

Decision

Allgas - Negative carbon cost pass through

2015-16

May 2015

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# Summary

Allgas Energy Pty Ltd (Allgas) is the owner of the Allgas natural gas distribution network in Queensland.[[1]](#footnote-2)

On 27 August 2014, Allgas applied to us for a tax change negative pass through event as a result of the repeal of the carbon tax. Allgas has proposed to remove the carbon tax component from its approved reference tariffs for the 2015–16 regulatory year. The proposed negative pass through amount is:

* – $1 234 139

We have determined that a negative carbon cost pass through event has occurred and we have approved the proposed pass through amount.

Allgas has already voluntarily reduced its tariffs to remove the carbon component, effective from 1 September 2014. Allgas' pass through application included a proposal to formally reduce its 2014–15 reference tariffs to reflect the reduction it had already made. This cost pass through decision will now take effect on 1 July 2015. The 2014–15 component of Allgas' original cost pass through application is no longer relevant.

In addition to removing its existing carbon price allowance from 2015–16 reference tariffs, Allgas has proposed return to customers previously over recovered carbon tax revenues. This is consistent with the true–up mechanism we have previously approved. For completeness we clarify here that we also approve Allgas' proposed return to customers:[[2]](#footnote-3)

* – $259 475

# Background

The Australian Energy Regulator is responsible for the economic regulation of covered natural gas distribution and transmission pipelines in all states and territories except Western Australia. Our functions and powers are set out in the National Gas Law (NGL) and the National Gas Rules (NGR).

The carbon tax was repealed by the Australian parliament on 17 July 2014 and received royal assent the same day, removing Allgas' carbon liability for 2014–15. As a result, Allgas no longer has an obligation to purchase and surrender carbon units as a liable entity under the Clean Energy Act 2011.

Prior to the carbon tax repeal, Allgas had an obligation under the Clean Energy Act 2011 to purchase and surrender carbon units for each tonne of carbon pollution emitted as a liable entity operating a facility that exceeds a scope 1 (direct) emissions threshold of 25 000 tonnes of carbon dioxide equivalent. This liability relates to fugitive gas emissions from transmission and distribution pipelines and emissions from gas combustion in pipeline compressor stations.

Light handed regulation

On 28 April 2015 the Australian National Competition Council (NCC) published its decision that the Allgas network be subject to light handed regulation.[[3]](#footnote-4) This means that, going forward, the AER will no longer set reference tariffs for the Allgas network. Rather, tariffs will be negotiated between Allgas and its customers or prospective customers. We will be available to arbitrate should disputes arise.

The NCC's determination comes into force 60 business days from the date it was made. This means that on 1 July 2015 the Allgas network will still be a regulated network for which the AER must approve reference tariffs. Hence, we must also consider Allgas' negative cost pass through and publish our decision.

# Application

Allgas considers the repeal of the carbon tax to be a Tax Change Event, as defined by the Allgas access arrangement, as it removes a Relevant Tax.[[4]](#footnote-5)

The incurred drop in operating expenditure as a result of the Tax Change Event is the reduction in costs due to the repeal of the Clean Energy Act 2011 and subsequent removal of the obligation imposed to purchase and surrender carbon units for each tonne of carbon pollution emitted, from 1 July 2014.

Allgas proposes to remove the existing carbon component from its 2015­–16 reference tariffs. This amount had been approved previously.

Allgas ceased collecting carbon related revenues from 1 September 2014. Before Allgas was able to give effect to the carbon tax repeal by adjusting its tariffs, Allgas incurred an over–recovery of carbon tax revenue for the months of July and August 2014. Allgas has proposed to return this over–recovery to customers through a further reduction in its 2015–16 reference tariffs.

# Approach and assessment

## Cost pass through event

Clause 4.5.4 of the Allgas access arrangement states:[[5]](#footnote-6)

"Subject to the approval of the AER under the NGR, Reference Tariffs may be adjusted after one or more Cost Pass-through Event/s occurs in which each individual event materially increases or materially decreases the cost of providing the reference services. Any such adjustment will take effect from the next 1 July."

The access arrangement defines a tax change event as:

"A tax change event occurs if any of the following occurs during the course of the Access Arrangement period for APT Allgas:

1. a change in a relevant tax, in the application or official interpretation of a relevant tax, in the rate of a relevant tax, or in the way a relevant tax is calculated;
2. the removal of a relevant tax;
3. the imposition of a relevant tax; and

In consequence, the costs to APT Allgas of providing the reference services are materially increased or decreased."

## Factors considered

We have assessed the negative cost pass through application in accordance with factors listed in clause 4.5.4 of the access arrangement. This section sets out those factors and our considerations against each.

In making its decision on whether to approve the proposed Cost Pass-through Event variation, the AER must take into account the following:

* the costs to be passed through are for the delivery of pipeline services

We accept that the costs relate to the delivery of pipeline services.

* the costs are incremental to costs already allowed for in reference tariffs

We accept that the costs are incremental to those already included in the Allgas reference tariffs.

* the total costs to be passed through are building block components of total revenue

We accept that the costs are building block components, in the nature of operating costs, or opex. Opex refers to the operating, maintenance and other non-capital costs incurred in the provision of pipeline services.

* the costs to be passed through meet the NGR criteria for determining the building block for total revenue in determining reference services

Rule 91(1) of the NGR provides that opex must reflect the costs incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering reference services. We are satisfied that Allgas' negative pass-through costs satisfy the NGR criteria set out in r. 91(1).

* any other factors which the AER considers relevant and consistent with the NGL and NGR.

The proposed carbon allowance removal pass through amount is appropriate, as it matches the carbon costs we have previously approved. It also meets the materiality threshold set out in the access arrangement. That is, at least one per cent of the smoothed forecast revenue specified in the Access Arrangement Information. Allgas' proposed return to customers of over recovered carbon tax revenues is not subject to the materiality threshold as it relates to an approved true–up mechanism.

|  |  |  |
| --- | --- | --- |
| Year | Pass through amount | Percentage of smoothed revenue |
| 2015–16 | – $1 234 139 | 1.43 per cent |

The proposed manner of Allgas' carbon cost removal from reference tariffs is appropriate, as it matches the manner in which carbon costs were previously incorporated. And we consider the pass through period is also appropriate. Carbon costs will be removed from reference tariffs in the year to which they relate.

# Decision

We determine that a negative carbon cost pass through event has occurred and that a negative pass through is appropriate, as follows:

* – $1 234 139

We also determine that a further negative pass through is appropriate, to return to customers previously over recovered revenues:

* – $259 475

The approved negative cost pass through amounts will be returned to customers in the form of lower reference tariffs in 2015–16.

1. Allgas operates the Allgas network as Allgas Energy Pty Ltd and Allgas Toowoomba Energy Pty Ltd. [↑](#footnote-ref-2)
2. We received a revised true–up proposal from Allgas on 15 May 2015. [↑](#footnote-ref-3)
3. NCC, Application by Allgas Energy Pty Ltd for Light Regulation of the Allgas Gas Distribution Network – Final decision, 28 April 2015. [↑](#footnote-ref-4)
4. APT Allgas Energy Pty Ltd, Access Arrangement effective 1 July 2011 – 30 June 2016, June 2011, p. 17. [↑](#footnote-ref-5)
5. APT Allgas Energy Pty Ltd, Access Arrangement effective 1 July 2011 – 30 June 2016, June 2011, p. 14. [↑](#footnote-ref-6)