is undertaken on a "fit-for-purpose" basis. This may mean that a different application of functional vs structural separation is appropriate depending on the size and scope of the covered network's affiliated operations. As an example, it may be that vertically or horizontally integrated covered networks with a high proportion of regulated network income from the NWIS relative to retail / generation income from the NWIS should be subject to structural (or legal) separation. Conversely, functional separation may be appropriate for covered networks with a low proportion of regulatory income compared to total income on the NWIS."*

And:

> *"On this basis, structural separation of Horizon Power's covered network may be appropriate (unless Horizon Power is able to demonstrate existing or proposed ring fencing arrangements are sufficient to address stakeholder concerns), while limited separation of certain functions may be appropriate for the Alinta DEWAP covered network at commencement."*

[9] Australian Energy Market Commission: "*Draft Report: Review into the scope of economic regulation applied to covered pipelines"*, Table 3.2, 27 February 2018.

This fit-for-purpose approach is vital for ensuring that the light-handed regulatory regime meets its overall efficiency objective and design principles.

3.4.1 Alinta's response to the structure and markets design elements

Design Element 17

Covered networks' regulated activities and functions will be required to be structurally or functionally separated from their non-regulated activities and functions. Business-specific requirements will be defined, following competition analysis.

Alinta agrees that ring fencing of covered network assets is important in any access regime.

However, Alinta notes that different requirements for different networks should exist depending on the extent of regulated income from a network business compared to its related businesses.

In the case of Horizon Power, the Government is in the unique position of being the asset owner and can therefore show leadership in the NWIS by agreeing to structurally separate the Horizon Power Network business from the Horizon Power retail/generation business. This would allow for the most optimal outcome in the NWIS by ensuring no conflict of interest exist.

However, if structural separation of Horizon Power does not occur, then there must be full ring fencing of the network business of Horizon Power.

Even with ringfencing, the regime should recognise the inherent conflict of interest that exists for vertically integrated networks. Because ringfencing alone can't be relied upon there must be an ability for independent review of decisions by a network operator in which a conflict of interest may arise with its generation or retail businesses.

3.5 Transitional Issues

3.5.1 Alinta's response to the transitional issues design elements

Design Element 18

A transition plan for the new NWIS light handed access regime will allow timelines that permit network service providers to efficiently meet new obligations, and also to ensure that existing contractual positions and operating positions are suitably protected.

Alinta first sought access to the Horizon NWIS network in 2014.

While Alinta agrees time should be allowed for participants to prepare for open access, these timeframes should be kept to a minimum with no further delays tolerated.

In particular, Alinta believes the access framework should be completed promptly with negotiations to begin while the ISO model is still being finalised. This will improve the likelihood that customers in the Pilbara will begin to benefit from competition in 2020.

4 Establishing an Independent System Operator

At present, there is no central system operator for the NWIS. Alinta believes there are benefits in having an independent system operator to ensure system security and stability in the NWIS, both intra-day and in the medium term. Alinta is pleased to see that the Australian Energy Market Operator (**AEMO**) which is independent and has extensive experience in operating electricity and gas markets in Australia is being considered for this important role.

4.1 Proposed ISO Framework

Alinta notes that the framework being proposed by the PUO for the ISO includes:

- a set of guiding objectives and operating principles to assist with the development of the other elements of the framework;
- the extent of the networks covered by the ISO;
- the functions & powers that the ISO could undertake, including identifying the information and powers it will require to successfully undertake its role and responsibilities;
- the structure of the ISO and governance of the ISO; and
- transition matters, noting that the recommended approach allows for the ISO to progressively assume a broader role if it is determined that there are net benefits in doing so.

Alinta is broadly supportive of this framework, subject to its comments in the following sections. However, Alinta notes that it is imperative that the ISO framework remains fit for purpose and is not over-scoped. Alinta is strongly of the opinion that before the ISO assumed any broader role that outlined in this paper, a robust and detailed assessment process would need to be undertaken.

4.2 Design objectives and principles

The Design Consultation paper notes that:

> *"In the absence of an ISO governing body (which would develop its own set of objectives and principles), interim objectives and principles have been developed to guide the design of ISO. The expectation is that the interim objectives and principles will be reviewed by the proposed ISO governing body in due course (in conjunction with key stakeholders)."*

Alinta supports this approach, noting that if the ISO governing body, when established, was going to amend the objectives and/or principles, this would be required to be done following robust consultation processes.

Design Element 19

The interim objective of the NWIS ISO should be consistent with the National Electricity Objective, namely:

'To promote efficient investment in, and efficient operation and use of, electricity services for the long-term interests of consumers of electricity with respect to price, quality, safety, reliability, and security of supply of electricity; and the reliability, safety and security of the NWIS.'

Alinta supports the application of the National Electricity Market Objective to the NWIS.

Design Element 20

The design principles for the ISO are:

1. the ISO's core function is to ensure the reliability and stability of the system;
2. the ISO should act with impartiality and transparency;
3. the ISO should act to maximise overall system efficiency;
4. the cost of establishing and operating the ISO should be kept to a practical minimum;
5. proposed arrangements should consider the commercial interests and priorities of privately-owned electricity network assets in the NWIS;
6. technical standards should not present a physical constraint to potential future interconnection of the NWIS, or a barrier to any technology type; and
7. the effectiveness of the ISO should be reviewed periodically.

Alinta supports the design principles outlined above.

4.3 ISO functions

Design Element 21

The ISO will undertake planning, scheduling and dispatch services for the NWIS interconnected network and will:

- develop and manage a full NWIS simulation model.
- have lead accountability for managing emergency response and post-incident investigations.

For a small market like the NWIS it's appropriate the ISO should have a limited role. Alinta supports the ISO dispatching electricity during emergency and contingency events only.

However, it's important to note that even in these circumstances contractual rights of customers must be respected. For example:

- there are priority rights of customers which must be factored into the ISO's decisions about dispatching electricity; and
- electricity dispatch by an ISO is not contemplated in supply agreements between participants of the NWIS. Therefore, adjustments to contracts must be made to give rights to the ISO.

Design Element 22

The ISO will take over the role of procuring and allocating the costs associated with the following Ancillary Services: frequency control, spinning reserve, balancing & settlements, reserve capacity, and black start capability.

Alinta has concerns about the central procurement of ancillary services due to networks needing to have their own ancillary services available when their network is disconnected or islanded.

Alinta supports the National Electricity Market model where each network is responsible for their own ancillary services procurement.

Design Element 23

The ISO will provide the following Network Services for the NWIS in conjunction with Network Owners, Generators, and End Customers: network coordination, technical oversight of connections and access, and publication of statements of transmission development and generation opportunities (whilst protecting commercially sensitive information)

The Horizon Power ISO+ model, including the proposed system operator's role in providing network transport services will be reviewed once the proposed ISO functions have been implemented and tested in practice.

Alinta does not support the ISO+ model being introduced or investigated.

Further, Alinta supports a limited role for the ISO and believes moving to central dispatch in the future would be unwarranted for the size of the NWIS and number of participants. Alinta supports maintaining the bilateral contract dispatch model indefinitely.

Design Element 24

The ISO will at initiation provide limited Market Services, with economic dispatch of generation unlikely to be justified in the NWIS for the foreseeable future. The ISO needs to be provided with an ability to cover its NWIS-related administrative costs and the costs of any Market Services that it provides.

Alinta supports the ISO having a limited role with its costs being recovered from market participants over time.

Design Element 25

With the recommended functions of the ISO in this document, the ISO will need to be regarded in the *Electricity Industry (Metering) Code 2012* as the equivalent of the Independent Market Operator/AEMO for the NWIS with similar rights, obligations and responsibilities. The ISO is not initially positioned as a Metering Services provider.

Alinta agrees with Design Element 25.

Design Element 26

The ISO will have sufficient powers to effectively enact its obligations and undertake its functions. The powers of the ISO will not extend to daily operational control of interconnected networks in NWIS unless such control is transferred to the ISO by agreement.

Alinta agrees Design Element 26 is important for the efficient operation of the NWIS.

4.4 ISO structure and operating cost

Design Element 27

The ISO will be a stand-alone entity, with the proposed functions undertaken by AEMO as an extension of its current Western Australian operations, noting that it may choose to contract with other network service providers for provision of some services.

Alinta supports Design Element 27.

Design Element 28

The ISO's annual revenue and capital expenditure forecast will be independently approved by the ERA.

Alinta agrees the ERA is well placed to assess the ISO's costs and that it's important the ERA consults with industry participants before making a determination in this regard.

Design Element 29

The ISO capital and operating costs will be recovered from market participants.

Alinta agrees the ISO costs should be recovered from market participants over time, but further work needs to be done in consultation with industry to determine the appropriate methodology.

Whatever methodology is adopted, it's important the scope and role of the ISO is limited to keep these costs to a minimum.

Design Element 30

The ISO will be governed by the AEMO Board on the basis that AEMO undertakes the ISO role for the NWIS. Its charter will be established with the involvement of key stakeholders.

Alinta supports Design Element 30.

Design Element 31

The ISO surveillance functions will be provided to the ISO governing body by the ERA.

Alinta supports Design Element 31.

Design Element 32

Changes to the NWIS Rules will be a service provided to the ISO governing body by the ERA.

Alinta supports Design Element 32 which ensures no conflict of interest between the body making and implementing the rules.

4.5 Coverage and liability

Design Element 33

The ISO will have coverage of the entire NWIS Interconnected System, with powers limited to those necessary to undertake its assigned functions consistent with the design objective.

For the avoidance of doubt, the ISO will not have powers to interfere with the efficient operations of networks, other than to protect the security and reliability of the NWIS and these powers do not necessarily require direct control of all network elements.

Any changes to the powers of the ISO will be subject to rigorous analysis with stakeholder input to ensure that there is a material net benefit of any proposed changes.

Alinta supports Design Element 33.

Design Element 34

The ISO will have the same immunity from damages claims as AEMO has for its operations in the SWIS.

Alinta supports Design Element 34.

4.6 Transition process

Design Element 35

Transitioning to the new ISO will allow timelines that permit the ISO and participants to efficiently meet new obligations and functions and for stakeholder participation in the development of the various design elements.

Alinta agrees with this design element however notes the complexity and time involved in establishing the ISO which is different to that involved in establishing open access.

To ensure that Pilbara electricity customers see the benefits of competition as soon as possible, access processes / negotiations should be able begin before the ISO is fully established.

5 Conclusion

Alinta welcomes and supports changes to the NWIS regulatory framework to allow the benefits from a non-discriminatory open access regime to be realised by participants and customers of the NWIS as soon as possible.

Access to the Horizon Network will unlock significant benefits to Pilbara customers and the region more broadly.

In this regard Alinta supports the development of a light-handed access regime which maximises net benefits.

Alinta is committed to doing what it can to ensure the light-handed framework is established in the NWIS in a timely manner and, in that respect, is open to including its DEWAP infrastructure. That being said, Alinta is not convinced that there is a clear net benefit from doing so.

Alinta looks forward to the light-handed regime being operational as soon as is practically possible and believes all industry participants, including government, must work together in good faith to ensure its swift and effective implementation so customers can start to realise the benefits that competition unlocks.

Alinta looks forward to continuing to work with the PUO, and other stakeholders, in developing a fit-for-purpose regulatory model which recognises the unique characteristics of the NWIS including the size, composition and maturity while providing sufficient regulatory oversight, which will in turn lead to an optimal and efficient outcome for the NWIS.

Please contact me on Jacinda.Papps@alintaenergy.com.au or 08 9486 3009 if you have any queries in relation to this submission.

Yours Sincerely

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