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

**Roundtable 17 – Business narrative. Accelerated depreciation analysis. Revised proposal updates on key elements.**

28 July 2022



# Today's discussion & format

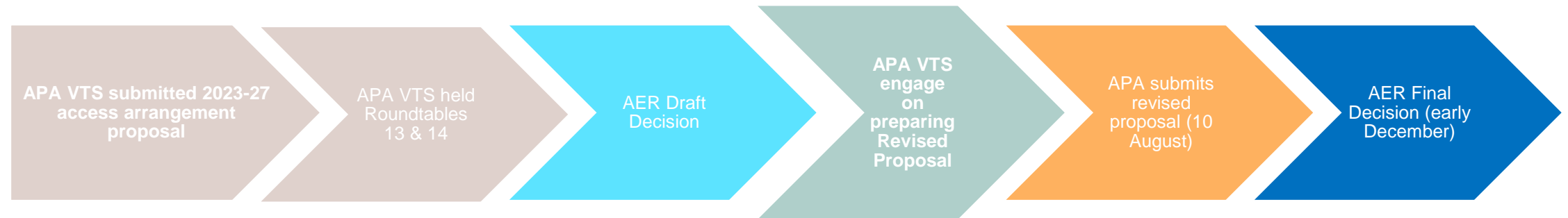
	Topics	Purpose
1	Welcome & Acknowledgement of Country	
2	Purpose today and of ongoing engagement	Update
3	Business narrative	Consult/ involve
4	Updated key positions	Consult/ involve
5	Accelerated depreciation – ACIL Allen to present scenario analysis (3pm)	Consult/ involve
5	Next steps	

*Note that the meeting will be recorded for internal purposes only.  
Video will not be distributed outside of APA without getting your agreement.*

*We are hoping to be more collaborative.  
We do encourage your views and feedback today.*

# Purpose of today

- R17 – Discussing the business narrative. Updates on key elements of revised proposal
  - AER Public Forum
  - *Where revisions to APA's proposal are required in response to this draft decision, we expect APA to engage with consumers on how they think APA should respond. Consumer views on how successful this has been?*



## Recent engagement:

- In R15 we asked for stakeholders for their suggested topics to engage on.
  - The only suggestion received was demand forecasting - this will be covered as part of ACIL Allen scenario analysis
- R16 – Engage on the accelerated depreciation, and discussion paper - Business narrative. CANCELLED due to MS Teams outage

# VTS Business narrative

# Discussion Paper on VTS business narrative

We received feedback from stakeholders wishing to see a business narrative to help them engage with issues raised as part of VTS access arrangement proposal.

The purpose of the discussion paper is present our views on the drivers, challenges, and opportunities for the VTS.

We are seeking to elicit views and expectations from stakeholders about the future for VTS for 2023-27 access arrangement and beyond.

## **Key theme: Balancing competing objectives (Discussed R12)**

During stakeholder engagement we characterised the current gas market environment as uncertain while at the same time having to balance competing objectives:

- Longer term forecast for declining consumption volumes vs. Consumers need for security of supply
- Risk of asset stranding vs. the need for ongoing investment to meet safety, integrity, and legislative obligations
- Safety and integrity vs. ageing assets and urban encroachment.
- Balancing the competing objectives are underpinned by impact on tariffs and affordability for consumers.

## **Since we submitted proposal - Fragility of the demand and supply balance in the east-coast region was revealed**

- Monday 18 July, AEMO issued warning of "threat to system security" due to low gasAEMO introduces administered gas spot price cap \$40/GJ in Victoria
- AEMO suspending the National Electricity Market on 16 June during 'perfect storm' of events
- Domestically we saw significant increases in inflation and interest rates and the election of Labor to Federal Government with its platform of reducing emissions to 43% below 2005 levels by 2030 under the Paris Agreement.
- At a global level, we are seeing the impact of the invasion of Ukraine on global fuel prices as Europe looks to reduce gas consumption and look to other markets.

# Drivers to deliver value for consumers

Drivers to deliver value to consumers are influenced by a range of internal and external drivers and APA business strategies.

Operation and investment in the VTS are influenced by a range of key drivers.

These drivers have been discussed during stakeholder engagement or were raised in submissions to the 2023-27 access arrangement proposal.

Meeting consumer needs

Meeting legislative obligations

Demand & supply balance

Ensuring security of supply

Government policy on net zero

Future fuel hydrogen

# Drivers to deliver value for consumers

## Meeting consumer needs

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National Gas Objective. “to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.”

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Energy transition is posing challenges to affordability for consumers. Energy costs have been exacerbated by the 2022 ‘energy crisis’ and ‘cost of living’ pressures

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Orderly transition means putting in place measures that will not expose vulnerable consumers and hard to abate industrial customers to a higher proportion of VTS costs

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How will transition impact use of the VTS?

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How will APA efficient investment be recovered?

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Most effective regulatory tool to balance gas affordability and recovery of efficient investment is accelerating depreciation of assets

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# Drivers to deliver value for consumers

## Demand & supply balance

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APA relies on AEMO for forecasting of demand as an important driver for investment decisions

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In 2022 AEMO raised concerns about a tight supply demand balance in the south-east regions of Australia from 2023 and 'growing gas supply scarcity challenge' of traditional supply from Bass Strait. AEMO assessed that:

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- In the short term to 2026, forecast risks can be mitigated by completion of committed infrastructure, development of anticipated projects, and – especially for winter 2023 – demand side solutions. To help alleviate concerns about winter 2023, AEMO mooted the possibility of duplication of the Winchelsea compressor on the SWP

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- After winter 2023, through to 2026, shortfall risks are expected to be further reduced by anticipated projects including Port Kembla Energy Terminal, Golden Beach and other Victorian offshore field developments

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- In the longer term, new sources of supply will be needed even though annual domestic gas consumption is forecast to decline.

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Demand and supply are largely outside of APA's control but will have huge implications for the VTS?

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We will discuss this in more detail during the presentation by ACIL Allen on accelerated depreciation

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We distributed a Paper on Load and demand forecasts on 15 July.

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# Drivers to deliver value for consumers

## Meeting legislative obligations

VTS is subject to Victorian pipeline legislation governing the safe operation of pipelines

Operate to minimise **as far as is reasonably practicable**: hazards and risks to the safety of the public arising from the pipeline operation; and hazards and risks to the environment arising from the pipeline operation

Primary drivers for replacement/ Stay in Business programs are safety, reliability, integrity and meeting regulatory obligations

APA's VTS Lifecycle Management Plan and the replacement/ stay in business capital program is focused on maintaining safety, integrity and reliability of the VTS infrastructure

Information technology and Operating Technology support the operation of infrastructure and corporate activities

VTS is critical infrastructure under the Security of Critical Infrastructure legislation

What's in it for consumers? Meeting legislative obligations ensures safe, reliable and secure service for consumers.

# Drivers to deliver value for consumers

## Ensuring security of supply

Investment in the Western Outer Ring Main and additional compression on the South West Pipeline have been driven by security of supply concerns

In 2022, APA responded to security of supply concerns for winter 2023 by the Victorian Government and AEMO by revising the 2021 proposal

In March, APA submitted a proposal for a second compressor at Winchelsea. APA worked urgently with compressor manufacturers to secure a compressor in time for winter 2023. The AER has accepted this updated proposal. We have commenced investment at own risk and no return for 2022

This is an example of the dynamic environment that we are in, and which requires the need to be flexible and respond quickly to the changing environment

Further, on Monday 18 July, AEMO issued warning of "threat to system security" due to low gas storage levels at the Iona underground gas storage due to run on gas for electricity generation, coal plant outages, and high heating demand.

This situation reinforces the prudent investment in WORM – *What's it in for consumers? From May 2023, will help to get more gas into Iona Storage during winter. Reduce risk on gas outages*

One of the actions in the Victorian Gas Substitution Roadmap states that the Victorian Government will work with gas infrastructure proponents to ensure timely investment to support secure and reliable supply while avoiding overbuild and minimising the risk of stranded assets

Noting BSL comments at AER Public Forum that fast tracking investment in long lived assets is not appropriate, and requesting greater consideration of demand management.

### Question

If there is a need for additional infrastructure for security of supply within the 2023-27 period, how should APA deal with this situation?

# Drivers to deliver value for consumers

## Government policy

In recent months, energy and climate policy priorities have become clearer with Federal Labor Government committing Australia to reducing emissions to 43% below 2005 levels by 2030

Victorian Gas Substitution Roadmap released in July provides guidance on the Victorian Government's priorities

- Changes to the Victoria Planning Provisions in 2022 to remove the requirement for new housing developments to be connected to gas.

- Focus on shifting residential gas users from gas to electricity by offering incentives to switch appliances

- Phasing out incentives for gas residential appliances by the end of 2023

- Consider establishing a renewable gas scheme, and renewable gas targets, to help drive investment in gas substitution and guide transition planning for businesses, consumers, and energy market participants

Implications for VTS are not certain. It will depend on how consumers respond to government incentives to switch to electricity, the economics of hydrogen and any further government action

# Drivers to deliver value for consumers

## Future fuels hydrogen

VGSR models outcomes where natural gas is displaced by hydrogen and biomethane by 2030s and 2040s

Victorian Government considering a renewable gas scheme and targets to help drive investment

Energy Safe Victoria articulated the need for a safety assessment before any hydrogen will be allowed to be introduced into a pipeline. AEMO supported the hydrogen study in its submission to the proposal

APA considers that to keep options open for hydrogen that it would be prudent to start testing for safety and integrity during 2023-27

In response to stakeholder submissions and AER draft decision we are reassessing study options, considering undertaking the study over two regulatory periods, preparing more detailed risk assessment, considering scope for government support.

In response to concerns about affordability, we are proposing to depreciate to study over the life of the pipe.

### Question

Do you consider hydrogen to be a potential energy source in the future?  
If yes, then what should we be doing to ensure that consumers and industry are able to access hydrogen?

# In times of uncertainty, we need to keep options open

APA welcomes the foresight shown by the AER in the ***Regulating gas pipelines under uncertainty information paper***.

The risks identified by the AER are real world risks being faced by APA VTS.

We have drawn on the AER's information paper in developing the VTS business narrative.

The regulatory framework was designed during times of relative stability and there is a limit to what we can propose to be flexible and manage uncertainty.

The regulatory toolkit we have now includes:

- Accelerated depreciation to start now before there is a large-scale shift by residential gas consumers to electrify (otherwise are we 'kicking the can down the road"?)
- Minimising capital expenditure needed to meet 'as low as reasonably practicable' requirements
- Minimising any increase in tariffs
- Undertaking a study to test safety and integrity of hydrogen on VTS
- Applications to AER for advance determinations with regard to future capital expenditure (pre-approval under National Gas Rules r.80) in response to uncertain events
- Cost pass through for pre-approved capex.

In the longer term, as the transportation of gas along the VTS will increasingly compete with electricity, batteries, and renewable sources of energy – and even with gas distribution businesses, there may be no need for economic regulation.

## Questions

Have recent global and domestic events changed your views in any way about the VTS access arrangement? If so, how?

Are there other regulatory tools we should consider to allow for more optionality?

What else should we consider as part of the business narrative for VTS?

# Updated key positions

# Updated position elements of AER Draft Decision

## What we have accepted

- Rate of Return - AER Rate of Return instrument comes into effect early 2022
- Operating expenditure – efficiency mechanism
- Winchelsea second compressor - \$60.1 million capex allowance
- Rejection of SWP570 proposal for compressors at Pirron and Stonehaven
- AER decision to reject on Rule 80 for SWP further expansion
- AER decision to reject some amendment to Tariff variation mechanism.

## What we do not accept and are resubmitting information on:

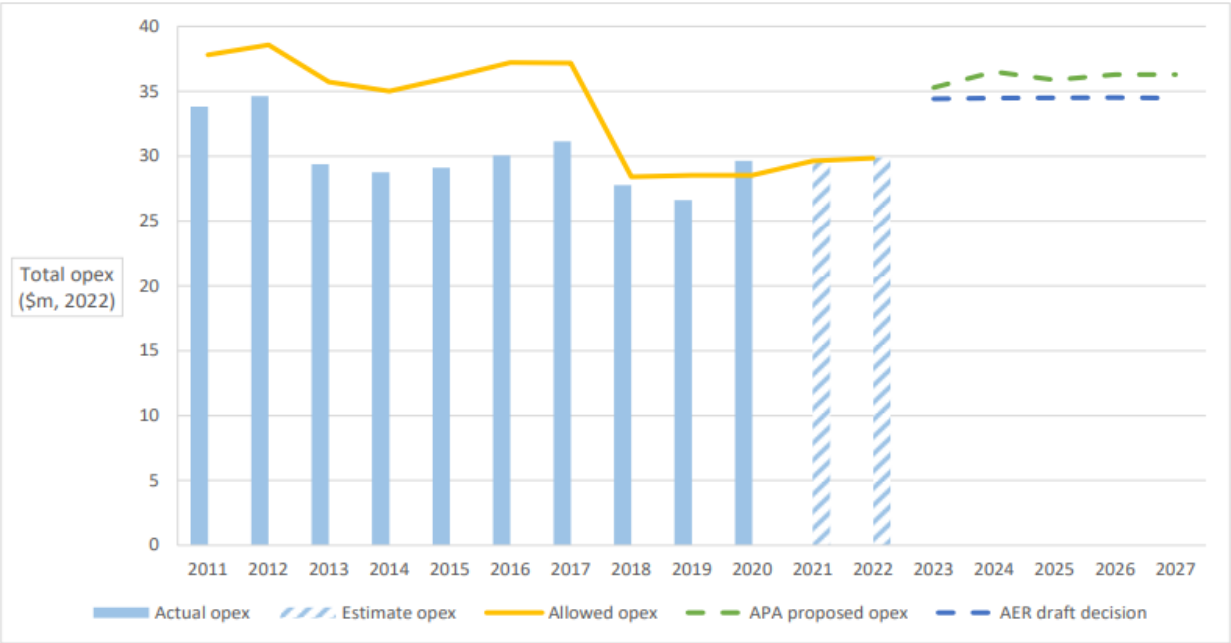
- Accelerated depreciation – we will be resubmitting scenario analysis
- Replacement capital expenditure
- Operating expenditure – step changes
- SoCI expenditure
- Information Technology and Operational Technology projects
- Hydrogen safety & integrity study

## Information we are updating:

- Western Outer Ring Main capital expenditure forecast
- Demand forecasts

# Update on operating expenditure revised forecast

Historical and forecast opex (\$million, 2022)



APA resubmitting information on step changes for

- Property taxes
- Winchelsea
- SoCI
- Information Technology & Operational Technology
- Carbon offsets.

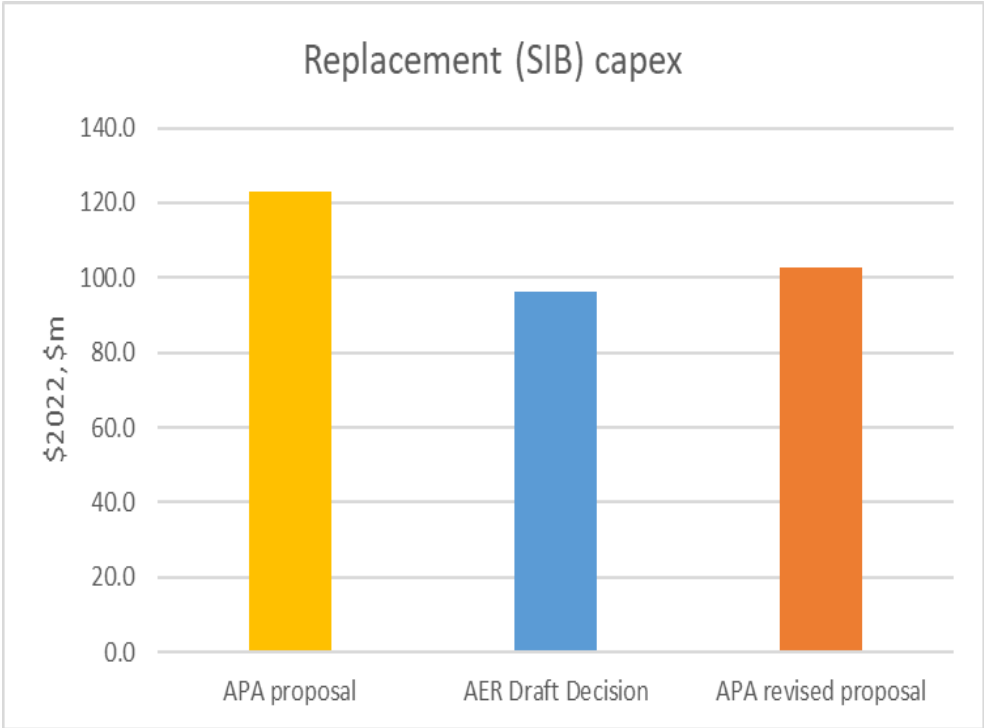
Source: AER Draft Decision, APA Victorian Transmission System (VTS) Access Arrangement 2023 to 2027, Overview, p.23



# Replacement capex – stay-in business

## Update

- APA proposed \$122.9 million for 31 programs & projects
- AER did not accept the proposal forecast and allowed \$96.3 million instead
- Of the 31 projects proposed by APA, AER approved 18, provided replacement forecasts for three and did not approve capex for 10 projects
- AER gave weight to AEMO's submission to APA's proposal which questioned the need for investment in Brooklyn Compressor Station (\$10.3m); Wollert Compressor Station A (\$1.3m), Iona Aftercooler (\$3.2m) and several other projects
- APA liaised with AEMO to discuss projects that it had not supported and took this into consideration in preparing revised business cases
- APA's revised proposal is likely to be around \$103 million based on:
  - Undertaking an end-of-life study for Brooklyn Compressor Station
  - Undertaking an end-of-life study for Wollert Compressor Station A
  - Accepting AER decision to reject Iona Aftercooler project
  - Resubmitting information for Waterbath Heater Integrity; Battery chargers
  - Accepting AER reduced allowance for Emergency spares, Liquids management, Mainline Valve upgrades
  - Deferral of AER rejected projects
  - New business case for Pipeline Fracture Resistance assessment (\$1.4m). The driver for this is a new requirement in AS 2885 which will come into effect 2023.



# Security of supply (expansion) revised capital expenditure forecast

In the 2022 updated WORM business case, the forecast cost to complete the WORM was \$185 million (excluding overheads).

The revised forecast was based on the best information available at the time but had not been Board approved.

We noted in the business case that there may be further changes to the forecast costs to address matters from the EES.

Further uncertainty was flagged because construction contracts had not been market tested and outcomes from the depending on the tenders received for construction.

### Timing of capital expenditure for WORM

The timing of the forecast costs are expected to be:

\$m	2018	2019	2020	2021	2022	2023	2024	Total
<b>WORM project</b>	0.8	6.7	8.7	22.3	117.8	59.5	1.0	<b>216.8</b>

In late May 2022, APA Board approved additional expenditure for the WORM project bringing the total APA Board approved expenditure to \$216.8 million.

The project has incurred additional costs largely linked to the increase in costs during the two-year delay as a result of having to prepare an Environmental Effects Statement and having to implement additional recommendations from the EES.

As tenders from construction and other services are being received we are finding that the current squeeze in the labour market and global supply chain backlogs are affecting the bid prices from contractors to undertake the work.

**Do you have any comments or questions?**

**What would you like to see in the revised proposal?**

*Noting AER's question - Where revisions to APA's proposal are required in response to this draft decision, we expect APA to engage with consumers on how they think APA should respond*

# VTS scenario analysis for accelerated depreciation

**Paul Hyslop**  
Chief Executive Officer  
ACIL Allen

# Next steps

## VTS key activities and dates

### Phase 4 - After we've submitted proposal

Who	Date	Activity	Topics
APA VTS	13 April 2022	Roundtable 13	AEMO to present on GSOO/ VGPR. Other updates.
APA VTS	25/05/2022	Roundtable 14	Updates & discussion of submissions
AER	30 June 2022	AER Draft Decision	AER publishes Draft Decision
APA VTS	12/07/2022	Roundtable 15	Discuss AER Draft Decision
APA VTS	21 July /2022	Roundtable 16 - Cancelled	ACIL Allen present on scenario analysis for accelerated depreciation. VTS business narrative
AER	25 July 2022	AER Public Forum	Draft Decision
APA VTS	28 July 2022	Roundtable 17	Revised proposal - collaborating on key elements of revised proposal
<b>APA VTS</b>	<b>10 August 2022</b>	<b>Revised proposal</b>	<b>APA VTS submits revised proposal</b>
Stakeholders	06 September 2022	Stakeholder submissions	Submissions on revised access arrangement proposal and draft decision
AER	Early December 2022	AER Final Decision	AER publishes final decision

# Thank you for participating on VTS engagement!



A BIG THANK YOU TO YOU!



WE HOPE YOU FOUND VALUE THIS ENGAGEMENT USEFUL



WE HAVE LEARNT A LOT AND CERTAINLY DID BENEFIT FROM YOUR PARTICIPATION



SCOTT AND I ARE ALWAYS AVAILABLE TO MEET WITH YOU



WE DO INTEND TO CONTINUE ENGAGING ON VTS

**For further information**

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