

# Draft decision: Multinet Gas 2018–22

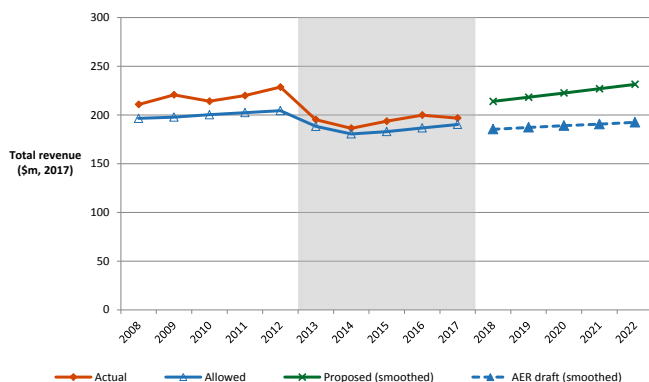
## Overview

The Australian Energy Regulator (AER) approves access arrangements for Multinet Gas (Multinet) and other major gas networks in most of Australia under the National Gas Law (NGL) and National Gas Rules (NGR). Multinet is the owner and operator of a gas distribution pipeline servicing customers in Victoria.

Our draft decision allows Multinet to recover \$1016.7 million (\$nominal) from its customers over five years commencing 1 January 2018. In real dollar terms, the revenue we have allowed for 2018 will be 5.8 per cent less than Multinet's actual revenue in 2017. In 2022, allowed revenue will be 2.2 per cent less in real dollar terms than Multinet's actual 2017 revenue.

The figure below shows the difference between Multinet's proposed revenue, and what we have allowed for each year of the access arrangement period.

### Multinet's past and proposed total revenue and AER draft decision revenue allowance (\$million, 2017)



The revenue we determine affects the distribution component of a customer's gas bill. For customers on Multinet's network, distribution charges account for approximately 19 per cent of an average residential customer's annual gas bill and approximately 11 per cent of an average small business customer's annual gas bill.

Other components of customer bills include the cost of sourcing the gas, transmission network charges and retailer costs. The AER does not set retail prices.

### Estimated impact on customer bills

If implemented, we expect that our draft decision will result in the distribution component of the average annual residential gas bills for Multinet customers rising over the 2018–22 access arrangement period.

The distribution component of the average annual residential gas bill in 2018 is expected to be about \$9 (nominal) below the current, 2017 level. By the end of the 2018–22 access arrangement period, the distribution component of the average annual bill is expected to be about \$38 above the current level.

The distribution component of the average annual small business gas bill in 2018 is expected to be about \$18 (nominal) lower than in 2017, and about \$75 above the current 2017 level by 2022.

### Key elements of our decision

We based our assessment of Multinet's proposed revenue on a number of components. These include expenditures to maintain and operate the pipeline, and the return to shareholders on their investment. Together, these determine the revenue that Multinet may recover from its customers.

There are two components of our draft decision that drive most of the difference between the revenue that Multinet was allowed to recover in the 2013–17 access arrangement period, and the level of revenue approved for the 2018–22 access arrangement period: rate of return, and operating expenditure. We discuss each of these below. We also discuss the key differences between our draft decision and Multinet's proposal.

### Rate of return

Significant investment is required to build a distribution pipeline. The return that Multinet must pay lenders and investors is referred to as the rate of return. Even a small difference in the rate of return can have a big impact on revenues.

Our draft decision sets the allowed rate of return (or 'cost of capital') at 5.75 per cent for 2017–18. This is a significant decrease compared to the rate of return approved in our previous (March 2013) final decision for Multinet of 7.03 per

cent.

The investment environment has improved since our previous decision, which was made during the period of uncertainty surrounding the global financial crisis. This improved investment environment translates to lower financing costs necessary to attract efficient investment.

The lower rate of return in this draft decision will reduce Multinet's average annual revenue requirement compared to the previous access arrangement period.

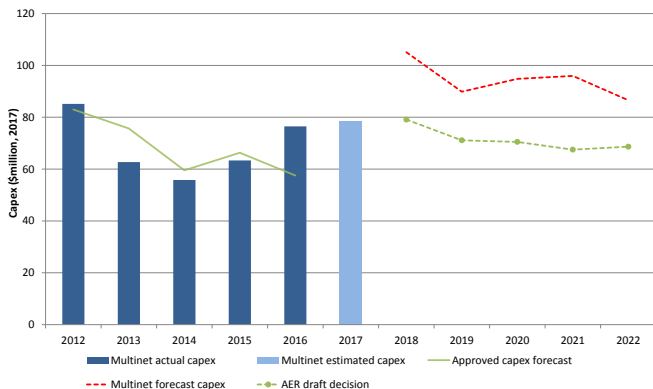
### Capital expenditure

Our draft decision approves total forecast capex of \$356.9 million (\$2017). This is around 24 per cent less than Multinet proposed, and closer to its current period expenditure. Most of the difference between our draft decision and Multinet's proposal relates to forecast capex for mains replacement.

Multinet's forecast mains replacement capex made up around 49 per cent of its total forecast gross capex. Its proposed expenditure of \$249.7 million was \$118 million higher than its actual mains replacement expenditure in the current period. On the information before us we are not satisfied that this increase in mains replacement expenditure is justified. In particular, the proposed forecast volume of mains to be replaced exceeds that required to minimise risks of leaks and improve network safety. The total capex forecast in our draft decision includes a lower mains replacement forecast of \$159.5 million, which is based on Multinet's historical annual replacement rates and the leak data provided by Multinet.

The figure below compares Multinet's past and proposed forecast capex, and the forecasts approved by us in our 2013–17 final decision and this draft decision for 2018–22.

### AER draft decision compared to Multinet's past and proposed capex (\$million, 2017)



### Operating expenditure

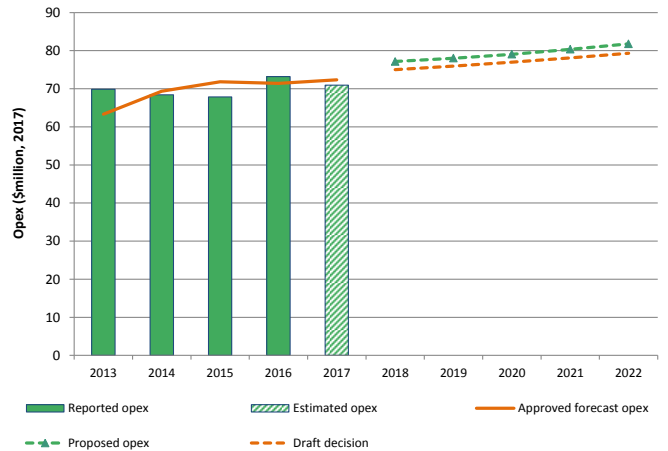
Opex includes forecast operating, maintenance and other non-capital costs incurred in the provision of distribution network services. It includes labor costs and other non-capital costs that Multinet is likely to require during the access arrangement period for the efficient operation of its network.

Our draft decision approves total forecast opex \$385.1 million (\$2017). This is a reduction of 2.8 per cent from Multinet's proposal. The main difference between our approved forecast and Multinet's proposal is that we have not approved its proposed step change for marketing. We consider marketing is a 'business-as-usual' expense for Multinet to prioritise within its existing base opex forecast, if it is prudent and efficient to

do so in the current operating environment.

The figure below shows our draft decision and Multinet's proposal in the context of its past allowances and actual expenditure.

### Our draft decision compared to Multinet's past and proposed opex (\$ million, 2017)



The increase in opex from the current period to the forecast for this draft decision reflects growth in Multinet's customer numbers and changes in its operating costs over time.

### Demand

Tariff levels depend on estimates of forecast total demand (GJ/day). In simple terms, tariffs are determined by dividing cost by total demand (GJ/day), such that an increase in forecast demand has the effect of reducing tariffs and vice versa.

Our draft decision is based on:

- a decrease in total residential gas demand of 1.2 per cent per year compared with 1 per cent per year in current period
- a decrease in total small commercial demand of 2.7 per cent per year compared with 2.5 per cent per year in current period
- a decrease in industrial demand of 1.9 per cent per year compared with 0.5 per cent in the current period.

### More information about our consultation process

Multinet will submit a revised proposal in response to this draft decision by 14 August 2017. Interested parties are invited to make submissions on both our draft decision and Multinet's revised proposal by 15 September 2017. More information on Multinet's proposal, our draft decision and how to make a submission is on our website: [www.aer.gov.au](http://www.aer.gov.au).