



FINAL DECISION
Australian Gas Networks (SA)
Access Arrangement

2021 to 2026

Attachment 13
Capital expenditure sharing
scheme

April 2021

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Note

This attachment forms part of the AER's final decision on the access arrangement that will apply to Australian Gas Networks (SA) ('AGN') for the 2021–26 access arrangement period. It should be read with all other parts of the final decision.

The final decision includes the following documents:

Overview

Attachment 2 – Capital base

Attachment 3 – Rate of return

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency carryover mechanism

Attachment 11 – Non-tariff components

Attachment 12 – Demand

Attachment 13 – Capital expenditure sharing scheme

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13 Capital expenditure sharing scheme

This attachment outlines our assessment of AGN's proposal for a capital expenditure sharing scheme (CESS) for the 2021–26 access arrangement period.

As the CESS is new for AGN, it will not impact revenues in the upcoming access arrangement period, but rather, future access arrangement periods. Consequently, our final decision relates to the design of the scheme.

In its initial proposal, the design of AGN's proposed CESS was based on the CESS previously approved for AGN's Victorian gas network. This deviates somewhat from the more recently approved CESS for JGN NSW, which excluded connections capital expenditure (capex).

In its revised proposal, AGN has amended its proposed CESS to exclude connections capex and updated its performance targets based on corrected calculations.

13.1 Final decision

Our final decision approves the application of a CESS in AGN's 2021–26 access arrangement period and the associated amendments in its revised proposal. This will be the first time that a CESS applies to AGN's South Australian gas network in an access arrangement.

13.2 AGN's revised proposal

In its revised proposal, AGN made the following amendments to its access arrangement in accordance to our draft decision:¹

- remove the expenditures related to connecting customers from the annual efficiency gain or loss under the scheme
- change its Unplanned SAIDI target from 314.97 to 307.04.

13.3 Assessment approach

Our assessment approach is the same as the draft decision.²

13.3.1 Interrelationships

The incentive scheme AGN proposes relates to various areas of the business covered by the 2021–26 access arrangement. For example, the introduction of a CESS may affect the size of the capital base (as it provides an incentive for service providers to

¹ AGN, *Access Arrangement for South Australia Gas Distribution Network 2021-2026 – MARKED UP*, January 2021, pp. 22, 64.

² AER, *Australian Gas Networks access arrangement 2021–26, Attachment 13 - Capital expenditure sharing scheme*, November 2020, p. 4.

reduce their capex, where such reductions will not reduce their service standard) and may alter the balance of investment signals between operating expenditure (opex) and capex. We aim to incentivise service providers, such as AGN, to make efficient decisions on when and what type of expenditure to incur, and to balance expenditure efficiencies with service standards.

13.3.2 Stakeholders

The South Australian Minister for Energy and Mining noted the government supports the AER's draft decision to introduce a CESS that excludes expenditure on new connections.³

13.4 Reasons for final decision

13.4.1 Exclusion of new connections capex from CESS targets

Consistent with our recent JGN NSW decision, and our draft decision for AGN, we consider connections capex should be excluded from the CESS.

We consider excluding new connections capex from the CESS better achieves the revenue and pricing principles of the NGR. The amount of capex spent on new connections is largely driven by economic activities and market forces outside of AGN's control. As a result, providing an incentive under the CESS is unlikely to promote economic efficiency to connections capex. Additionally applying the CESS may result in AGN receiving a reward or penalty for factors beyond its control.

The volume of new connections capex is largely driven by the number of new dwellings constructed, which is again outside of AGN's control. Given the new connections are installed using a tender process, AGN has limited scope to obtain lower unit rates after it has selected its preferred provider. AGN's performance against its targets is also largely unrelated to the amount of new connections capex it undertakes.

As AGN has excluded connections capex from its revised proposal, we are satisfied that the design of the scheme is reasonable.

13.4.2 Asset Performance index range

The CESS proposed by AGN contains a mechanism to vary CESS payments based on AGN's performance against certain service targets. This is known as the asset performance index (API). The API is in place to balance the incentive for AGN to make efficiency savings on capex while maintaining quality of service.

The API allows CESS payments to be made to AGN on a sliding scale. AGN has proposed the range for the API be set from 80 to 100 per cent consistent with our

³ South Australian Minister for Energy and Mining, *Submission to AER on Draft Determination and AGN Revised Access Arrangement*, 16 February 2021, p. 1.

Victorian gas network decision. Under this arrangement, if AGN achieves 100 per cent of its performance targets, it will receive a full payment. The payment will then reduce if AGN does not achieve 100 per cent on a sliding scale, and AGN will not receive a CESS payment if its performance is less than 80 per cent even if a capex reduction were to occur.

We have accepted AGN's proposal to apply the API range from 80-100 for the 2021–26 period. We consider the performance targets proposed and calculations used are broadly similar to those approved in NSW and Victoria.

13.4.3 Performance targets for the asset performance index

AGN's API includes a series of targets, or point of references, to which its actual performance is compared, when determining the CESS payment.

In our draft decision, we reviewed the historical data that AGN used to develop these targets and noted that the calculation for unplanned SAIDI included one observation that was more than six times higher than the next highest observation.

In response, AGN has provided updated information, noting that the observation in question was based on an incorrect calculation. The new information provided a more stable path across years, and our draft decision adopts this figure in place of AGN's initial proposal.

We have also considered other aspects of the performance targets and accepted that it provided a sound basis to assess the actual performance of AGN over the access arrangement period.

Given AGN has amended its revised proposal to reflect the correct calculation, we are satisfied that the performance targets are reasonable.

13.5 Proposed revisions

Based on the information before us, we do not require any further amendment in AGN's access arrangement associated with the capital expenditure sharing scheme.

Shortened forms

Shortened form	Extended form
AER	Australian Energy Regulator
AGN	Australian Gas Networks (SA)
API	Asset performance index
capex	capital expenditure
CESS	capital expenditure sharing scheme
JGN	Jemena Gas Networks (NSW) Pty Ltd
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
NSW	New South Wales
opex	operating expenditure
SAIDI	System Average Interruption Duration Index