FINAL DECISION
Australian Gas Networks (SA)
Access Arrangement

2021 to 2026

Attachment 6
Operating expenditure

April 2021

AUSTRALIAN ENERGY REGULATOR

Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Tel: 1300 585 165
Email: AERInquiry@aer.gov.au

AER reference: 65192

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

Contents

6 Operating expenditure

Operating expenditure (opex) is the operating, maintenance and other non-capital expenses, incurred in the provision of pipeline services. Forecast opex is one of the building blocks we use to determine a service provider's total regulated revenue requirement.

This attachment outlines our assessment of AGN's revised proposed opex forecast for the 2021–26 access arrangement period.

6.1 Final decision

Our final decision is to accept AGN's total opex forecast of $355.6 million ($2020–21),[1] including debt raising costs, for the 2021–26 access arrangement period. This is because our alternative estimate of $351.4 million is not materially different ($4.3 million ($2020–21), or 1.2 per cent lower) from AGN's total opex forecast proposal. Therefore we consider that AGN's total opex forecast satisfies the opex criteria,[2] and satisfies the criteria for forecasts and estimates.[3]

Our final decision is:[4]

- $43.2 million (or 10.8 per cent) lower than the opex forecast we approved in our final decision for the 2016–21 period.
- $22.9 million (or 6.9 per cent) higher than AGN's actual (and estimated) opex in the 2016–21 period.
- $6.1 million (or 1.7 per cent) lower than AGN's original proposal.

Figure 6.1 compares AGN's actual opex, our previous approved forecasts, AGN's revised proposal and our alternative estimate for this final decision.

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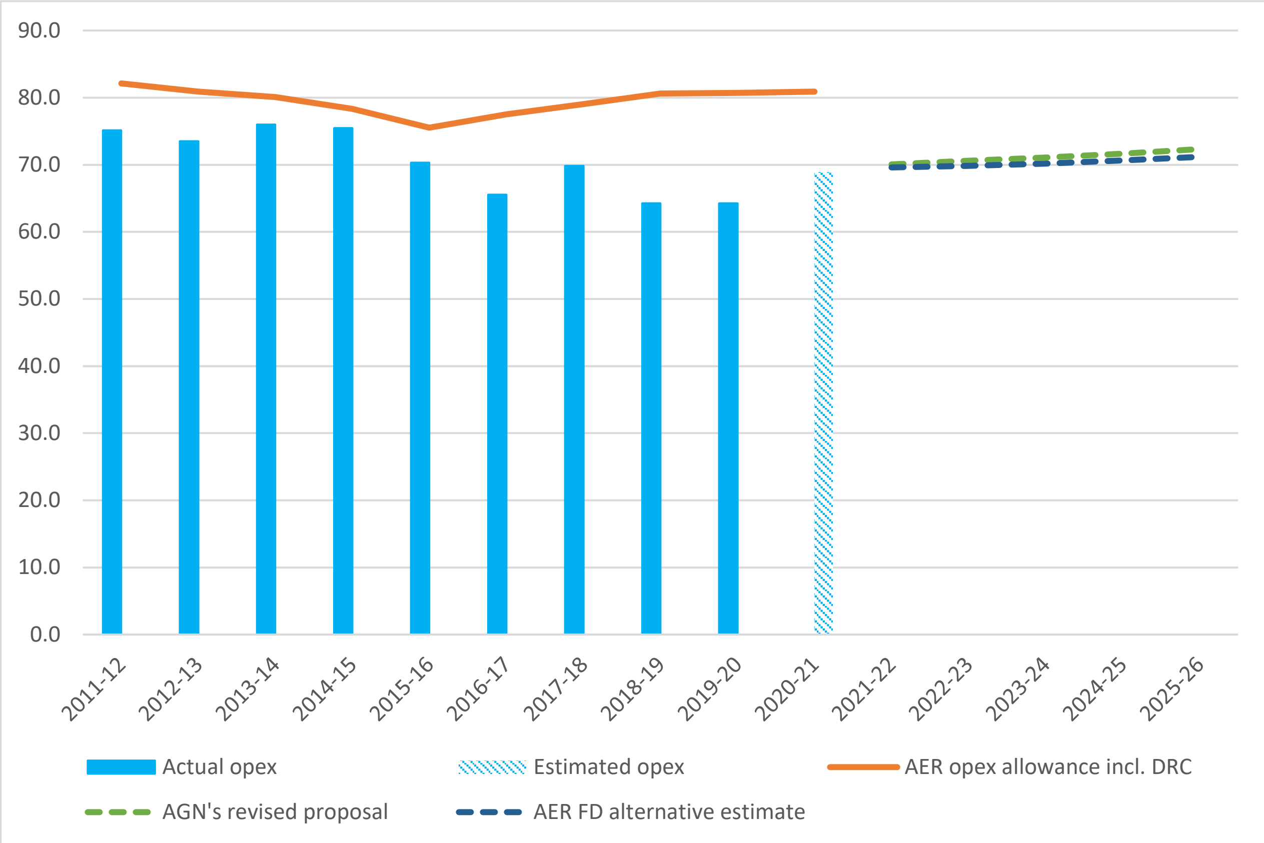
1 AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM,* 13 January 2021.

2 NGR, r. 91.

3 NGR, r. 74.

4 Adjusted to real dollar terms based on June quarter CPI.

Figure 6.1 AER's final decision compared to AGN's past and proposed revised opex ($million, 2020–21)



Source: AGN, *Annual reset RIN*, 30 November 2020; AER, *Final Decision, Australian Gas Networks Arrangement – Post Tax Revenue Model*, May 2016; AER, *Final Decision - amended, Envestra SA – PTRM – tribunal varied,* January 2012; AER analysis.

Note: Includes debt raising costs and unaccounted for gas.

Table 6.1 sets out AGN's revised proposal, our alternative estimate for the final decision and the differences between them.

Table 6.1 AER's alternative opex estimate compared to AGN's revised proposal ($million, 2020–21)

	AGN(SA)'s Revised Proposal	AER alternative estimate Final Decision	Difference
Based on reported opex in 2019	321.2	319.4	-1.8
2019 to 2020–21 increment	3.1	1.1	-2.0
Remove category specific forecasts	-27.0	-24.1	2.9
Output growth	7.2	7.2	-0.1
Price growth	1.8	2.8	0.9
Productivity growth	-3.7	-3.5	0.1
Step changes	4.3	–	-4.3
Category specific forecasts	44.3	44.3	-0.0
Debt raising costs	4.3[5]	4.3	0.0
Total opex	355.6	351.4	-4.3

Source: AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021*;* AER, *Final Decision, Australian Gas Networks access arrangement 2021–26, Opex Model*, April 2021; AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM*, 13 January 2021; AER analysis.

Note: Includes debt raising costs. Numbers may not add up to total due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

The key factor which contributed to our different alternative estimate total opex forecast is we did not include AGN's proposed step changes for the customer relationship management system and incremental insurance costs totalling $4.3 million ($2020–21). For both step changes we are not satisfied, taking into account base opex and the forecast rate of change, that additional opex is required. In particular, for insurance we were not persuaded that non-labour price growth, including for insurance costs, does not adequately compensate the forecast incremental costs.

6.2 AGN's revised proposal

AGN used a 'base–step–trend' approach to forecast opex for the 2021–26 period, consistent with our preferred approach.

In applying our base-step-trend approach to forecast opex, AGN:[6]

- used reported opex in 2019–20 as the base for forecasting its opex over the 2021–26 period ($321.2 million ($2020–21))

[5] AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM*, 13 January 2021.

[6] AGN, Revised Final Plan *2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AER analysis.

- then adjusted its base opex by:
    - removing category specific forecasts for unaccounted for gas (UAFG), debt raising costs and movement in provisions ($27.0 million ($2020–21))
    - applied a rate of change to calculate the 2019–20 to 2020–21 opex increment (to arrive at the starting point for its forecast).[7] This increased its opex forecast by $3.1 million ($2020–21).
- applied its overall rate of change forecast to its adjusted base opex, increasing its forecast opex by $5.4 million ($2020–21) comprising:
    - forecast output growth of $7.2 million ($2020–21)
    - input price growth of $1.8 million ($2020–21) and
    - productivity growth reduced forecast opex by $3.7 million ($2020–21).
- added two step changes for a digital customer experience and insurance premiums. This increased its opex forecast by $4.3 million ($2020–21)
- added two opex category specific forecasts totalling $44.3 million ($2020–21) for UAFG ($40.4 million) and the vulnerable customer assistance program ($3.9 million)
- added forecast debt raising costs of $4.3 million ($2020–21).[8]

AGN's total opex forecast is $355.6 million ($2020–21) for the 2021–26 access arrangement period (see Table 6.2).

Table 6.2 AGN's revised proposed opex for the 2021–26 access arrangement period ($million, 2020–21)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
Total opex, excluding debt raising costs	69.2	69.7	70.2	70.8	71.4	**351.3**
Debt raising costs	0.8	0.9	0.9	0.9	0.9	**4.3**
Total opex, including debt raising costs	**70.0**	**70.6**	**71.1**	**71.6**	**72.3**	**355.6**

Source: AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM*, 13 January 2021; AER analysis.

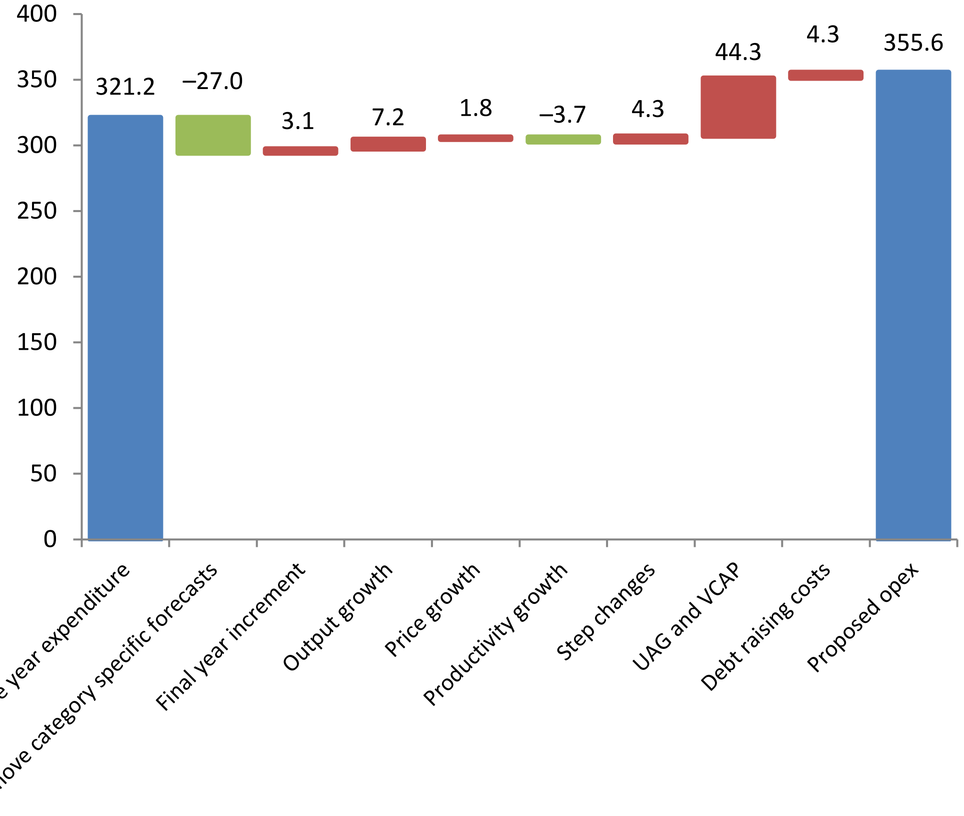
Note: Numbers may not add up due to rounding. Includes debt raising costs.

Figure 6.2 shows the different elements that make up AGN's revised opex forecast for the 2021–26 period.

[7] This increment is necessary to ensure we measure incremental efficiency gains accurately. This is discussed in: *AER, Better Regulation, Explanatory Statement, Expenditure forecast assessment guideline,* November 2013, pp. 62–65.

[8] AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM*, 13 January 2021.

Figure 6.2 AGN's revised opex forecast for the 2021–26 access arrangement period ($million, 2020–21)



Source: AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM*, 13 January 2021; AER analysis.

6.2.1 Stakeholder views

We received submissions from eleven stakeholders on AGN's 2021–26 revised proposal with most raising at a high level the need to account for the impacts of COVID-19. Submissions broadly supported AGN's revised opex proposal with particular emphasis on the high level of customer engagement that AGN conducted.

We have taken these submissions into account in developing the positions set out in this final decision. Table 6.3 summarises the stakeholder issues raised in submissions.

Table 6.3 Submissions on AGN's 2021–26 opex proposal

Stakeholder	Issue	Description
Energy Consumers Australia (ECA)	Base opex	ECA noted AGN have updated base opex to reflect actual expenditure.[9]
ECA, Origin	Rate of change	ECA supported the use of multiple indices to forecast wage price growth provided each index does not suffer any inherent flaws. [10] Origin stated their initial expectation is that wage growth may be more subdued than forecast by AGN.[11]
The AER's Consumer Challenge Panel, sub-panel 24 (CCP24), ECA, SA Minister for Energy & Mining	Step changes	CCP24 retained support for the Digital Customer Experience step change and were satisfied that it is a step up on existing IT capability.[12] ECA were unable to conclude that the digital customer experience initiative would be more than just a service improvement, rather than a step change.[13] SA Minister for Energy & Mining urged the AER to identify the benefits of the Digital Customer Experience Project prior to accepting AGN's reproposed step change.[14]
ECA, Red Energy and Lumo Energy	Consumer Engagement	Red Energy and Lumo Energy stated AGN's consumer engagement in the preparation of its 2021–2026 proposal has been comprehensive, with strong retailer and consumer engagement generally delivering better outcomes for consumers.[15] ECA submission on consumer engagement states it gives rise to two issues.[16] Firstly, the role that consumer engagement plays in assessing the revenue proposals of businesses. While consumer engagement is an important consideration, it should not be a proxy for consistency with the National Gas Objective. Consumer engagement is only one of a number of factors that the regulator must take into account. The second issue that the AER's statement gives rise to what is relevant information that the AER must take into account when performing its statutory role. It is important for all relevant information to be considered by the AER, not just the subset of relevant information referred to in the AER's statement.

9 Energy Consumers Australia, *Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26*, 22 February 2021, p. 19.

10 Energy Consumers Australia, *Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26*, 22 February 2021, pp. 19–20.

11 Origin Energy, *Response to AER draft decision and revised access arrangement proposal for AGN (SA) 2021–26*, 17 February 2021, p. 2.

12 CCP24, *Advice to Australian Energy Regulator on Australian Gas Networks Revised Final Plan for AGN Gas Networks (South Australia) Access Arrangement 2021–26*, 17 February 2021, p. 22.

13 Energy Consumers Australia, *Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26*, 22 February 2021, p. 21.

14 South Australian Minister for Energy and Mining, *Submission to AER on Draft Determination and AGN Revised Access Arrangement*, 16 February 2021, p. 2.

15 Red Energy and Lumo Energy, *Submission to AER on AGN's Draft Decision Gas Access Arrangement,* 19 February 2021, p. 1.

16 Energy Consumers Australia, *Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26*, 22 February 2021, p. 3.

Stakeholder	Issue	Description
CCP24, Energy Consumers Australia, SA Minister for Energy & Mining, Energy Water Ombudsman South Australia (EWOSA), South Australian Council of Social Service (SACOSS), South Australian Financial Counsellor's Association (SAFCA), South Australian Federation of Residents and Ratepayers Association Inc. (SAFRRA)	Opex category specific forecasts	CCP24 were pleased the AER accepted the AGN proposal to source a proportion of its UAFG from renewable gas. CCP24 also raised how the average commodity price might be lower were AGN to have the flexibility to source some of its gas from the spot market.[17] SA Minister for Energy and Mining stated the UAFG forecast volumes do not appear to factor in a decrease resulting from the replacement of the remaining Cast Iron and UPS mains during 2021–26.[18] SACOSS supported the AER's draft decision of incorporating costs of purchasing up to 20 per cent of UAFG as renewable gas in the annual tariff variation mechanism. However, SACOSS considered that while the price of UAFG is largely known, there may not the same level of certainty around the volume forecast and if so, this could be reflected in the annual tariff variation.[19] CCP24 endorsed the reclassification of the vulnerable customer assistance program (VCAP) as a category specific forecast and also expressed the view that shareholders should be making a contribution to this program.[20] EWOSA stated that they perceived no duplication with other third party initiatives in respect to the VCAP program.[21] SAFCA stated it was very supportive of the proposed Step Change around the Vulnerability Customer Assistance Program (VCAP) and commended AGN on the Vulnerability Program and also on the stakeholder engagement around VCAP and the wider gas access arrangement proposal development.[22] SAFRRA commends and strongly supports the Vulnerable Customer Assistance Programme and asks the AER to support these initiatives and make sure AGN have the ability to implement meaningful hardship programmes. SAFRRA also supports the AER accepting a portion of UAFG gas with renewable gas and is open to collectively engaging on the future of gas [23] SACOSS attended the workshop hosted by AGN on 4 December 2020 and noted that there were questions from some retailers around various pathways of referral and whether the program duplicates retailer offerings. From SACOSS' perspective, it was clear from the meeting that further work was required to flesh out how the VCAP offerings interface with current ones.[24] Red Energy and Lumo Energy state customer assistance programs are best administered by those with the customer relationship, namely retailers.[25] Energy Consumers Australia stated that while they supported genuine initiatives for vulnerable customers, they had a number of issues with the VCAP proposal.[26] They considered a review of current vulnerable customer initiatives should be taken to identify whether they appropriately targeted, what gaps there are and how could be addressed, and which stakeholder in the customer journey is best placed to provide the initiative. Energy Consumers Australia did not consider the information AGN provided in its revised proposal demonstrated there was a material increase in the level of service provide and questioned whether retailers should be in charge of the proposed VCAP initiatives. Additionally, they did not consider VCAP was appropriately scoped and considered if an amount is included for VCAP, it should not be covered by the ECM.

6.3 Assessment approach

Our role is to decide whether or not to accept a business' forecast opex. We approve the business' forecast opex if we are satisfied that it meets with the opex criteria. The opex criteria require that:

> Operating expenditure must be such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services.[27]

In deciding whether forecast opex meets the opex criteria, we also apply the forecasting and estimate requirements under the National Gas Rules (NGR):

> A forecast or estimate (a) must be arrived at on a reasonable basis; and (b) must represent the best forecast or estimate possible in the circumstances.[28]

We use a form of incentive based regulation to assess the business' forecast opex over the access arrangement period at a total level. To do so, we develop an alternative estimate of total opex using a 'top-down' forecasting method, known as the 'base–step–trend' approach.[29]

Once we have developed our alternative estimate of total opex, we compare it with the business' total opex forecast to form a view on the reasonableness of the business' proposal. If we are satisfied the business' total forecast meets the NGR requirements, we accept the forecast. If we are not satisfied, we substitute the business' forecast with our alternative estimate.

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17 CCP24*, Advice to Australian Energy Regulator on Australian Gas Networks Revised Final Plan for AGN Gas Networks (South Australia) Access Arrangement 2021–26*, 17 February 2021, pp. 20–21.

18 South Australian Minister for Energy and Mining, *Submission to AER on Draft Determination and AGN Revised Access Arrangement*, 16 February 2021, pp. 2–3.

19 SACOSS, *Submission to AER on AGN's Revised Proposal and AER's Draft Decision 2021–26*, 16 February 2021, p. 3.

20 CCP24*, Advice to Australian Energy Regulator on Australian Gas Networks Revised Final Plan for AGN Gas Networks (South Australia) Access Arrangement 2021–26*, 17 February 2021, p. 23.

21 Energy & Water Ombudsman SA, *Submission to the AER on AGN Draft Determination and Revised Access Arrangement 2021–26,* 21 January 2021, p. 3.

22 SAFCA, *Submission to AER on AGN's Revised Proposal and AER's Draft Decision 2021–26,* 3 March 2021, p. 2.

23 SAFRRA, *Submission to AER on AGN's Revised Proposal and AER's Draft Decision 2021–26*, 17 February 2021, p. 2.

24 SACOSS, *Submission to AER on AGN's Revised Proposal and AER's Draft Decision 2021–26*, 16 February 2021, pp. 2–3.

25 Red Energy and Lumo Energy, *Submission to AER on AGN's Draft Decision Gas Access Arrangement,* 19 February 2021, pp. 1–2.

26 Energy Consumers Australia*, Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26*, 22 February 2021, pp. 20–21.

27 NGR, r. 91.

28 NGR, r. 74(2).

29 A 'top-down' approach forecasts total opex at an aggregate level, rather than forecasting individual projects or categories to build a total opex forecast from the 'bottom up'.

In making this decision, we take into account the reasons for the difference between our alternative estimate and the business' forecast, and the materiality of that difference. We also take into consideration the interrelationships between the opex forecast and other constituent components of our decision, such that our decision is likely to contribute to the achievement of the National Gas Objective (NGO).[30]

6.3.1 Building an alternative estimate of total forecast opex

As a comparison tool to assess a business' opex forecast, we develop an alternative estimate of the business' total opex requirements in the forecast period, using the base–step–trend forecasting approach. We apply the forecasting and estimate requirements under the NGR.[31] If a business adopts a different forecasting approach to derive its opex forecast, we develop an alternative estimate and assess any differences with the business' forecast opex.

Figure 6.3 summarises the base–step–trend forecasting approach.

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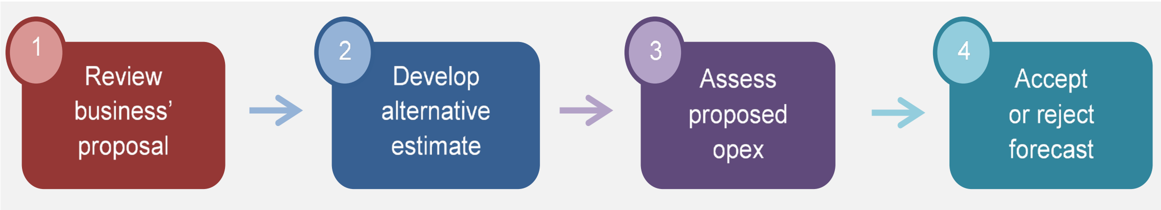
30 NGL, s. 28(1).

31 NGR, r. 74(2).

Figure 6.3 AER's opex assessment approach



1. Review business' proposal

We review the business' proposal and identify the key drivers.

2. Develop alternative estimate

Base

We use the business' opex in a recent year as a starting point (revealed opex). We assess the revealed opex (e.g. through benchmarking) to test whether it is efficient. If we find it to be efficient, we accept it. If we find it to be materially inefficient we may make an efficiency adjustment.

Trend

We trend base opex forward by applying a forecast 'rate of change' to account for growth in input prices, output and productivity.

Step

We add or subtract any step changes for costs not compensated by base opex and the rate of change (i.e. costs associated with regulatory obligation changes or capex/opex substitutions).

Other

We include a 'category specific forecast' for any opex component that we consider necessary to be forecast separately.

3. Assess proposed opex

We contrast our alternative estimate with the business' opex proposal. We identify all drivers of differences between our alternative estimate and the business' opex forecast. We consider each driver of difference between the two estimates and go back and adjust our alternative estimate if we consider it necessary.

4. Accept or reject forecast

We use our alternative estimate to test whether we are satisfied the business' opex forecast is such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services (opex criteria). We accept the proposal if we are satisfied.

If we are not satisfied the business' opex forecast reasonably reflects the opex criteria, we substitute it with our alternative estimate.

6.3.2 Interrelationships

In assessing AGN's revised total forecast opex, we also took into account other components of its access arrangement proposal that could interrelate with our opex decision. The matters we considered in this regard included:

- the operation of the Efficiency Carryover Mechanism (ECM) in the 2016–21 access arrangement period, which provides AGN an incentive to reduce opex in the base year
- our assessment of forecast demand growth, including AGN's forecast growth in customer numbers and mains length, which we used to forecast output growth
- the impact of cost drivers that affect both forecast opex and forecast capex, including forecast labour price growth
- our assessment of the rate of return, to ensure there is consistency between our determination of debt raising costs and the rate of return building block
- the outcomes of AGN's consumer engagement in developing its regulatory proposal.

6.4 Reasons for final decision

Our final decision is to accept AGN's revised proposal total opex forecast of $355.6 million ($2020–21), including debt raising costs, for the 2021–26 access arrangement period.

We have tested AGN's revised proposal by comparing it to our alternative estimate of the total opex forecast of $351.4 million ($2020–21), including debt raising costs, which is not materially different from ($4.3 million ($2020–21), or 1.2 per cent lower) AGN's revised proposal. Therefore, we are satisfied that AGN's proposed forecast reasonably reflects the opex criteria,[32] and satisfies the criteria for forecasts and estimates.[33]

We discuss the components of our alternative estimate below. Full details of our alternative estimate are set out in our opex model, which is available on our website.

6.4.1 Base opex

For our final decision we have used base opex of $63.9 million ($2020–21) for each year of the 2021–26 access arrangement or $319.4 million ($2020–21) over five years to form our alternative estimate.

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32 NGR, r. 91.

33 NGR, r. 74.

Consistent with its initial proposal, and our draft decision, AGN's revised proposal used 2019–20 as the base year for opex.[34] AGN's revised proposal included actual expenditure for 2019–20 compared to estimates used in the draft decision.[35]

AGN is subject to the incentives of an ex ante regulatory framework, including the application of the ECM for opex. Typically, where a service provider is subject to these incentives, we are satisfied there is a continuous incentive for a service provider to make efficiency gains and it does not have an incentive to increase its opex in the proposed base year.[36]

Our final decision is consistent with the draft decision[37] in that we consider our review of AGN's opex over time has not identified any significant inefficiencies. We note no stakeholder submissions to the revised proposal raised concerns regarding the efficiency of AGN's opex. In the absence of any evidence suggesting the contrary, we are satisfied that the 2019–20 base year opex is not materially inefficient. As such, we have used 2019–20 as the base year in our alternative estimate. We note the choice of base year not only affects our alternative opex estimate, but also our calculation of ECM carryover amounts.

The base opex we use in our alternative estimate is $63.9 million ($2020–21). This figure has been updated from the draft decision to reflect updated inflation forecasts in the Reserve Bank of Australia's February 2021 *Statement on monetary policy*[38] for the year ending June 2021 and AGN's actual expenditure submitted in its annual RIN.[39]

6.4.1.1 Final year increment

We need to estimate opex for the final year of the current (2016–21) period because we will not have a reported opex amount at the time of our final decision in April 2021. Our standard practice, set out in our Expenditure Forecast Assessment Guideline, to calculate final year opex is to add the difference between the opex forecast for the final year of the preceding access arrangement period and the opex forecast for the base year to the amount of actual opex in the base year.[40]

Our final decision alternative estimate final year increment of $1.1 million ($2020–21) is $2.0 million ($2020–21) lower than AGN's revised proposed $3.1 million ($2020–21). To calculate the final year increment we have applied the methodology set out in the Expenditure Forecast Assessment Guideline. AGN have calculated the final year

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34 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 1, 5.

35 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, p. 1.

36 NGR, r. 71(1).

37 AER*, Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating Expenditure, November 2020*, pp. 21–23.

38 Reserve Bank of Australia, *Statement on Monetary Policy*, February 2021.

39 AGN, *Annual reset RIN*, 30 November 2020.

40 AER, *Expenditure forecast assessment guideline,* November 2013. pp. 22–23.

increment by applying a forecast rate of change from their base year. We have not used AGN's approach in our alternative estimate as it is inconsistent with how the final year increment is calculated in the ECM. It is important our final year estimate is the same as that used in the ECM. This allows the service provider to retain incremental efficiency gains made after the base year through its opex forecast.

6.4.2 Rate of change

Having determined an efficient starting point, or base opex, we trend it forward to account for the forecast growth in prices, output and productivity. We refer to this as the rate of change.[41]

We have applied a forecast average annual rate of change of 0.7 per cent, which contributes $6.4 million ($2020–21) to our alternative estimate. This is $1.0 million ($2020–21) higher than AGN's forecast rate of change. We compare both forecasts in Table 6.4.

Table 6.4 AER's final decision and AGN's revised proposed forecast annual rate of change in opex 2021–26 access arrangement period (per cent)

	2021–22	2022–23	2023–24	2024–25	2025–26
AGN's revised proposal					
Input price growth	0.2	0.0	0.2	0.4	0.6
Output growth	0.7	0.8	0.8	0.8	0.8
Productivity growth	0.4	0.4	0.4	0.4	0.4
Opex rate of change	**0.6**	**0.5**	**0.5**	**0.8**	**1.1**
AER's final decision					
Input prices	0.4	0.2	0.2	0.3	0.4
Output growth	0.7	0.9	0.8	0.8	0.9
Productivity growth	0.4	0.4	0.4	0.4	0.4
Opex rate of change	**0.8**	**0.7**	**0.6**	**0.7**	**0.9**

Source: AER analysis; AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021.

Note: The rate of change = (1+ price growth) × (1+ output growth) × (1+ productivity growth) – 1.

The difference between our forecast rate of change and AGN's forecast rate of change is driven by the updated Deloitte April 2021 labour price growth forecasts.

We discuss these issues below.

41 AER, *Expenditure forecast assessment guideline*, November 2013, pp. 23–24.

6.4.2.1 Forecast price growth

We have applied a real average annual price growth of 0.3 per cent to develop our alternative estimate of total opex. This increased our total opex alternative estimate by $2.8 million ($2020–21). It compares to AGN's proposed average annual price growth of 0.3 per cent, which increased its total opex forecast by $1.8 million ($2020–21).[42]

Our real price growth forecast is a weighted average of forecast labour price growth and non-labour price growth:

- to forecast labour price growth, we have used the most up-to-date forecast of growth in the utilities WPI for South Australia. Specifically, we have used an average of forecasts from Deloitte's April 2021 forecasts[43] and the BIS Oxford forecasts submitted by AGN in its revised proposal. AGN's revised proposal used an average of Deloitte's August 2020 forecasts as per our draft decision and their submitted BIS Oxford forecasts.[44] In our draft decision we did not use the BIS Oxford forecasts submitted by AGN with its initial proposal because we considered they did not account for the COVID–19 pandemic or the legislated changes to the superannuation guarantee.[45] The revised BIS Oxford forecasts submitted by AGN now account for both of these issues[46]
- both we and AGN applied a forecast non-labour real price growth rate of zero.[47] This is consistent with our draft decision and AGN's initial and revised proposals[48]
- we and AGN have applied the same weights to account for the proportions of opex that is labour and non-labour, 59.7 per cent and 40.3 per cent, respectively.[49] This is consistent with our draft decision and AGN's initial and revised proposals.[50]

6.4.2.2 Forecast output growth

We have adopted AGN's approach to forecast output growth. We forecast average annual output growth of 0.8 per cent. This is the same output growth proposed by AGN

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42 AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AER analysis.

43 Deloitte, *Wage Price Index forecasts - Report prepared for the Australian Energy Regulator,* 1 April 2020, p. xiii.

44 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, p. 8.

45 AER, *Draft decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, pp. 25–27.

46 AGN, *Revised Final Plan 2021–26, Attachment 7.8A - BIS Oxford Input Cost Escalation Forecasts to 2025–26,* 13 January 2021.

47 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, p. 10.

48 AGN, *Final Plan: Five year plan for our South Australian network, 2021–26,* 1 July 2020, p. 79; AER, *Draft decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 25.

49 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 10–11.

50 AGN, *Final Plan: Five year plan for our South Australian network, 2021–26,* 1 July 2020, p. 79; AER, *Draft decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 25.

in its revised proposal[51] and increases our alternative estimate of total opex by $7.2 million ($2020–21). The change in output growth from AGN's initial proposal is due to updated connection numbers and the Mt Barker extension not proceeding.[52]

6.4.2.3 Forecast productivity growth

Consistent with our draft decision, we have forecast annual productivity growth of 0.4 per cent.[53] This is the same productivity growth proposed by AGN in its revised proposed[54] and reduces our alternative estimate of total opex by $3.5 million ($2020–21).

6.4.3 Step changes

In its revised proposal AGN reproposed the following two step changes[55] which we did not include in our draft decision alternative estimate of opex:

- a customer relationship management system (CRMS)
- insurance.

The first of these proposed step changes were for new activities that AGN developed in response to feedback through its customer and stakeholder engagement program. Our assessment of how we accounted for customer feedback is outlined in our draft decision.[56]

Table 6.5 summarises the step changes AGN included in its initial and revised proposals, our draft decision and our alternative estimate for the final decision.

For the final decision we have not included any of the proposed step changes in our alternative estimate. We have examined each step change on its own merit, taking into account considerations set out in our Expenditure Forecast Assessment Guideline.[57]

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51 AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AER analysis.

52 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 1, 11.

53 AER, *Draft decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 28.

54 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, p. 11.

55 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 1, 12.

56 AER, *Draft decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, pp. 29–31.

57 AER, *Expenditure forecast assessment guideline*, November 2013, pp. 11, 24.

Table 6.5 AGN's step change proposals and our alternative estimate ($million, 2020–21)

Step change	AGN's Initial proposal	AER draft decision	AGN's Revised proposal	AER alternative estimate for Final Decision	Difference between AGN's Revised Proposal and AER alternative estimate for Final Decision
Vulnerable Customer Assistance Program	3.9	–	N/A[58]	N/A	N/A
Customer Relationship Management System	1.4	–	1.4	–	-1.4
Insurance	2.9	–	3.0	–	-3.0
Total step changes	8.1	–	4.3	–	-4.3

Source: AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AGN, *Final Plan 2021–26, Attachment 7.1 – Opex Forecast Model,* 1 July 2020; AER, *Draft decision, Australian Gas Networks access arrangement 2021–26*, *Opex model,* November 2020; AER analysis.

Note: Numbers may not add up to total due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

The following sections sets out the reasons for our alternative estimate of each step change.

6.4.3.1 Customer relationship management system

Consistent with our draft decision,[59] our final decision is to not include the $1.4 million ($2020–21) step change for a new customer relationship management system (CRMS) in our alternative estimate.

Table 6.6 AGN's Customer Relationship Management System ($million, 2020–21)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
AGN's revised proposal	0.0	0.3	0.3	0.4	0.4	1.4
AER final decision	–	–	–	–	–	–
Difference	0.0	-0.3	-0.3	-0.4	-0.4	-1.4

Source: AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AER analysis.

Note: Numbers may not add up due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

58 VCAP has been submitted as a category specific forecast.

59 AER, *Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure,* November 2020, pp. 31–33.

The CRMS step change was developed by AGN in response to feedback through its customer and stakeholder engagement program. Our draft decision considered that if customers support an initiative and are willing to pay more for the increased outputs then we would need to be satisfied that the proposed customer supported initiative delivers a genuine step increase in the quality of service provided. We also emphasised that to include a customer supported initiative in our alternative estimate, we would further need to be satisfied the customer supported initiative has to be prudent and efficient and is not accounted for in base opex or the rate of change.[60]

Our draft decision alternative estimate[61] did not include AGN's proposed step change for a new CRMS over the 2021–26 access arrangement period. Our draft decision recognised that AGN undertook robust consumer consultation and that customers strongly supported this initiative. However we concluded the total opex forecast, without including the proposed step change, was sufficient to deliver the proposed additional online services. We considered the proposed service improvements to be a refinement of services AGN currently provides and is consistent with the gradual improvement of good industry practice that is accounted as part of the forecast rate of change.[62]

AGN's revised proposal reproposed the CRMS step change as a customer supported initiative. AGN stated this project is a distinct uplift in services, for all customers, rather than a refinement of existing services and should be captured through additional opex rather than through the forecast rate of change which reflects incremental costs associated with their existing cost base.[63]

CCP24 noted in their submission[64] that they retained support for the CRMS and were satisfied that the step change was a step up on existing IT capability, whereas Energy Consumers Australia[65] noted that they were unable to conclude that the CRMS would be more than just a service improvement rather than a step change. The SA Minister for Energy and Mining urged the AER to identify the benefits of the CRMS step change prior to accepting the proposed step change.[66]

Our final decision, consistent with our draft decision, still considers that the costs are not additional to the trend costs for the efficient benchmark. AGN's revised proposal

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60 AER, *Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, pp. 29–31.

61 AER, *Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 31.

62 AER, *Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 31–33.

63 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 13–14.

64 CCP24, *Advice to Australian Energy Regulator on Australian Gas Networks Revised Final Plan for AGN Gas Networks (South Australia) Access Arrangement 2021–26*, 17 February 2021, p. 22.

65 Energy Consumers Australia*, Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26,* February 2021, pp. 21–22.

66 South Australian Minister for Energy and Mining, *Submission to AER on Draft Determination and AGN Revised Access Arrangement*, 16 February 2021, p. 2.

has not presented any new information to change our assessment that this cannot be funded within their total opex forecast. While we recognise the introduction of a CRMS allows for services to be provided to customers via an online portal, we consider these are a refinement of the existing types of services, such as notifications about planned maintenance, provided to customers. Such refinements are consistent with the gradual improvement of good industry practice and should be compensated through the forecast rate of change. For these reasons we have not included the CRMS step change in our alternative estimate and that the costs for this initiative should remain within the total opex forecast.

6.4.3.2 Insurance

Consistent with our draft decision,[67] our final decision is to not include the $3.0 million ($2020–21) step change for an incremental increase of AGN's insurance premiums in our alternative estimate.

Table 6.7 AGN's Insurance ($million, 2020–21)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
AGN's revised proposal	0.4	0.5	0.6	0.7	0.7	3.0
AER final decision	–	–	–	–	–	–
Difference	-0.4	-0.5	-0.6	-0.7	-0.7	-3.0

Source: AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AER analysis.

Note: Numbers may not add up due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

Our draft decision did not include AGN's proposed step change for the incremental increase of insurance premiums over the 2021–26 access arrangement period for the following reasons:[68]

- our trend forecast includes an allowance for non-labour price growth and this covers any potential increases in costs like insurance premiums. We are not persuaded that AGN has demonstrated that non-labour price growth of CPI, including for insurance costs, does not adequately compensate the forecast increases
- we expect some non-labour components in opex will increase by more than CPI and some less than CPI. To the extent that higher insurance premiums rise by more than CPI, we expect this will to an extent be offset by other non-labour costs rising by less than CPI.

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67 AER*, Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure,* November 2020, pp. 35–36.

68 AER, Draft Decision*, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure,* November 2020, pp. 35–36.

AGN's revised proposal reproposed a step change for forecast increases to insurance premiums over and above the trend over the next access arrangement period.[69] AGN have stated that the rate of change in opex is unlikely to sufficiently compensate them for the increases in costs of the next access arrangement period.[70] AGN submitted the Marsh report[71] which concludes that the insurance market is currently in the "hard phase" for both Property and Liability categories with double digit increases in recent quarters and this trend continuing throughout the next access arrangement period.

As discussed in previous decisions,[72] we approve total opex rather than individual cost categories in an incentive-based regulatory regime. Once approved, a network provider has the flexibility to vary it's spend on individual cost categories as it sees fit and to make savings under the incentives provided in the regime. It follows that step changes, or category specific forecasts, are not needed where the items are not material, given the expectation that network providers manage 'overs and unders' within the total allowance approved by the regulator.

We do not consider that the circumstances that AGN faces in the insurance liability market is sufficiently exceptional that it would materially change its total opex over time beyond what is captured through our price growth forecast. The proposed cost of the insurance premium step change has a relatively low materiality, representing 0.8 per cent of total opex. This is consistent with our final decision for South Australian Power Networks distribution determination 2020–25,[73] where we also did not include a proposed a step change, which accounted for 1 per cent of total opex, for incremental costs related to insurance premiums.

For the reasons outlined above we have not included the step change for incremental costs related to insurance premiums in our alternative estimate.

6.4.4 Category specific forecasts

We have included three expenditure items; vulnerable customer assistance program (VCAP), unaccounted for gas (UAFG) and debt raising costs in our alternative estimate of total opex which we did not forecast using the base-step-trend approach.

6.4.4.1 Vulnerable Customer Assistance Program

Our final decision is to include $3.9 million ($2020–21) as a category specific forecast in our alternative estimate to account for costs related to VCAP over the 2021–26

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69 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021 p. 14.

70 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 14–15.

71 AGN, *Final Plan 2021–26, Attachment 7.7 - Marsh Insurance AA Report*, July 2020.

72 AER, *Final decision*, *South Australian Power Networks distribution determination 2020–25 Attachment 6 - Operating Expenditure,* July 2020, p. 28.

73 AER, *Final decision*, *South Australian Power Networks distribution determination 2020–25 Attachment 6 - Operating Expenditure,* July 2020, pp. 26–29.

access arrangement period. Our draft decision[74] did not accept AGN's initial proposal of the VCAP which was proposed as a step change.

Table 6.8 AGN's Vulnerable Customer Assistance Program ($million, 2020–21)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
AGN's revised proposal	0.9	0.7	0.7	0.7	0.7	3.9
AER final decision	0.9	0.7	0.7	0.7	0.7	3.9
Difference	0.0	0.0	0.0	0.0	0.0	0.0

Source: AGN, *Revised Final Plan 2021–26, Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021; AER analysis.

Note: Numbers may not add up due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

In our draft decision we were satisfied that AGN undertook robust consumer consultation and that the consulted customers supported the provision of a VCAP. However, we considered we required further information to be satisfied that we should include the VCAP in our alternative estimate. In particular we considered AGN needed to demonstrate the VCAP would materially increase the quantity or quality of services AGN provides.[75]

Our draft decision also considered whether providing a step change is the best way to provide additional opex to deliver a customer supported initiative. We concluded that customer supported initiatives, such as the VCAP, should be classified as a category specific forecast instead of a step change to minimise potential perverse ECM outcomes.[76] To enable the VCAP to be excluded from the ECM, AGN would also need to demonstrate that the VCAP's costs are discrete and measureable.[77]

In their revised proposal, AGN submitted the VCAP as a category specific forecast of $3.9 million ($2020–21).[78] AGN noted that this was in response to the AER's draft decision. Including the VCAP as a category specific forecast demonstrates it is both discrete and measurable as the delivery costs will be annually reported[79] and will not be included in base opex after the 2021–26 period.

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74 AER*, Draft decision, AGN access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, pp. 33–35.

75 AER*, Draft decision, AGN access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 35.

76 AER, *Draft decision, AGN access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, pp. 30–31, 35.

77 AER*, Draft decision, AGN access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 35.

78 AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex,* 13 January 2021, pp. 15, 17.

79 AGN*, Revised Final Plan 2021–26, Attachment 7.2A - addendum to Opex Business Case,*13 January 2021, p. 13.

AGN's revised proposal also addressed our concerns of delivering a materially higher level of service stating they currently have no formal programs in place to support vulnerable customers. AGN considered that the materially higher level of service will be delivered through the VCAP initiatives of: [80]

- a dedicated vulnerable customer role ensuring vulnerable customers get more focused and personalised customer service when complaints are raised
- a priority services register resulting in a more responsive customer environment
- gas safety appliance checks and emergency appliance repairs improving the safety and reliability of our vulnerable customers gas appliances and gas use
- financial support to help access to more efficient appliances reducing the financial barriers associated with switching to these appliances.

AGN's revised proposal further detailed a VCAP stakeholder workshop held in December 2020 with members from the South Australia Reference Group, Retailer Reference Group, social service experts and CCP24 as observers. In both workshop discussions and feedback to AGN, participants stated that they were comfortable there was no duplication between the initiatives of the VCAP and other existing programs.[81]

In its stakeholder submission the Energy and Water Ombudsman SA (EWOSA) supported VCAP and stated that it does not perceive any duplications with the VCAP and other existing programs.[82] CCP24's submission further endorsed the reclassification of the VCAP as a category specific forecast and also expressed the view that shareholders should be making a contribution to this program.[83] The South Australian Financial Counsellors Association (SAFCA) whom attended the workshops at which the program was developed were also very supportive of this program.[84] Red Energy and Lumo Energy queried whether customer assistance were best administered by retailers who have a direct relationship with customers.[85] The South Australian Council of Social Service (SACOSS) noted the concerns raised by retailers in AGN's December 2020 workshop around pathways of referral and duplication with retailer offerings and considered further work was required to establish how the VCAP interfaces with other offerings.[86] Energy Consumers Australia[87] also had similar concerns to SAFCA and SACOSS. They also had concerns that VCAP had not been

[80] AGN*, Revised Final Plan 2021–26, Attachment 7.2A - addendum to Opex Business Case,*13 January 2021, p. 10.

[81] AGN, *Revised Final Plan 2021–26, Attachment 7.2A - addendum to Opex Business Case,*13 January 2021, p. 12.

[82] Energy & Water Ombudsman SA, *Submission to the AER on AGN Draft Determination and Revised Access Arrangement 2021–26*, 21 January 2021, pp. 1–3.

[83] CCP24, *Advice to Australian Energy Regulator on Australian Gas Networks Revised Final Plan for AGN Gas Networks (South Australia) Access Arrangement 2021–26,* 17 February 2021, p. 23.

[84] SAFCA, *Submission on AGN Proposal 2021–26*, 3 March 2021, p. 2.

[85] Red Energy and Lumo Energy, *Submission to AER on AGN's Draft Decision Gas Access Arrangement,* 19 February 2021, pp. 1–2.

[86] SACOSS, *Submission to AER on AGN's Revised Proposal and AER's Draft Decision 2021–26,* 16 February 2021, pp. 2–3.

[87] Energy Consumers Australia*, Submission, Response to Evoenergy and Australian Gas Network (SA) Revised proposals 2021–26*, 22 February 2021, p. 20–21.

appropriately scoped and AGN has not been able to show the initiatives provide a material increase in the level of service. If included in the opex forecast, Energy Consumers Australia considered it should not be subject to the ECM.

Based on our analysis of AGN's revised proposal and support from a number of stakeholder submissions, particularly from organisations which deal with vulnerable customers, we consider that AGN has addressed our concerns set out in our draft decision. We are satisfied on balance that VCAP materially increases the level of services provided by AGN, does not duplicate other existing programs and is clearly distinguishable from its marketing activities.

For the reasons stated above, our final decision is to include the VCAP as a category specific forecast in our alternative estimate.

6.4.4.2 Unaccounted for gas

Our final decision is to include $40.4 million ($2020–21) as a category specific forecast in our alternative estimate to account for costs of UAFG over the 2021–26 access arrangement period. The difference from our draft decision position is that our forecast of UAFG costs factor in the cost of purchasing a portion of replacement gas from renewable biogas.

Table 6.9 AGN's Unaccounted for gas (UAFG) ($million, 2020–21)

	2021–22	2022–23	2023–24	2024–25	2025–26	Total
AGN's revised proposal	8.1	8.1	8.1	8.1	8.1	40.4
AER final decision	8.1	8.1	8.1	8.1	8.1	40.4
Difference	–	–	–	–	–	–

Source: AGN, *Revised Final Plan 2021–26*, *Attachment 7.1A - Revised Opex Forecast Model,* 13 January 2021

Note: Numbers may not add up due to rounding. Differences of '0.0' and '–0.0' represent small variances and '–' represents no variance.

Our draft decision[88] did not accept AGN's proposed UAFG forecast and we included a lower amount our alternative estimate of opex. While we agreed with the approach of calculating forecast UAFG costs as the product of UAFG volumes and the cost of replacement gas, we considered:[89]

- the forecast UAFG volumes proposed by AGN using a three year average of actuals did not represent the best forecast possible in the circumstances. We engaged with our consultant Zincara and agreed with their recommendation to use a forecast of UAFG based on a two year average of settled volumes at 2016–17

88 AER*, Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, p. 37.

89 AER*, Draft Decision, Australian Gas Networks access arrangement 2021–26, Attachment 6 - Operating expenditure*, November 2020, pp. 38–40.

and 2017–18 in our alternative estimate. We considered this approach better factored in the impact of recent mains replacement program on reducing UAFG volumes

- while AGN had demonstrated there was strong consumer support and a customer willingness to pay for AGN to replace up to 20.0 per cent of its UAFG with renewable gas, it was not necessary to factor in the price of renewable gas in the forecast cost of replacement gas. We considered that there was sufficient flexibility for AGN to source a portion of its replacement gas from renewable sources and account for the additional costs via the tariff variation mechanism. We otherwise considered AGN's forecast replacement gas prices to be reasonable.

UAFG volumes

AGN's revised proposal[90] accepted the AER's draft decision to use a two year average of actual volumes to forecast the volume of UAFG over the next access arrangement period.

The South Australian Minister for Energy and Mining stated in its submission that the forecast volumes do not appear to factor in a decrease resulting from the replacement of the remaining mains during 2021–26.[91] SACOSS also queried whether there is sufficient certainty around the forecast volumes of UAFG and considered to the extent there is variation in volumes year on year, this may be better reflected in the annual tariff variation mechanism.[92]

For our final decision we have continued to use a two year average of actual volumes to forecast UAFG volumes. While mains replacement in 2021–26 may further reduce UAFG volumes, the magnitude of this impact is difficult to forecast with any accuracy. We consider the use of a two year average factors in the known impact of the mains replacement program to date on UAFG volumes whilst still providing AGN an incentive to reduce UAFG levels in the future.

Cost of replacement gas

AGN's revised proposal specified that the cost of replacement gas should include the price of purchasing renewable gas. AGN considered this approach was appropriate as the costs of renewable gas, specifically biogas, are reasonably known.[93] To support this, AGN provided an extract of the contract for the purchase of replacement gas,[94] including prices, which they are currently finalising for the next access arrangement

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[90] AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex*, 13 January 2021, p. 8.

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

[92] SACOSS, *Submission to AER on AGN's Revised Proposal and AER's Draft Decision 2021–26*, 16 February 2021, p. 3.

[93] AGN, *Revised Final Plan 2021–26, Attachment 7.10 - Response to Draft Decision on Opex*, 13 January 2021, p. 15.

[94] AGN, *Information Request 030 - UAFG Contracts (Confidential),* 23 February 2021.

period. The contract provides for a portion of the replacement gas to be sourced from renewable biogas.

CCP24's submission proposed 'the AER consider how it might incentivise networks to look for lower commodity prices. One approach might be through flexibility in the level of take or pay (ToP) in the GSA to enable sourcing a component of spot gas when the price is favourable'.[95]

Our final decision is to calculate UAFG costs using a forecast cost of replacement gas based on the contract prices provided by AGN. This price factors in sourcing 20 per cent of replacement gas from biogas. This approach ensures that our overall forecast UAFG costs represents the best possible forecast or estimate possible in the circumstances.[96] We are satisfied that AGN has demonstrated there is strong customer support and a willingness to pay for the incorporation of biogas for UAFG. Further, AGN have provided evidence that the volumes of renewable biogas can be sourced, and what the costs of this would be.[97]

In coming to our final decision position, we considered CCP24's suggestion on how to incentivise networks to look for lower commodity prices. Ultimately, we are required to use a forecast or estimate which represents the best forecast or estimate possible in the circumstances.[98] We consider the contract price represents the best forecast estimate in comparison to estimating forecasts of spot gas prices over the access arrangement period.

6.4.4.3 Debt raising costs

We have included debt raising costs of $4.3 million ($2020–21) in our alternative estimate. AGN's revised proposal included debt raising costs of $4.3 million ($2020–21).[99] Debt raising costs are transaction costs incurred each time a business raises or refinances debt. The appropriate approach is to forecast debt raising costs using a benchmarking approach rather than a service provider's actual costs in a single year. This provides for consistency with the forecast of the cost of debt in the rate of return building block.

We used our standard approach to forecast debt raising costs which is discussed further in attachment 3 to the draft decision.

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95 CCP24, *Advice to Australian Energy Regulator on Australian Gas Networks Revised Final Plan for AGN Gas Networks (South Australia) Access Arrangement 2021–26*, 17 February 2021, p. 21.

96 NGR, r. 74.

97 AGN, *Information Request 030 - UAFG Contracts (Confidential),* 23 February 2021.

98 NGR, r. 74.

99 AGN, *Revised Final Plan 2021–26, Attachment 1.4A - PTRM,* 13 January 2021.

Shortened forms

Shortened form	Extended form
AER	Australian Energy Regulator
capex	Capital expenditure
CCP24	Consumer Challenge Panel, sub-panel 24
CPI	Consumer price index
CRMS	Customer relationship management system
ECA	Energy Consumers Australia
ECM	Efficiency carryover mechanism
EWOSA	Energy and Water Ombudsman SA
NER	National Electricity Rules
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
opex	Operating expenditure
PTRM	Post-tax revenue model
RIN	Regulatory Information Notice
SACOSS	South Australian Council of Social Service
SAFCA	South Australian Financial Counsellors Association
SAFRRA	South Australian Federation of Residents and Ratepayers Association
ToP	take or pay
UAFG	Unaccounted for gas
VCAP	Vulnerable customer assistance program
WPI	Wage price index