

**STANDING COMMITTEE ON
ESTIMATES AND FINANCIAL OPERATIONS**

ONGOING BUDGET ESTIMATES HEARINGS 2010–11

**TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
WEDNESDAY, 7 JULY 2010**

SESSION SIX

Members

**Hon Giz Watson (Chair)
Hon Philip Gardiner (Deputy Chair)
Hon Liz Behjat
Hon Ken Travers
Hon Ljiljanna Ravlich**

Hearing commenced at 4.42 pm**COLLIER, HON PETER****Minister for Energy,****sworn and examined:****DAWSON, MR ALLAN****Chief Executive Officer, Independent Market Operator,****sworn and examined:****CRIBB, MR MURRAY****Manager, Finance and Administration, Independent Market Operator,****sworn and examined:**

The DEPUTY CHAIR: Welcome to the committee hearing. Before we begin, I must administer the oath or affirmation. I ask you to indicate to the committee clerk whether you prefer to take the oath or affirmation.

[Witnesses took the oath or affirmation.]

The DEPUTY CHAIR: You will have signed a document entitled “Information for Witnesses”. Have you read and understood that document?

The Witnesses: Yes.

The DEPUTY CHAIR: These proceedings are being recorded by Hansard. The transcript of your evidence will be provided to you. To assist the committee and Hansard, please quote the full title of any document you refer to during the course of this hearing for the record and please be aware of the microphones and try to talk into them. Ensure that you do not cover them with papers or make noise near them and try to speak in turn. I remind you that your transcript will become a matter for the public record. If for some reason you wish to make a confidential statement during today’s proceedings, you should request that the evidence be taken in closed session. If the committee grants your request, any public and media in attendance will be excluded from the meeting. Please note that the uncorrected transcript should not be published or disclosed. This prohibition does not, however, prevent you from discussing your public evidence generally once you leave this hearing. Government agencies and departments have an important role and duty in assisting Parliament to scrutinise the budget papers on behalf of the people of Western Australia, and the committee values your assistance in this.

Members, it will assist greatly Hansard if, when referring to the budget statement volumes or the consolidated fund estimates, you please give the page number, item, program, amount and so on in preface to your questions.

Hon KATE DOUST: I refer to page 593 of budget paper No 2. I have a series of questions on the expenditure of 2010–11 and future years to upgrade and enhance the wholesale electricity market. What upgrades are planned and what is their cost?

Mr Dawson: Currently, we are reviewing the market design for the market. The costs included in the budget are an estimate of the costs to upgrade and maintain the current systems. However, we are currently evaluating the current market design and will make a decision at some point about whether we will move to a different market design. Those costs are not included in the budget simply because we have not yet determined what those costs will be.

Hon KATE DOUST: Has the IMO consulted market participants regarding the proposed changes?

Mr Dawson: At length.

Hon KATE DOUST: I imagine you have. What benefits do you think those upgrades will have?

Mr Dawson: We will try to define a broad cost benefit for a market advisory committee meeting that will occur on the nineteenth of this month. Those papers will be provided on the IMO website one week before that meeting. It is envisaged that any move to what has been described as a mature market model would have to be associated with a comprehensive cost-benefit analysis that would support a decision to move to that. We expect that to take somewhere in the region of nine to 12 months to complete once a decision on the appropriate pathway is made.

[4.47 pm]

Hon KATE DOUST: How do you see the wholesale electricity market functioning in Western Australia as a whole?

Mr Dawson: I think the wholesale electricity market in Western Australia was designed, firstly, as an interim step towards reform. I was not here at the time; I am assuming that. It was certainly designed to encourage private sector investment in the wholesale electricity and generation sector, which it has done. It has also incentivised quite a lot of innovation as far as demand side management and generation upgrades.

Hon KATE DOUST: Coming back to that budget paper and looking at the area funded by—it has got borrowings there—I notice that the IMO funding over the next few years is to be funded by borrowings. Does the IMO have any current debt, and what is it; and how is the IMO funded other than through borrowings?

Mr Dawson: Can we take the borrowings amount on notice? Is that okay?

Hon KATE DOUST: Absolutely, yes.

Mr Dawson: The other funding that we receive—clearly, the state is not burdened by the costs of the IMO; we actually levy market participants per megawatt-hour traded through the market. That budget is, firstly we get a three-year allowable revenue approval from the Economic Regulation Authority, which we have just undertaken for a three-year period. Then, annually, a market budget, and the IMO budget is submitted to the minister for approval and is published, and that forms the basis of our market fees. Those market participants participate in the consultation around all of those documents, including the three-year revenue allowance.

Hon PETER COLLIER: That is all recurrent funding; it comes from those market fees and the participants.

The DEPUTY CHAIR: F1: details of the borrowings.

[*Supplementary Information No F1.*]

Hon KATE DOUST: One of your major reports that is undertaken is your statement of opportunities, which is prepared under clause 4.1.8 of the Wholesale Electricity Market Rules—I must say, you are always very timely with getting that report in, minister; others could learn. The most recent 2010 document states —

... there appears to be more than sufficient potential new generation and DSM to meet the 8 MW identified as additional capacity required for 2012/13.

What does the IMO expect this demand side management to entail?

Mr Dawson: The demand side management area of the market has been a significant development over the last two or three years. We have seen the entry of two dedicated demand side managers into the Western Australian market; they are Energy Response and a company called DMTenergy. We are now seeing interest from an American demand side manager called ENOC, which has

expressed interest in joining our market as well. Demand side management is seen as quite a significant area of innovation for the market.

Hon KATE DOUST: I might just get you to explain what demand side management is.

Mr Dawson: Demand side management is turning off consumption, when it is required, at peak periods. There is very sophisticated technology now that can manage smaller industrial users' load, and can turn off non-essential consumption during periods of peak, and that would be dispatched on the orders or on the request of our system manager here.

Hon KATE DOUST: In relation to this, what will be the impact of the 330kV project stage 1 from Neerabup to Eneabba being delayed to the energy requirement of the SWIS? This is relating back to your statement of opportunities.

Mr Dawson: In our load forecasting we identified a number of larger loads—mining loads—that may be potentially impacted by not being able to connect to the transmission network. It has been anecdotally suggested to us that there are potentially some wind assets up there that would be affected by this transmission network not being connected. But the predominant effect on the statement of opportunity is the reduction in load in our forecast that would not be able to be connected if that extension is not there on time.

Hon KATE DOUST: I suppose the same reply then for the stage 2 being delayed, in terms of Eneabba to just before Geraldton, and its impact on capacity for that area up there.

Mr Dawson: We just evaluated it for the year that we did it. We had to make a determination whether it would be there for that capacity year, or whether it would be there in later capacity years. We just made that determination for the year that we were evaluating.

Hon KATE DOUST: My other question in terms of 330kV lines is: I think in earlier statements you had looked at the 330kV line from Collie to Perth and how that would impact on future capacity. Now that that 330kV line is not being progressed, has the IMO had the opportunity to look at how that will impact on future capacity?

Mr Dawson: No, we have not.

Hon KATE DOUST: The only other thing I was going to ask about was, you have already talked about the vesting contract and market rule changes, and I imagine that is something that we will look at in a few months' time. Earlier today there was some discussion about the gas bulletin board, and given the nature of the work that the IMO currently does, I would have thought this would have fitted in very well with where you are at. If the IMO was to be successful in obtaining the management of that board, what changes would that require in your office, if any?

Mr Dawson: We are currently evaluating that and submitting our proposal to the Office of Energy by Friday of this week. We would envisage, depending on the design—currently the Office of Energy has commissioned a consultant to look at what would go on a gas bulletin board and what would go on a gas statement of opportunity, and those recommendations and the adoption of those recommendations will influence significantly the impact on the IMO with regard to resources and systems and investments. The gas emergency management committee did suggest, I think, in its recommendations that a gas bulletin board may be secured from AIMO, for instance, and if that was the design that was adopted then the capital cost would be significantly less than if Western Australia built its own bulletin board. So there are some pretty key decisions that need to be made on what is included in it before we can really determine what impact it will have.

Hon LJILJANNA RAVLICH: I do not really know much about this subject at all, so I hope you can help me through it, Mr Dawson. In terms of the role of the independent market operator, is it predominantly concerned about the wholesale electricity market, or is it also concerned about other aspects of the energy market?

Mr Dawson: It administers and operates the wholesale electricity market.

Hon LJILJANNA RAVLICH: Is it just the wholesale electricity market?

Mr Dawson: Yes.

Hon LJILJANNA RAVLICH: Can you advise what the current size of this market is at the moment, and do you keep records of that?

Mr Dawson: The market itself is based around bilateral contract submission. The total size of wholesale electricity traded in Western Australia in the SWIS, which is where we administer our market, is 17 000 gigawatt hours. The level of electricity that is traded through the markets that we administer is approximately 10 per cent of that volume.

Hon LJILJANNA RAVLICH: I am assuming that that is an increase on perhaps where it was a couple of years ago, so you have actually got a growing market—is that correct?

Mr Dawson: Look, I think the market in Western Australia—electricity demand goes up with economic growth. Western Australia's economic growth has been pretty prodigious over the last five years. We are seeing energy growth growing in line with economic growth; however, our peak load in Western Australia continues to grow at a rate higher than energy growth.

Hon LJILJANNA RAVLICH: Why is that? Is that because of the demand from heavy industry, from the mining sector?

Mr Dawson: I actually think that they usually take load consistently. Peak load is largely driven by —

Hon LJILJANNA RAVLICH: Cold snaps?

Mr Dawson: — discretionary electricity consumption, air-conditioning. Wealth tends to prompt peak load growth.

Hon PETER COLLIER: There has been a significant increase in electricity air-conditioning uptake.

Hon LJILJANNA RAVLICH: In terms of reverse cycle air-conditioning?

Hon PETER COLLIER: A combination, yes.

Hon LJILJANNA RAVLICH: Would you know how many competitors there are in this market?

Mr Dawson: We know how many registered participants there are.

Hon LJILJANNA RAVLICH: Okay.

Mr Dawson: This is approximate, so I do not know exact the number—I can take it on notice. There are approximately 27 generator market participants, and there are somewhere in the region of 20 retail, or market customer, market participants. It is quite a little vibrant market with lots of new entry.

The DEPUTY CHAIR: Do you need to have that information, or is that sufficient for you?

Hon LJILJANNA RAVLICH: It would be good if we could get some trend data over the last two or three financial years in terms of how this market has been growing, if you like.

The DEPUTY CHAIR: Can you do that?

Mr Dawson: I can provide the number of market participants trends over the last five years.

The DEPUTY CHAIR: That would be very helpful; thank you.

[Supplementary Information No F2.]

Hon LJILJANNA RAVLICH: Usually markets just operate, sort of, on their own with information and all the characteristics of a market, but it seems like you have got this very unusual role where you are almost setting up the market and making sure that everything works as it is

supposed to during an infancy stage. I do not know what happens in the longer run, whether you will still have an ongoing role in it or it just continues to be.

[5.00 pm]

Mr Dawson: Typically, while electricity markets are established to encourage investment from whatever sector comes in, one of the aspects of an electricity market is that it needs someone to coordinate the input. That typically requires either a market operator or a system manager. We have both in Western Australia. My understanding of electricity markets suggests you will always need those to coordinate because everyone wants their lights on when they want them on. That coordination occurs to some extent 24 hours a day, seven days a week.

Hon LJILJANNA RAVLICH: Is the price of electricity in the wholesale electricity market determined by supply and demand or are there some other interfering factors?

Mr Dawson: It is.

Hon LJILJANNA RAVLICH: Solely on supply and demand?

Mr Dawson: There is a supply and demand for energy that establishes the price for it every half hour.

Hon KEN TRAVERS: In your operational plan for 2009–10 your estimated total budgeted expenditure was \$11.5 million. But your website talks about your system management budget. I am trying to understand the difference. In your budget there is only \$6.6 million. Can you explain to me what the difference is? Is it because you are spending less money this year or does the system management budget not cover something that is covered in your operational plan budget?

Mr Dawson: It is not our budget. We are required to set a market fee, and that includes our costs. It includes a ring-fenced department in Western Power called system management. That is Western Power's costs. It also includes an element of Economic Regulation Authority costs. The market fee includes three costs from three separate agencies. That is what I think you were referring to from our website.

Hon KEN TRAVERS: Is that the system management budget?

Mr Dawson: The system management budget is the one from Western Power.

Hon KEN TRAVERS: That is separate from your own budget?

Mr Dawson: It is.

Hon KEN TRAVERS: What is your budgeted expenditure for the IMO in the financial year?

Mr Cribb: The total budget expenditure for the year 2010–11 is \$11.791 million. That includes special project funding of \$869 000. The budget for normal operations is \$10.922 million.

Hon KEN TRAVERS: Does that include the money we just talked about for the system operation?

Mr Cribb: No, it does not; it is purely the IMO.

Hon KEN TRAVERS: How does that \$11 million break up in your functional areas—market administration and market operation system capacity?

Mr Cribb: It is broken into three components. The market administration component is \$2.016 million. The market operation is \$7.058 million, and system planning is \$1.848 million.

Hon KEN TRAVERS: There seems to be some reasonably significant shifts from last year's budget in that regard. Market administration was going to be \$3 million last year and market operation \$6.5 million. What has caused the change?

Mr Cribb: We would need to go back and look at the underlying contributing factors for those. It is probably to do with some internal restructuring around some of those operations. We have

transferred functions between some of those areas, which maybe influencing some of those changes. But we can take that on notice and provide some information.

Hon KEN TRAVERS: If you could.

[Supplementary Information No F3.]

Hon KEN TRAVERS: Is it correct that part of the fees you collect go to the ERA?

Mr Dawson: We collect fees on behalf of the ERA through out settlement function, yes.

Hon KEN TRAVERS: Does the ERA approve the fees you charge for your budget? I am trying to see the link between the two organisations.

Mr Dawson: Every three years the ERA reviews an allowable revenue submission that we make to the ERA. It approves a financial envelope for our operation for the next three years. That basis of funding and budgeting is then used to establish an annual budget, which is submitted to the minister's office for approval. Once approval has been received from the minister for the annual budget, which needs to be consistent with the ERA allowable revenue approvals, we then submit the fees to the market participants. The ERA approves for three years and we prepare an annual budget for the minister's office

Hon KEN TRAVERS: When is that three-year cycle due?

Mr Dawson: It has just been completed for the next three years. The first three-year cycle ended on 30 June and the new three-year cycle starts on 1 July.

Hon KEN TRAVERS: Are its current approvals publicly available?

Mr Dawson: They are available on the ERA website with all the submissions from market participants on those.

Hon KEN TRAVERS: I want to make sure I understand this correctly. The ERA approve the general revenue you can charge. So, it basically approves your income side of it, and you fix your budget to meet your expenditure to meet what they have approved to collect as fees from the market. Is that correct?

Mr Dawson: We establish a budget.

Hon KEN TRAVERS: The ERA bases what it allows you to charge on what it thinks you need, but ultimately it approves how much you can collect rather than how much you spend?

Mr Dawson: That can vary annually in the annual budget submission process to the minister. If, for instance, a special project came up, we could vary that allowable revenue amount by, I think, up to 15 per cent. We do not, but we have submitted special project funding to the minister for approval, and he has approved that in the past, which has allowed us to do some work that our participants have asked us to do.

Hon KEN TRAVERS: You can go up to 15 per cent over what the ERA has approved?

Mr Dawson: Yes.

Hon KEN TRAVERS: Within that, you still collect fees on behalf of the ERA that fund the ERA.

Mr Cribb: That component that relates to the ERA's budget, which is a small component, is separately approved by the Treasurer.

Hon KEN TRAVERS: The Treasurer is the only person who sets the amount of money you can collect to fund the ERA?

Mr Cribb: The Treasurer approves it.

Hon KEN TRAVERS: There is no other approval process?

Mr Dawson: We are not the ERA. The ERA submits it to us. We collect it simply because we administer settlement in the electricity market. We collect on behalf of system management and the ERA as a consequence of just administering the settlement. That part of our function is to make sure everyone gets paid, and part of the requirements under the rules is to make sure the system management and the ERA's function that support the electricity market are paid for by the participants.

The DEPUTY CHAIR: You talked about the wholesale electricity market in terms of increasing the private sector of the market and the innovation that resulted from the system you were developing. In a number of budget papers there is an item called "Key Performance Indicators", which is not in your state budget papers. In terms of innovation, can you indicate to me what are the most fruitful innovative outcomes as a result of the system you are structuring for the wholesale electricity market?

Mr Dawson: I think the emergence of demand-side management is a key efficiency. The emergence of demand-side management and the technology that allows this energy management to be dispatched saves Western Australia from building, I think at the end of this capacity year, the equivalent of a Collie power station. It is that level of despatchable capacity that it has saved the state from. That is a very significant cost saving.

The DEPUTY CHAIR: I would have thought that should be in the budget papers as a key performance outcome.

Mr Dawson: We do offer key performance indicators in our operational plan. Because we borrow only from WATC, that is the only piece of the submission into the budget process.

The DEPUTY CHAIR: I understand. But if the design is structured for that kind of outcome, it is a very big saving for the state. I agree. I would have thought that value was worth being in the budget papers.

In terms of our system compared to the eastern states network system, does it already have the level of innovation about which you are talking?

Mr Dawson: The NEM has a different structure; it does not have a capacity market. We have a capacity market in the west, which is designed specifically to incentivise the entry of new capacity. The NEM relies on an energy only price. We pay people to come and bring their capacity. That underwrites this innovation. The NEM does not recognise demand-side management as a source of capacity in its market.

The DEPUTY CHAIR: That is the distinction between the national electricity market and our market?

Mr Dawson: It is one of the distinctions, yes.

Hon PETER COLLIER: There are several others.

The DEPUTY CHAIR: You mentioned the private sector segment of that system. Is that where you describe the 27 registered participants? That is what you mean by the private sector. Can you explain in practical terms how each of those private operators work?

Mr Dawson: Some of them are as small as a landfill gas site. We have in this state people who tap into landfill gas sites and refuse places and generate electricity from them. There is a dedicated company that does that. In that 27 is Verve, our biggest state utility, and Alinta, the gas utility, also a generator in our market, and there is Griffin. Wind farms are included in the 27. Emu Downs Wind Farm is a market participant in its own right. Every one of those is included in the 27—from the very small up to quite significant utilities.

Hon LJILJANNA RAVLICH: Can we get a list of those 27 please?

Hon PETER COLLIER: I think we have already agreed to that.

The DEPUTY CHAIR: Yes; we have. It is supplementary information No F2.

Hon LJILJANNA RAVLICH: Sorry; my mistake.

The DEPUTY CHAIR: If biomass pyrolysis plants were being considered for the Wheatbelt and so on, would the proponent come to you to talk about what it is proposing to do in terms of feeding energy into the system or would the proponent go to Verve or others?

Mr Dawson: We are typically the first port of call for new investors in the state seeking entry. Firstly, we would not naturally buy from them. They would have to find a customer for that energy. They would typically talk to retailers, and there are a number of retailers active in the state. They would have to find connection to the grid and they would have to talk to Western Power and get emissions EPA. Typically, they come to us and we tell them what they have to do to start their business.

[5.15 pm]

Hon PETER COLLIER: That comes back to the point I made earlier with regard to the notion that there is a lot of innovation and a lot of enthusiasm with regard to the energy sector, particularly in the renewable component. But there are a lot of dots to join, particularly off-take agreements and whether they have access to the network and whatever. But it is not as simple as just building a biomass plant assuming you can feed into the grid.

Hon KEN TRAVERS: The first point of call for anyone who is considering this who has some technology advancement would be to come to see your office first and you could guide them about how to feed into the system?

Mr Dawson: We see that as one of our key roles—almost like a business development role. New developers eventually get to us anyway and we are very happy to help them. We are neutral, so we can direct them and try to assist them to enter the market. It has worked very well for a number of developers.

The DEPUTY CHAIR: We discussed this in answer to a question I asked earlier. For example, I know there are some solar projects engaged in seeking funds from the commonwealth in the last round. Were you involved in making any support or helping to structure their applications?

Mr Dawson: They did not ask us. I am aware of them. They came and talked to us about it. They have not asked us for support. I imagine in their business case, the revenues they would have through the market for capacity provision, for instance, would have been included in that and my team would have helped assist them with those revenue estimates.

Hon KEN TRAVERS: Have you agreed to the operational plan for 2010-11 yet, with the minister?

Mr Dawson: We have submitted it to the minister for approval

Hon KEN TRAVERS: Has it been agreed?

Mr Dawson: Not at this stage.

Hon PETER COLLIER: No; it has not.

Hon KEN TRAVERS: Under the electricity industry independent market operator regulations, how long do you have from the time you submit it to the minister approving the operational plan? My recollection is that it might be 30 business days.

Mr Dawson: I would have to take that on notice. I do not have the regulations here

Hon KEN TRAVERS: Do you know what date you submitted it?

Mr Dawson: We are required, I think, under the regulations, to submit it on 30 April.

Hon KEN TRAVERS: According to your 2009-10 operational plan, you were required to submit it on 30 April and the minister is required to approve the operational plan within 30 business days. I

would have thought we had gone well past the 30 business days since 30 April. Is there a reason it has not been agreed to, minister - just laziness, slackness?

Hon PETER COLLIER: No; I cannot comment.

Hon KEN TRAVERS: Why can you not comment; you are the one who has to agree to it.

Hon PETER COLLIER: Precisely. But, with all due respect, I will take it on notice and get back to you. There must be a reason.

[Supplementary Information No F4.]

Hon KEN TRAVERS: Seriously, something like that when you have an obligation under the legislation.

Hon PETER COLLIER: You are making it out to be a clandestine thing that has not happened. I gave you a very real reason with regard to Western Power as to why that happened.

Hon KEN TRAVERS: We did not accept, it but you tried.

Hon PETER COLLIER: It was true; it was a good point. I am not sure with regard to the operational plan. I will go back and check and let you know.

The DEPUTY CHAIR: We will wait for the response.

Mr Cribb: It runs to a fairly tight time frame in that one of the requirements is that it needs to have the Treasurer's concurrence as well.

Hon KEN TRAVERS: It is impossible to get that, is it not minister?

Hon PETER COLLIER: I suggest that problem is the reason for considering the changeover in Treasury.

Hon KATE DOUST: With all due respect, it is not possibly the reason, you as the minister should know exactly where that is at.

Hon PETER COLLIER: I have given a commitment to get back to you.

The DEPUTY CHAIR: I think we have got the response. I do not think the minister can give any further information.

Hon KEN TRAVERS: I think there is a further question. We are sitting here and having a budget hearing. We are unable to know the operational plan, which would be significant in terms of what the forward year's program is. I would like to know whether it is because you do not have the concurrence of the Treasurer. I would also like an explanation about what is the problem between the minister and his agency and the Treasurer; the reason why you have not been able to get the concurrence of the Treasurer

Hon PETER COLLIER: I assume it is because we do not have the concurrence of the Treasurer, but I cannot verify that. I will find out why and get back to the committee.

The DEPUTY CHAIR: Any other questions? That probably concludes the hearing and reflects for most of us if not all of us an area we did not know a great deal about. Thank you for elucidating us on a substantial part of that. The committee will forward any additional questions it has to you via the minister in writing in the next couple of days, together with a transcript of evidence, which includes the questions you have taken on notice. If members have any unasked questions, I ask them to submit these to the committee clerk at the close of this hearing. Responses to these questions will be requested within 10 working days of receipt of the questions. Should the agency be unable to meet this due date, please advise the committee in writing as soon as possible before the due date. The advice is to include specific reasons as to why the due date cannot be met. On behalf of the committee, thank you very much for your time and attendance. On behalf of the committee I thank the minister for a long day in the chair.

Hon PETER COLLIER: A pleasure.

The DEPUTY CHAIR: I also thank our participating member who has been here under some pain with a heavy cold for the whole day.

Hearing concluded at 5.21 pm