FINAL DECISION
Evoenergy
Access Arrangement

2021 to 2026

Attachment 5
Capital expenditure

April 2021

AUSTRALIAN ENERGY REGULATOR

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Note

This attachment forms part of the AER's final decision on the access arrangement that will apply to Evoenergy 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 7 – Corporate income tax

Attachment 12 – Demand

Attachment 13 – Capital expenditure sharing scheme

Contents

5 Capital expenditure

Capital expenditure (capex) refers to the capital costs and expenditure incurred in the provision of pipeline services.[1] This investment mostly relates to assets with long lives and the costs are typically recovered over several access arrangement periods.

This Attachment sets out our final decision on Evoenergy's forecast capex for the 2021–26 access arrangement period. It includes our final decision on conforming capex for the 2016–21 period, which forms part of Evoenergy's opening capital base.[2] All dollar amounts are stated in real $2020–21, unless otherwise specified.

5.1 Final decision

We approve Evoenergy's revised proposal of $80.1 million of total net capex for the 2015–16 to 2019–20 regulatory years.[3]

We approve $50.9 million of total net capex for the 2021–26 period as conforming capex under the National Gas Rules (NGR).[4] Our decision is 5.8 per cent lower than Evoenergy's revised proposal forecast of $54.0 million. A summary of our reasons is at section 5.4, while a detailed assessment is at section 5.5.

5.2 Evoenergy's revised proposal

5.2.1 Capex for 2015–16 and the 2016–21 period

Evoenergy has proposed a net capex of $18.5 million for 2015–16 and $76.2 million for the 2016–21 period.

Evoenergy underspent against the net capex forecast we approved for the 2016–21 period by 12.6 per cent ($11.0 million).[5] The underspend largely occurred due to downgrading or deferral in the network renewal category. Projects which are either not proceeding, or proceeding on a smaller scale, in the current period are:

- Watson pressure limiting station (PLS)
- West Belconnen secondary main
- inlet piping rectifications.

Evoenergy provided additional information with respect to the Ginninderry development in its revised proposal, which was highlighted as a placeholder in our draft decision.[6]

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1 NGR, r. 69.
2 NGR, r. 77.
3 NGR, r. 79.
4 NGR, r. 71 and r. 79.
5 Evoenergy's capex for 2020–21 is an estimate.
6 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 18.

5.2.2 Capex for the 2021–26 period

Evoenergy's revised proposal included a net capex forecast of $54.0 million for the 2021–26 period, which is $9.3 million lower than our draft decision and Evoenergy's initial proposal. Evoenergy's forecast is $22.2 million (29.1 per cent) lower than its actual net capex for the 2016–21 period.[7] Given our concerns with the demand forecast in the draft decision, we treated Evoenergy's initial proposal of $63.3 million as a placeholder in our draft decision.[8]

Table 5.1 shows the drivers of Evoenergy's revised forecast capex proposal. The major components of the forecast are meter replacement (48.6 per cent), network renewal (23.5 per cent), and connections (20.2 per cent).

Table 5.1 Evoenergy's revised proposed capex by category over the 2021–26 access arrangement period ($2020–21, million)

Category	2021–22	2022–23	2023–24	2024–25	2025–26	Total
Market expansion (Connections)	4.3	3.3	1.1	1.2	1.2	11.0
Stay-in-business - meter renewal (Meter replacement)	5.8	4.7	5.8	4.6	5.5	26.4
Capacity development (Augmentation)	0.2	0.2	0.2	0.2	0.2	1.1
Stay-in-business - network renewal (Mains replacement plus facilities and pipes)	3.8	4.6	2.0	1.9	0.5	12.8
Non-system (Other)	-	-	-	-	-	-
Overhead	0.8	0.8	0.5	0.5	0.4	3.1
GROSS TOTAL	**14.9**	**13.6**	**9.7**	**8.4**	**7.8**	**54.4**
Contribution	0.2	0.1	0.0	0.0	0.0	0.3
NET TOTAL	**14.7**	**13.5**	**9.6**	**8.4**	**7.8**	**54.0**

Source: AER analysis. Totals may not sum due to rounding

5.3 Assessment approach

The AER must make two decisions when assessing Evoenergy's capex proposal. First, we are required to assess whether past capex is conforming, such that it should be added to the opening capital base.[9] Second, we must assess Evoenergy's forecast of

[7] Evoenergy's capex for 2020–21 is an estimate.

[8] AER, *Draft Decision, Evoenergy(SA) access arrangement 2021–26, Attachment 5 – Capital Expenditure*, November 2020, p. 8.

[9] NGR, r. 77(2)(b).

required capex for the 2021–26 period to determine whether it is conforming capex. Capex will be 'conforming' if it meets the NGR's new capex criteria.[10]

The following sections set out the approach, tools and techniques we employ in forming a view on these two decisions.

5.3.1 Capex for 2015–16 and the 2016–21 period

We consider the following when determining the opening capital base for 2021–26:

- 2015–20 capex – since the data we have is actual capex for these years, we can assess whether this is conforming capex. We have included conforming capex in the opening capital base for 2021–26
- 2020–21 capex – we do not yet have actual capex data for 2020–21 and have included Evoenergy's estimate in the opening capital base. We have not assessed whether Evoenergy's estimate is conforming. Rather, we will assess whether Evoenergy's capex for that year is conforming in the next access arrangement review, when actual expenditure data will be available.

5.3.2 Capex for the 2021–26 period

We have assessed the key capex drivers of Evoenergy's proposal to consider whether its forecast complies with the new capex criteria. In doing so, we relied on the following information:

- Evoenergy's access arrangement submission and access arrangement information, which outline its capex program and main capex drivers
- Evoenergy's revised proposal, and associated information
- Evoenergy's Regulatory Information Notice (RIN) response
- Evoenergy's capex forecast model
- Evoenergy's responses to our information requests
- engineering advice we commissioned from our consultant, Zincara Pty Ltd (Zincara), to help us assess the prudency and efficiency of selected projects
- stakeholder submissions.

For each category of capex, we considered the scope, timing and cost of the proposed capex in order to form a view on whether it complies with the new capex criteria. We also considered whether cost forecasts were arrived at on a reasonable basis and represent the best forecast possible in the circumstances.

We use this assessment to estimate the business's total capex requirements in the forecast period. If we are satisfied the business's total forecast meets the NGR

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[10] NGR, r. 79.

requirements, we accept that forecast. If we are not satisfied, we substitute the business's forecast with our alternative estimate.[11] In making this decision, we take into account the reasons for the difference between our alternative estimate and the business's forecast, and the materiality of that difference.

5.4 Reasons for final decision

5.4.1 Capex for 2015–16 and the 2016–21 period

We accept Evoenergy's revised proposal of net capex of $18.5 million for the year 2015–16 and $61.6 million for the years 2016–20. We have included Evoenergy's estimate of $14.7 million for 2020–21 in its opening capital base, and will review Evoenergy's actual expenditure at the next access arrangement review.

In our draft decision, we expressed concerns relating to market expansion capex in the Ginninderry development. Evoenergy provided further information that addressed our concerns. Our reasons are set out in section 5.5.1.1. Table 5.2 shows our decision on an annual basis.

[11] NGR, r. 64.

Table 5.2 AER's approved capex for 2015–2021 ($2020–21, million)

Category	2015–16	2016–17	2017–18	2018–19	2019–20	2020–21[(a)]
Market expansion (Connections)	7.6	9.8	8.8	10.2	8.0	8.2
Stay-in-business - meter renewal (Meter replacement)	3.6	2.5	3.0	2.9	3.1	3.7
Capacity development (Augmentation)	2.5	4.4	0.1	0.2	1.9	0.3
Stay-in-business - network renewal (Mains replacement plus facilities and pipes)	3.8	2.6	1.4	0.3	0.3	1.8
Non-system (Other)	0.0	0.0	0.0	0.0	0.0	0.0
Overhead	1.1	1.2	0.8	0.8	0.8	0.8
GROSS TOTAL	**18.6**	**20.5**	**14.0**	**14.4**	**14.2**	**14.8**
Contributions	0.1	0.0	0.5	1.0	0.0	0.1
NET TOTAL	**18.5**	**20.5**	**13.5**	**13.4**	**14.1**	**14.7**

Source: Evoenergy, Response to information request IR025, March 2021. Totals may not sum due to rounding.

Note: (a) We have not assessed the 2020–21 amounts as approved capex under this decision. This is because these values are estimates. We will undertake an assessment of whether the 2020–21 amounts are conforming capex in our next access arrangement decision.

5.4.2 Capex for the 2021–26 period

We have accepted net capex of $50.9 million as conforming for the 2021–26 period, $3.1 million (5.8 per cent) lower than Evoenergy's revised proposal.

We had some outstanding issues in the draft decision relating to minor capex projects. Evoenergy provided further information that addressed our concerns. Our reasons are set out in sections 5.5.2.3 and 5.5.2.4.

Evoenergy's decreased connections capex in its revised proposal by $13.5 million (55.2 per cent) from its initial proposal, and increased meter replacement capex by $4.5 million (20.3 per cent). The increase in meter replacement is not the result of a change in the underlying volume, but represents a change in the allocation of Evoenergy's construction management fee.[12] Our assessment of the revised connections forecast is found in section 5.5.2.1 and our discussion on the construction management fee is in section 5.5.2.6.

[12] The construction management fee is allocated across Evoenergy's capex programs, in a manner somewhat similar to an overhead allocation. As Evoenergy reduced its volume of connections, and hence its market expansion capex, it sort to transfer the associated allocation of the construction management fee to the meter replacement category.

The difference between our final decision and the revised proposal is the result of a reduction in the construction management fee, updated inflation figures and labour price growth. Evoenergy's revised proposal, along with its responses to information requests and our analysis, addressed many of the questions raised in our draft decision. Table 5.3 compares Evoenergy's revised proposal to our final decision for each capex category.

Table 5.3 AER's final decision and Evoenergy's revised proposal for capex over the 2021–26 access arrangement period ($2020–21, million)

Category	Evoenergy's revised proposal (RP)	AER's final decision (FD)	Difference (RP - FD)
Market expansion (Connections)	11.0	10.4	-0.6
Stay-in-business - meter renewal (Meter replacement)	26.4	24.5	-2.0
Capacity development (Augmentation)	1.1	1.0	-0.1
Stay-in-business - network renewal (Mains replacement plus facilities and pipes)	12.8	12.4	-0.3
Non-system (Other)	-	-	-
Overhead	3.1	2.9	-0.2
GROSS TOTAL	**54.4**	**51.2**	**-3.2**
Contribution	0.3	0.3	0
NET TOTAL	**54.0**	**50.9**	**-3.1**

Source: AER analysis. Totals may not sum due to rounding

Inclusive of inflation and labour price growth adjustments (section 5.5.2.7).

We assessed Evoenergy's forecast capex, taking into account the available information, submissions from stakeholders and advice from Zincara. Our alternative estimate of Evoenergy's efficient capex is less than Evoenergy's revised proposal. A detailed assessment of each driver is included in section 5.5 of this Attachment.

5.5 Detailed assessment of capex drivers

In assessing Evoenergy's access arrangement proposal, we must decide whether capex from previous periods is conforming,[13] and whether Evoenergy's capex forecast is conforming, or if not, whether it should be substituted with an alternative estimate of capex that is conforming.

[13] We assess capex for the regulatory years from 2015–16 to 2020–2021. As capex in 2020–21 is currently an estimate, we will assess whether actual capex is conforming for this year in the 2026–31 access arrangement review.

5.5.1 Conforming capex for 2015–16 and the 2016–21 period

Evoenergy has proposed net capex of $76.2 million for the 2016–21 period, where capex in 2020–21 is an estimate.

We accept $61.6 million as conforming capex for the 2016–17 to 2019–20 years, and will assess whether capex incurred in 2020–21 is conforming at the next (2026–31) access arrangement review.

In reaching this view, we have considered the following factors:

- Evoenergy's capex is expected to be $76.2 million or 12.6 per cent less than the $87.2 million we approved for the 2016–21 period
- the largest underspends in the 2016–21 period occurred in the network renewal category and connections category, for reasons consistent with our draft decision

Table 5.4 Evoenergy capex performance against the AER final decision by category over the 2016–21 access arrangement period ($2020–21, million)

Category	AER final decision	Actual	Difference (Allow – Act)
Market expansion (Connections)	46.4	45.0	-1.4
Stay-in-business - meter renewal (Meter replacement)	17.0	15.2	-1.8
Capacity development (Augmentation)	6.7	6.8	0.1
Stay-in-business - network renewal (Mains replacement plus facilities and pipes)	15.9	6.5	-9.4
Non-system (Other)	0.6	0.0	-0.6
Overhead	5.2	4.5	-0.7
GROSS TOTAL	**91.6**	**77.9**	**-13.7**
Contribution	4.4	1.7	-2.8
NET TOTAL	**87.2**	**76.2**	**-11.0**

Source: AER Analysis. Totals may not sum due to rounding.

5.5.1.1 2016–21 market expansion

Draft decision

Our draft decision sought additional information about the 2016–21 laying of gas main in stage 1 of the Ginninderry development.

In its proposal, Evoenergy stated that the gas mains laid during stage 1 of the development enabled the connection of a future school and commercial area. Stage 2

would involve installing backbone infrastructure to facilitate connection to green gas options if at a future point, it is deemed appropriate. At the time of our draft decision, it was understood that no customer was connected to the gas network in the Ginninderry development.

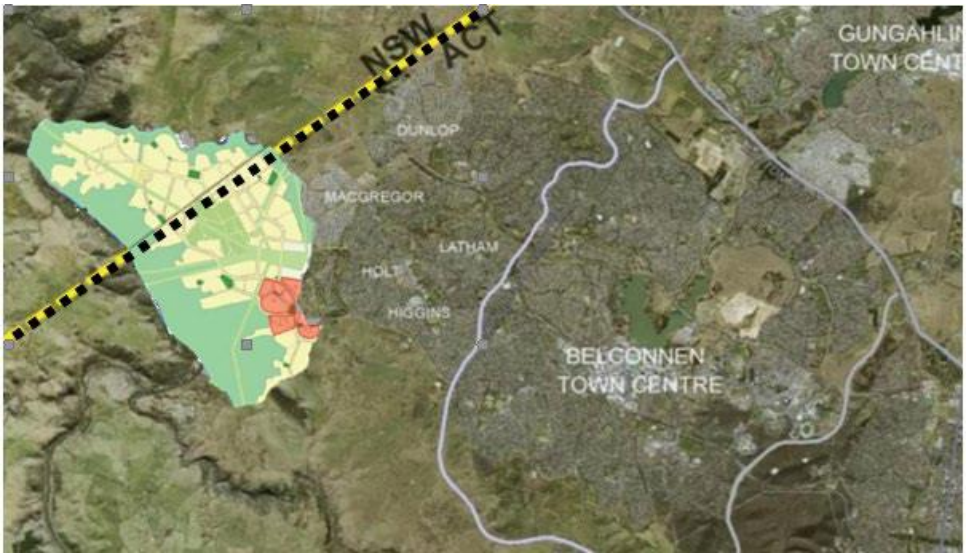
Distribution network assets are commonly installed months prior to actual utilisation for operational and efficiency reasons. We sought additional information from Evoenergy on:

- known or committed gas connections in the Ginninderry development, including their actual or expected connection year, and the likelihood of future gas connections in the Ginninderry development in the next period in light of recent commitments from the ACT Government to achieve net zero emissions
- the economic test and key assumptions undertaken by Evoenergy at the time of investment, as further rationale that the expenditure associated with the gas mains to the Ginninderry development is conforming capex
- other developments similar to the Ginninderry development where Evoenergy has, or is expected to, lay gas mains to the site this period.

Revised Proposal

Evoenergy provided additional information to address the concerns expressed in our draft decision.[14]

Figure 5.1 Ginninderry precinct



Source: Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, Figure 3.1, p. 18.

[14] NGR, r. 79(1).

The Ginninderry development straddles the border between the ACT and NSW. It has a planned total of 11,500 dwellings, over multiple stages, with 1,800 in the initial stage (2017–2022).[15] The initial stage is shaded red in Figure 5.1. Gas mains installed in stage 1 of the development are required to enable gas reticulation in latter stages of the Ginninderry development.[16]

The investment decision was made prior to the publication of the ACT Government's *Climate Change Strategy 2019–25* and at the time Evoenergy expected future revenues "would exceed the costs of laying the mains".[17] Considerations of Evoenergy's investment decisions included:

- the need to supply gas to commercial premises
- NSW homes are highly likely to want gas connections
- the expectation that ACT homes would likely connect to gas, based on the existing high switching rates from electricity to gas at the time of the decision. Analysis indicating a connection rate as low as 20 per cent would see revenue exceed costs
- significantly lower costs of laying mains in shared trenches, which is only available when mains are laid while the development is under construction.[18]

Assessment and final decision

Evoenergy has not advised us of the number of gas connections in the Ginninderry development. However this information is not relevant in determining whether the $0.2 million is conforming capex. The information available at the time of the final investment decision and materiality of the amount spent are more significant criteria in determining conforming capex. For the Ginninderry investment decision, the relevant criteria to address are:

- that the capex would be incurred by a prudent service provider acting efficiently and in accordance with accepted good industry practice
- expected incremental revenue exceeds the present value of the capex.

To determine if we should find the expenditure on mains in Ginninderry stage 1 conforming capex, there are two questions we must address:

- was it the right investment at the time of the investment decision
- what is the materiality.

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15 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 18.

16 Ibid.

17 Ibid.

18 Ibid., p. 19.

The Consumer Challenge Panel (CCP24) raised concerns about the merits of mains laying in the Ginninderry development.[19] Planning and discussions for both the ACT and NSW components of the Ginninderry development commenced in 2013 and have been ongoing since.[20] For a trial period of at least three years, a gas-free residential precinct of 350 homes within stage 1 of the development was required.[21] Dwellings in the NSW portion of the development do not have similar restrictions. Evoenergy advises that the gas mains laid in stage 1 of the Ginninderry development are a prerequisite for gas reticulation in the latter stages, including NSW.[22] Evoenergy's investment decision was made prior to the publication of either the ACT Government's *Climate Change Strategy 2019–25* or the recent *Parliamentary and Governing Agreement*.[23]

On the ACT side, Evoenergy expected that after the all-electric trial, some dwellings would seek gas connections, and that gas would be reticulated throughout the remainder of the development during the construction phase. At the time of the investment decision, 85 per cent of new homes were connecting to gas. Evoenergy advises it needed as little as 20 per cent connections for expected revenue to exceed costs.[24] At the time of the investment decision, Evoenergy demonstrated conforming capex based on the best available information.[25]

On the NSW side, approximately 5,000 new homes have been approved out of a total 11,500 dwellings across the entire Ginninderry development.[26] The new homes in NSW will require a penetration rate of less than 50 per cent to achieve the overall 2,300 connections required to make the Ginninderry development economically viable. As a measure of comparison, the average penetration rate for Jemena Gas Networks (NSW) Ltd's (JGN) gas distribution network is 73 per cent.

Evoenergy has advised that $0.2 million was incurred during the current period (2016–21) to lay gas mains in the Ginninderry development. Given the information before us, we find that:

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19 CCP24, *Advice to the AER on Evoenergy revised gas network 21 plan for Evoenergy (ActewAGL) ACT, Queanbeyan and Palerang access arrangement July 2021–June 2026*, February 2021, p. 26.

20 Ginninderry Joint Venture, *Masterplan – Ginninderry Timing*, accessed 1 February 2021, https://ginninderry.com/about/masterplan/.

21 Berry, Y (Deputy Chief Minister, ACT), *Ginninderry pilots ACT's first gas-free housing trial for 350 homes*, media release, 2 February 2018, https://www.cmtedd.act.gov.au/open_government/inform/act_government_media_releases/yvette-berry-mla-media-releases/2018/ginninderry-pilots-acts-first-gas-free-housing-trial-for-350-homes.
Ginninderry Joint Venture, *All-electric Suburb Trial*, https://ginninderry.com/electric-suburb-trial/, accessed 9 February 2021,

22 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 19.

23 Ibid., p. 18.

24 Ibid., p. 19.

25 NGR, r. 79(1)(a) and r. 79(2)(a).

26 Goulburn Post, https://www.goulburnpost.com.au/story/6842425/over-5000-new-homes-in-yass-valley-as-parkwood-planning-proposal-given-green-signal/, 21 July 2020 accessed 1 February 2021

- Evoenergy has acted in good faith in planning efficiently and in accordance with good industry practices at the time of investment
- there is no evidence to suggest there will be no gas customers requesting connection in the 2021–26 period on the NSW side of the Ginninderry development
- this is not a material expenditure.

Our final decision is to accept a net capex of $0.2 million for the Ginninderry development in the 2016–21 period.

5.5.1.2 2016–21 Geospatial Information System (GIS)

Draft decision

In our draft decision, we sought clarity from Evoenergy on the procurement of a GIS to their electricity and gas businesses' capital base. Evoenergy incurred no expense for this service, against an approved forecast of $0.6 million for the 2016–21 period. We sort further information on whether any expenditure was incurred on GIS, and if so, why nil expense was reported for the gas business.[27]

Revised proposal

In its revised proposal, Evoenergy advised it did not incur GIS related capex in the current period for the gas business.[28] It explained that the electricity business component of Evoenergy's operations is the main user of GIS and there were no additional costs attributable to extending the GIS to the gas business.

Final decision

As Evoenergy has confirmed its intention to not allocate GIS costs from the electricity business to the gas business,[29] our final decision approves nil conforming capex for 2016–21.

5.5.2 Conforming capex for the 2021–26 period

5.5.2.1 Market expansion (connections)

Draft decision

In our draft decision, we accepted the unit rates proposed by Evoenergy. However, we requested further information on the volume forecast in line with our demand decision.

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27 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, pp. 32–33.

28 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 22.

29 Ibid., p. 22.

Consequently, we accepted Evoenergy's connections capex of $24.8 million as a placeholder.[30]

Revised proposal

Evoenergy's revised proposal included $11.0 million for connections capex,[31] $13.8 million (55.6 per cent) less than its initial proposal.

Connections capex has typically been the largest component of the capex program. However, recent commitments of the ACT Government to phase out the use of natural gas for new ACT customers by 2023 has resulted in Evoenergy reducing its connections capex further.[32]

Final decision

The Conservation Council (ACT Region) expressed its preference that Evoenergy have proactive policies discouraging gas connections and transitioning households away from gas appliances.[33] In our final decision, we have accepted Evoenergy's proposal to remove all greenfield developments by 2021 and brownfield developments by 2023.

Evoenergy has reduced the connections capex for the ACT in line with stated ACT Government policy. Further information on forecast connection volumes can be found in Attachment 12 (Demand).

Our final decision accepts Evoenergy's proposed reduction in connection volumes and approves $10.4 million in connections capex. This is marginally lower than Evoenergy's revised proposal. The differences arise due to changes in the amount of the construction management fee, the rate of inflation and labour price growth.

5.5.2.2 Meter replacement

Draft decision

In our draft decision, we accepted Evoenergy's proposed meter replacement of $22.2 million as conforming capex.[34]

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30 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 23.

31 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 17.

32 ACT Government, *Parliamentary & Governing Agreement, 10th Legislative Assembly Australian Capital Territory, Appendix 1*, March 2021.

33 Conservation Council ACT Region, *Submission to the Australian Energy Regulator (AER) Evoenergy revised 2021–2026 gas access arrangement proposal*, February 2021, pp. 2–3.

34 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 27.

Revised proposal

Evoenergy's revised proposal included meter replacement capex of $26.4 million, an increase of $4.2 million (18.9 per cent) on its initial proposal. Evoenergy advised that the increase was due to increased allocation of indirect costs and overheads.[35]

Final decision

In its submission, the Conservation Council (ACT Region) suggested Evoenergy engage with stakeholders including the AER and the ACT Government to address the regulatory obligation required on gas meters.[36]

Evoenergy has an obligation to maintain accurate metering devices under the National Measurement Act and Australian standard AS4944. Should a meter not comply with the accuracy required, it is not considered a legal billing instrument. If the standard or its obligation changes in the future, we expect Evoenergy to amend its capex requirement for its meter replacement program and pass any potential savings to consumers.

Analysis of the information provided in the revised proposal, together with the capex model, revealed that the underlying direct capital expenditure had not changed.[37] The capex increase is primarily the result of a higher allocation of the construction management fee.

While our final decision accepts Evoenergy's proposed meter replacement volumes, we do not accept the material increase in the allocated construction management fee.

Our final decision approves $24.5 million in meter replacement capex, which is $2 million (7.5 per cent) less than Evoenergy's revised proposal.

Our assessment of construction management fee is set out in detail at section 5.5.2.6.

5.5.2.3 Augmentation

Draft decision

In our draft decision, we accepted Evoenergy's proposed forecast of $0.9 million of augmentation capex as a placeholder. We requested that Evoenergy demonstrate actual expenditure trends to support the forecast of $0.2 million per annum which includes the construction management fee for minor capital works.[38]

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35 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 16.

36 Conservation Council ACT Region, *Submission to the Australian Energy Regulator (AER) Evoenergy revised 2021–2026 gas access arrangement proposal*, February 2021, pp. 2–3.

37 Evoenergy, *Attachment 3.1 Capex Model (confidential)*, January 2021.

38 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 31.

Revised proposal

In its revised proposal, Evoenergy provided five years (2015–16 to 2019–20) of average direct costs of capex for minor works on both pipes and high pressure valves.

Table 5.5 Expenditure on minor capital works, ($2020–21, millions, direct costs)

Program	Annual Forecast Requirement	Average annual spend (2015–16 to 2019–20)
Minor capital works (networks)	0.10	0.14

Source: Evoenergy, *Attachment 3.3 – Minor capital works, Revised GN21 Plan – ACT and Queanbeyan-Palerang gas network 2021–26,* January 2021, Table 1, p. 1.

Minor capital works (networks) relate to the replacement of medium pressure (210kPA plastic) network, such as mains, district regulators or small reinforcement augmentations.[39]

Minor capital works are normally found during field investigations, analysis of the performance of the network, or defects. Minor capital works are undertaken to maintain operability, safety or supply.[40]

Final decision

Consistent with Zincara's assessment,[41] and our assessment in the draft decision, we approve $1.0 million of augmentation capex consisting of minor capital works.

5.5.2.4 Network renewal

Draft decision

In our draft decision, we accepted Evoenergy's proposed forecast of $12.2 million of network renewal capex as a placeholder. We requested that Evoenergy demonstrate actual expenditure trends to support two projects for minor capital works included in other network renewal category, each with an allocation of approximately $0.2 million per annum (including the construction management fee) or $1.8 million[42] in total for the 2021–26 period.[43]

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39 Evoenergy, *Attachment 3.3 – Minor capital works, Revised GN21 Plan – ACT and Queanbeyan-Palerang gas network 2021–26,* January 2021, pp. 1–3.

40 Ibid.

41 Zincara, *Evoenergy Access arrangement 2021 – Capital Expenditure – Stage 2*, March 2021, p. 8.

42 The components do not sum to the total due to rounding.

43 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 30.

Revised proposal

In its revised proposal, Evoenergy provided the five-year average (2015–16 to 2019–20) capex for minor works on both pipes and high pressure valves.

Table 5.6 Expenditure on minor capital works, ($2020-21, millions, direct costs)

Program	Annual Forecast Requirement	Average annual spend (2015–16 to 2019–20)
Minor capital works (pipes)	0.10	0.17
Minor capital works (high pressure valves)	0.10	0.13

Source: Evoenergy, *Attachment 3.3 – Minor capital works, Revised GN21 Plan – ACT and Queanbeyan-Palerang gas network 2021–26,* January 2021, Table 1, p. 1.

Minor capital works (pipes) covers reactive capex on both underground and aboveground pipelines. Minor capital works (high pressure facilities) reflect the replacement of failed or at risk equipment on high-pressure facilities.[44]

Minor capital works are normally found during field investigations, analysis of the performance of the network, or defects. Minor capital works are undertaken to maintain operability, safety or supply.[45]

Final decision

Consistent with Zincara's assessment,[46] and our draft decision, we are satisfied that Evoenergy has addressed our concerns, and we approve $12.4 million of mains renewal capex.

5.5.2.5 Non-system and other

Draft decision

We accepted Evoenergy's proposal of nil capex in the draft decision as a placeholder, and requested further information on the SCADA RTU project in the capex model.[47]

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44 Evoenergy, *Attachment 3.3 – Minor capital works, Revised GN21 Plan – ACT and Queanbeyan-Palerang gas network 2021–26,* January 2021, pp. 1–3.

45 Ibid.

46 Zincara, *Evoenergy Access arrangement 2021 – Capital Expenditure – Stage 2*, March 2021, p. 9.

47 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, pp. 32–33.

Revised proposal

In its revised proposal, Evoenergy advised the project in question was a SCADA remote terminal unit project. This project relates to the replacement of obsolete remote terminal units, and is distinct from SCADA system expenditure.[48] While it is classified as non-network telemetry in the capex model, it is correctly allocated to the network renewal capex category.

Final decision

Our final decision approves nil for non-system capex and the associated allocation for the SCADA RTU project.

5.5.2.6 Construction management fee

Draft decision

In our draft decision, we accepted the proposed construction management fee as conforming capex. However, we did not accept that the fee was a fixed cost over time, and encouraged Evoenergy to consider the level of service required should its capex program continue to decline.[49] The actual value of the construction management fee is subject to a confidentiality claim, and is not included in documents published by the AER.

Revised proposal

Evoenergy's revised proposal reduced overall capex by $9.3 million (14.6 per cent) from its initial proposal. Connections forecast was the largest decrease, with a reduction of $13.8 million (55.6 per cent) compared to its initial proposal. Despite the material reduction in connections requirement, the total construction management fee remained unchanged. As a result, meter replacement capex has increased due to the reallocation of the construction management fee.[50]

Assessment and final decision

In our draft decision, we approved the proposed construction management fee. In particular, we considered our analysis, which showed the forecast construction management fee was reasonably lower in the 2021–26 period compared to the 2016–21 period was consistent with Evoenergy's overall lower capex forecast. This is

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48 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 22.

49 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 37.

50 Zincara, *Evoenergy Access arrangement 2021 – Capital Expenditure – Stage 2*, March 2021, p. 7.

consistent with our view that the construction management fee is not entirely fixed over time.[51]

Zincara reviewed the total construction management fee as part of its assessment of Evoenergy's revised proposal.[52] Zincara recommended that for the 2021–26 period, a reasonable construction management fee should be $2.6 million lower than Evoenergy's proposal.[53]

Due to confidentiality claims, we are unable to quantify the magnitude of construction management fee in our decisions.

As capex declines, it is reasonable to assume that the resources supporting the capex programs will also be lower.

Our final decision approves a $2.6 million reduction in the construction management fee.

5.5.2.7 Cost escalation and reconciliation

For this capex final decision, we considered the following inputs for inflation and labour price growth:

- actual inflation up to 2020–21
- adjusted labour price growth in line with our opex alternative forecast (section 4.5 of the Overview) and the appropriateness of its application to the capex forecast.

As Evoenergy has based its forecast on historical inputs and presented the inputs in 2019–20 and 2020–21 dollar terms in its capex model, we have confirmed actual rates of inflation prior to 2020–21.

As noted in our draft decision,[54] we have updated estimated inflation with actual inflation for 2020–21, in line with our roll forward model (RFM) and our capital base decision (see Attachment 2). This resulted in a $0.6 million reduction in total capex.

In terms of labour real cost escalators, we have updated for labour price growth in line with our opex alternative forecast. This resulted in a $0.1 million increase in total capex.

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51 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 37.

52 Zincara, *Evoenergy Access arrangement 2021 – Capital Expenditure – Stage 2*, March 2021, pp. 10–12.

53 Zincara, *Evoenergy Access arrangement 2021 – Capital Expenditure – Stage 2*, March 2021, p. 12.

54 AER, *Draft decision, Evoenergy access arrangement 2021–26, Attachment 5 – Capital expenditure*, November 2020, p. 37.

5.5.3 Speculative Capital Expenditure Account

A speculative capital expenditure account (SCA) is a mechanism under rule 84 of the NGR. An SCA allows spending on non-conforming capital that at a later date may become conforming and may be added to the capital base.

Draft decision

Evoenergy did not include an SCA in its initial proposal. Accordingly, there was no discussion of an SCA in our draft decision.

Revised Proposal

Evoenergy's revised proposal states that it is investigating the introduction of renewable gas alternatives into its gas network, though it has not identified any projects. The unidentified projects will "support renewable alternatives and promote the energy market's drive towards decarbonisation via storage service provisioning, distribution, and delivery of renewable energy".[55]

The revised capex forecast does not include financial costings for the unspecified projects. Recognising that expenditure on transforming the gas network may not initially meet the criteria of conforming capex, Evoenergy "intend to make use of the Speculative Capex Account (SCA) provision…to record non-conforming expenditure".[56]

Assessment and final decision

In its submission on Evoenergy's revised proposal, CCP24 advised it considers the SCA to be a useful mechanism for trialling non-conforming capex. However, consideration should also be given to the following conditions before an SCA is opened:[57]

- detailed consumer engagement
- whether funding for such trials is not available from other non-customer sources
- whether the trial links with other relevant renewable gas programs and trials
- whether there is a well-developed, practical and costed project proposal
- resolution of any project aspects which are not consistent with the NGR.

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55 Evoenergy, *Revised GN21 plan – Response to the draft decision, ACT and Queanbeyan-Palerang gas network 2021–26*, January 2021, p. 22.

56 Ibid., p. 23.

57 CCP24, *Advice to the AER on Evoenergy revised gas network 21 plan for Evoenergy (ActewAGL) ACT, Queanbeyan and Palerang access arrangement July 2021–June 2026*, February 2021, p. 26.

In our JGN 2020–25 decision,[58] we approved the opening of an SCA. In that instance, JGN provided estimated costs for a specific project they sought to include in the SCA. JGN's 'Green Gas Trial' project, conducted in conjunction with the Australian Renewable Energy Agency (ARENA), is investigating the production of hydrogen and trialling its use in the network.[59]

At the time, JGN provided us with sufficient project detail to warrant an SCA, including reasons why such a project may bring about material benefits, costings and scope. In comparison, Evoenergy has not provided sufficient details on project scope, timing, costs or expected benefits.

NGR r. 84(3) indicates the reason capex is added to the SCA is that the type or volume of services does not meet the new capex criteria. If, at any future time, the type or volume of service changes, such that the capex complies with the capex criteria, the amount in speculative capex may then be rolled into the capital base. Consequently, there must be sufficient information about the type and volume of services proposed for the SCA for the AER to assess the proposal.

Based on the information before us, we do not accept Evoenergy's proposed opening of an SCA in the 2021–26 period. In particular, we do not consider Evoenergy's proposal contains sufficient detail for us to approve the opening of an SCA. However, Evoenergy may propose to open an SCA in the future once a project scope, timing and costs and expected benefits are available for assessment, along with stakeholders support.[60]

5.6 Proposed revisions

We require the following revisions to make the access arrangement proposal acceptable:

Table 5.7 Revisions

Revision 5.1	Remove clauses 5.1 from the Access arrangement, Evoenergy's gas distribution network, 1 July 2021 – 30 June 2026.

[58] AER, *Final decision, JGN access arrangement 2020–25, Attachment 5 – Capital expenditure*, June 2020, pp. 42–43.

[59] Ibid., p 42

[60] NGR, r. 65.

Shortened forms

Shortened form	Extended form
ACT	Australian Capital Territory
AER	Australian Energy Regulator
ARENA	Australian Renewable Energy Agency
Capex	Capital Expenditure
CCP/CCP24	Consumer Challenge Panel, sub-panel 24
DAMS	Distribution Services Agreements
Evoenergy	ActewAGL Distribution
GIS	Geospatial Information System
IT	Information Technology
JAMS	Jemena Asset Management Pty Ltd
JGN	Jemena Gas Networks (NSW) Pty Ltd
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
NSW	New South Wales
PLS	Pressure Limiting Station
RFM	Roll Forward Model
RIN	Regulatory Information Notice
RTU	Remote Terminal Unit
SCA	Speculative capex account
SCADA	Supervisory Control And Data Acquisition
Zincara	Zincara Pty Ltd