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**Victorian Transmission System Stakeholder  
Engagement Group. 2023-27 access  
arrangement (AA6).**

**Roundtable 7 – Capital program update & first  
look at operating expenditure**

Scott Young, Daniel Tucci, Adam Newbury, Nives Matosin  
16 June 2021



## Acknowledgement of Country

In the spirit of reconciliation, we would like to begin by paying respect to the Traditional Owners of the land on which we meet today and their continuing connection to land, waters and community.

We pay our respect to Traditional Owners, their cultures, and to their elders past and present.



# Today's discussion

Welcome & Acknowledgement of Country

Engagement timeline

Reference services – AER decision

Feedback from Roundtable 6

Capital program issues paper

Update on capital program - replacement capex, WORM

Review of demand & supply forecasts

Operating expenditure &  
Efficiency carryover mechanism

Wrap up

**Purpose of today's discussion is to inform and consult.**

# Engagement timeline

VTS stakeholder engagement key activities and dates				
Phase	Date	Activity	Topics	IAP2 spectrum
<b>Phase 2 - Getting to the detail - revenue requirements, tariffs and access arrangements</b>				
	14/05/2021	Issues Paper	Capital program	Involve
	19/05/2021	Roundtable 6	AEMO presentation on VGPR. Demand forecasts.	Inform/ Consult
	19/05/2021	AER decision	AER decision on reference services	
	16/06/2021	Roundtable 7	Further draft of capital program. First look at operating expenditure forecasts, efficiency mechanism and other revenue components.	Inform/ Consult/ Involve
	14/07/2021	Roundtable 8	First look at total revenue, revenue allocation and tariff structures A look at the Access Arrangement – proposed revisions	Inform / Consult
	14/07/2021	Information/ Issues Paper	VTS tariff structures	Inform/ Involve
	18/08/2021	Roundtable 9	Continue discussion on cost allocations and tariff structures.. Making changes to the Access Arrangement	Involve Involve
	22/09/2021	Roundtable 10	What we've heard so far, our response. Further opportunity for input.	Involve
<b>Phase 3 - Putting the plans together</b>				
	6/10/2021	Consultation	APA release Consultation draft proposal for comment	Involve
	13/10/2021	Roundtable 11	Early consultation proposal - questions and answers session	Involve
	17/11/2021	Roundtable 12	Our draft proposal and how you shaped our thinking.	Involve

# Reference services – AER decision

APA VTS proposed only one reference service, the **Tariffed Transmission Service**. This is because:

- AEMO’s declared system functions include “to control the operation and security of the declared transmission system” (s91BA(1)(b));
- the service provider for the declared transmission system (APA VTS) must have an agreement (a *service envelope agreement*) with AEMO for the control, operation, safety, security and reliability of the declared transmission system (s91BE(1));
- “Under the service envelope agreement, the service provider makes the declared transmission system available to AEMO (and, in doing so, provides a pipeline service)” (s91BE(2)).

Under the market carriage structure, this is the only service APA VTS is able to offer

- although not strictly the Reference Service, the **Tariffed Transmission Service** is the mechanism under which APA VTS charges for its services according to the Transmission Payment Deed.

We lodged our Reference Service proposal in December 2020. The AER found that proposal to be compliant with the Rules.

The AER called for submissions – none were received

On 19 May 2021 the AER approved our Reference Service proposal

<https://www.aer.gov.au/system/files/APA%20VTS%202023-27%20-%20APA%20VTS%20reference%20service%20proposal%20-%20AER%20Final%20Decision%20-%20PDF%20version%20-%2019%20Ma%2812342007.1%29.pdf>

# What we heard at Roundtable 6 and our response

Topic	Issue	Response
Forecasts	Are AEMO's forecasts conservative if they don't include new Beach supplies. If the Esso refinery closes, will there be more gas available (in the VTS). What is the impact if the refinery closes? So the forecasts are conservative if they exclude the new Beach supplies.	APA is considering engaging a consultant to review the supply and demand forecasts in light of changes after the AEMO 2021 VGPR was published.
Review AEMO forecasts	Suggested that APA consult with stakeholder group on the Terms of Reference.	Great suggestion. Draft TOR for the review have been sent the Stakeholder group for comment.
Capacity certificates	Is there a break glass mechanism so that APA/AER can approve augmentations (i.e SWP expansion) within the access arrangement period if needed for system security?	<p>Jessie noted that AEMO Final documents and tracked procedures have been published  <a href="https://aemo.com.au/consultations/current-and-closed-consultations/implementation-of-2020-dwgm-enhancement-rule-changes">https://aemo.com.au/consultations/current-and-closed-consultations/implementation-of-2020-dwgm-enhancement-rule-changes</a></p> <p>AEMO will consult as per Procedures on how the LNG injections will be considered for SWP capacity certificates.</p>
Hourly vs daily demand	Does AEMO look at hourly demand for gas also rather than Daily? Gas demand is moving ever more towards electricity peak demands particularly as renewable increase, so looking at capacity on a daily could be misleading. ( ie may not met MDQ but will meet equivalent MHQ).	AEMO looks at daily demand at this stage.

# What we heard at Roundtable 6 and our response

Topic	Issue	Response
South West Pipeline	[regarding LNG injections backing off Iona CPP injections] ...What is the quantum of back off effect to Iona CPP with LNG import?	Jessie noted that investigations are underway.
South West Pipeline	[response by participant] The rate at which gas would be injected into the VTS would be driven by the market demand and not by any "need" for the FSRU to quit its load.	Ok.
Western Outer Ring Main (WORM)	What is the benefit of the WORM? looking at the graphs is it 66 TJ withdrawal and 15TJ injection?	Note that the purpose of the WORM is to provide security of supply.
Net zero emissions	Still trying to understand impact of a net zero emissions policy on the forecast.	Jessie noted this is a question for AEMO forecasting team.
Accelerated depreciation	In the AER final decision on EVO, AER approved accelerated depreciation. Is APA considering this?	One of the reasons for commissioning the review of supply and demand forecasts is to help inform APA in developing a position on this issue.

# Capital program issues paper

We issued capital program issues paper on 13 May

The paper summarises issues raised, so far, during stakeholder engagement and sets out our current thinking in response to those issues

We have also posed a number of questions for your consideration.

We will accept comments by 30 June

Are there any matters you wish to raise today?

<b>Question 1</b>	Are there potential projects arising from the VGPR that APA should take into consideration in preparing the capital plan for the 2023-27 VTS?
<b>Question 2</b>	Are there any other matters that APA should take into consideration in preparing the capital plan for the 2023-27 VTS?
<b>Question 3</b>	Are there any further matters you wish APA to address about the WORM?
<b>Question 4</b>	Are there any further matters APA should consider with respect to potential LNG Gas Terminals coming on line in Victoria?
<b>Question 5</b>	Are there any other options you want us to consider regarding the funding of gas import terminals?
<b>Question 6</b>	Are there any other questions about how augmentation or other projects get considered by the AER?
<b>Question 7</b>	Do you have further questions about APA's approach to planning for stay-in-business (replacement and upgrade)
<b>Question 8</b>	Are there any other questions about APA's hydrogen initiatives in relation to the VTS?
<b>Question 9</b>	Are there any other matters about the VTS capital program that you wish the raise with APA?



# Update on Western Outer Ring Main (WORM)

- In December 2019, the Victorian Minister for Planning determined that an Environment Effects Statement (EES) was required for the WORM
- EES process identified matters that needed to be addressed including, an increase in number and length of horizontal directional drilling (HDD)
- In addition, the cost of meeting biodiversity offset obligations is significantly higher than originally forecast
- The delay in commencement of construction has also resulted in an increased cost of steel and higher construction costs due to construction now scheduled to be across and including a winter season
- The cost of the WORM is forecast to increase from the original \$126.7 million (2017) to \$167 million (note this figure is not market tested)
- EES public exhibition expected in next few weeks.



# Update on replacement (stay-in-business) forecasts

Replacement capital expenditure is necessary to maintain and improve the **safety** of services; or maintain the **integrity** of services; or comply with a **regulatory obligation** or requirement; or **maintain capacity** to meet levels of demand for services existing at the time the capital expenditure is incurred

- **Since Roundtable 5**
  - The total replacement capital expenditure programs forecasts are in line with numbers previously provided (approx. \$83 million)
  - Investigations are underway to better phase the stay-in-business programs over the access arrangement period
  - Re-phasing of the program will allow for better resourcing and avoiding resourcing constraints
  - A key program is maintaining pipeline integrity by intelligent inline inspection (or 'pigging').
    - Adam will present information on in-line inspections program (also known as 'pigging').

# Supply and demand for gas in Victoria – draft terms of reference

## Summary of proposed Terms of Reference:

### Actions:

- survey of the current gas supply and demand dynamics
- items announced post the publication of the GSOO and VGPR
- survey Victoria's decarbonisation and electrification legislation and other policy statements
- *wide engagement with industry participants (new)*
- time horizon of 2040 with a particular focus on the period up to 2028

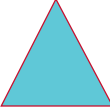

### Deliverables:

- supply and demand forecast to support the 2023-27 VTS access arrangement - volumes and MDQ
- draft written report, circulated to stakeholders for comment
- attendance and presentation at a workshop with the stakeholder forum,
- final public written report, reflecting comments and inputs from stakeholders

### Timing

- draft written report is to released by 31 July 2021 for a workshop in mid-August (date TBA)
- final written report by 31 August.

# Forecasting operating expenditure

- Two approaches to forecasting operating expenditure
  - Bottom up approach
  - Top down approach
- Bottom up 
  - Examine all costs and forecast them out for five years
  - Beneficial if starting from scratch or facing big changes in operating costs
- Top down 
  - Most common approach is the base, step and trend method
  - Commonly accepted by the AER
  - The base step trend model works in conjunction with the efficiency carry-over mechanism.

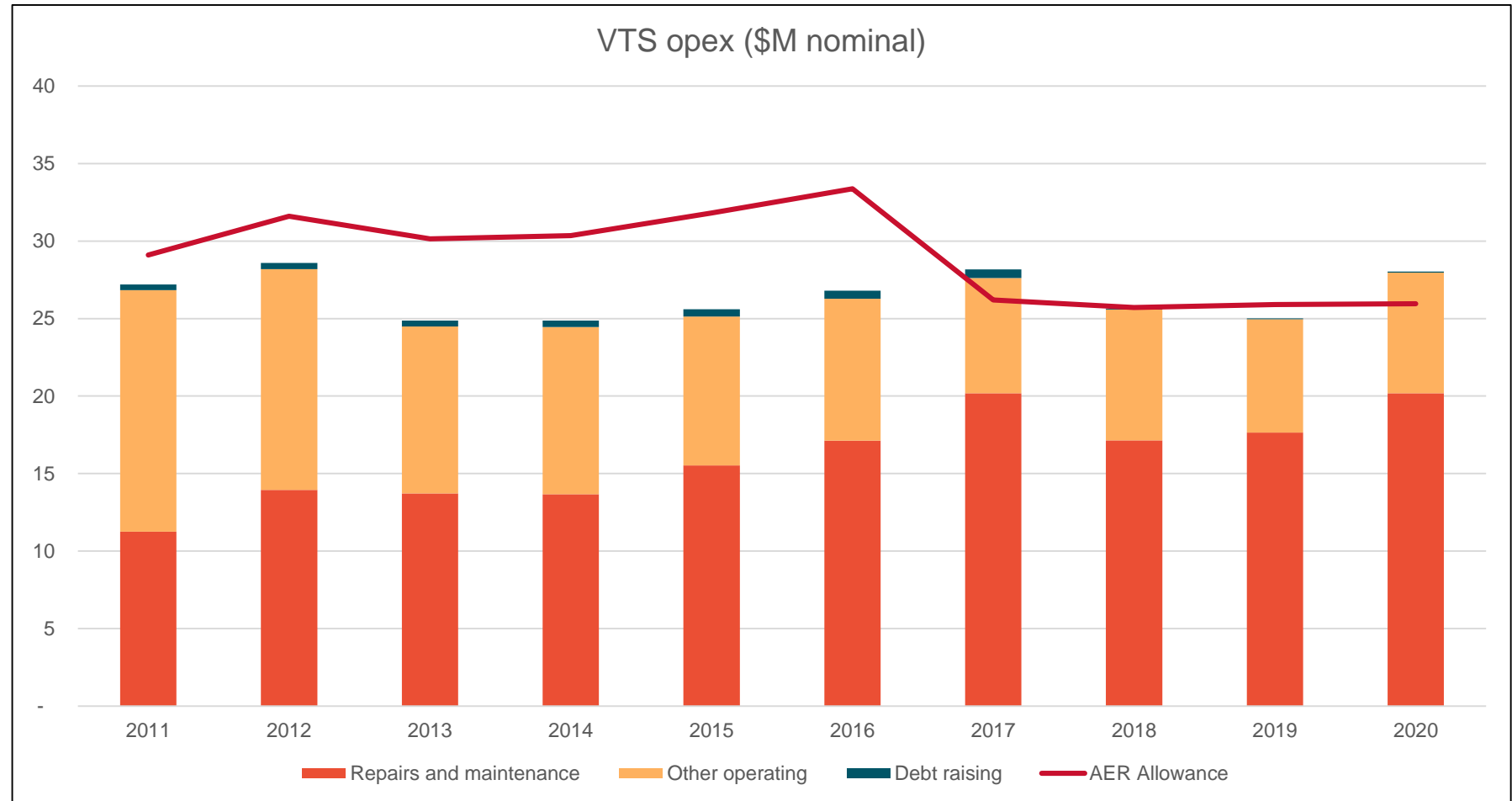
# VTS opex history

Actuals as reported to AER

2018-21: ~\$3M overspend relative to AER allowance

2020 increase driven by:

- A half-year increase in insurance premiums
  - Expecting further increases



# Adopting base-step-trend for VTS

## Base year opex

- We are proposing to use CY2020 as the base year.

## Trend

- We are proposing a rate of change based on forecast change in real labour costs only.
- The most current information prepared for the AER by Deloitte Access Economics (June 2019). We are proposing to use the national forecast because we are competing in the national labour market.

## Step changes

- We are anticipating a step changes cyber security costs and migration to cloud-based IT costs.

## Other costs

- We are anticipating debt raising costs. Debt raising costs will be based on the AER's benchmark debt raising unit rate to the debt portion of our regulatory asset base.

# Preliminary Base – Step – Trend analysis

- **2020 calendar year will be our Base Year**
  - Total Opex = \$28.03M (including \$0.06M AER-determined debt raising costs)
  - Trend is relatively flat 2018-21
- **We expect to see the following opex step changes:**
  - **Insurance**
    - Global increases in property, liability and D&O insurance costs only partially reflected in 2020 actual costs
    - VTS benefits from APA portfolio scale
  - **Cloud based computing**
    - APA 10-year-old systems no longer supported – moving to cloud based systems
    - Unclear how much will be capex vs opex (SaaS = Software as a Service)
    - VTS carries about 9-10% of these corporate costs
  - **Cyber security**
    - As part of recommendations associated with the Finkel Review 2017, the Australian Energy Sector Cyber Security Framework has been expanded to cover the gas sector. Gas transmission is ranked as high risk
    - Not included in 2020 calendar year opex – but likely to increase.

# Efficiency carryover – incentive – mechanism

## What is it?

- The AER has previously approved an **incentive mechanism** to encourage efficiencies in the operation of VTS.
- This incentive mechanism is the **efficiency carryover mechanism**.
- Efficiency carryover mechanism:
  - Provides an incentive to keep operating costs down
  - This reveals the efficient operating costs
  - Incentive applies for each year of the regulatory period
- Our overspend against our allowance means that we will have a negative efficiency carryover.



## Wrap up

- Summary of key outcomes from today
- Next step - Roundtable 8 on 14 July
  - First look at total revenue, revenue allocation and tariff structures
  - A look at the VTS Access Arrangement
- Forward any comments on capital program issues paper by 30 June
- Forward any further comments or questions to Scott and Nives.
- Note, APA is holding its first Stakeholder Engagement Forum on 28 June 2021 – hope to see you there...

**Thank you for participating,  
See you in July....**

**For further information**

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