

27 October 2014



Mr Adam Petersen
Director
Australian Energy Regulator
Level 2, 19 Grenfell Street
Adelaide SA 5000

Dear Mr Petersen,

Proposed 2015 Victorian Reference Tariffs

This letter sets out Australian Gas Networks' (AGN - formerly known as Envestra) reasons for varying its Reference Tariffs to apply from 1 January 2015. AGN is proposing to vary its Reference Tariffs in a manner that is consistent with clause 4.3 of the *Access Arrangement for Envestra's Victorian Gas Distribution System* (hereafter referred to as the Access Arrangement).

AGN has however submitted two tariff models and two tariffs schedules. The first tariff model and schedule (attachment 1 and 2 respectively) utilize an x-factor of -2.0 per cent, which x-factor was approved with the AER's Further Final Decision for the Victorian network in April 2013. This x-factor is set out in Annexure D of our approved Access Arrangement.

The second tariff model and schedule (attachment 3 and 4 respectively) utilises an x-factor of -5.1 per cent, which x-factor has been proposed by AGN as part of its Mains Replacement pass-through application submitted to the AER in July 2014.

The x-factor of -5.1 per cent includes the x-factor of -2.0 per cent set out in the Access Arrangement plus an additional -3.1 per cent, which reflects the impact of the mains replacement pass through application. Under the Access Arrangement, AGN is allowed to apply for a pass through when a Mains Replacement Event has occurred, which event is defined in the Access Arrangement as:

"Mains Replacement Event means the event whereby Envestra:

- (a) completes 268 kilometres of its planned total completion of Historical Volumes of Mains Replacement during the course of the Fourth [2013 to 2017] Access Arrangement Period; and*

- (b) *costs are incurred, or are to be incurred, by Envestra in the remainder of the Fourth Access Arrangement Period to complete a volume of Mains Replacement in excess of the Historical Volumes.*

The Mains Replacement Event occurred in June 2014. AGN is seeking funding for an additional 331km of mains replacement for a total of 696km over the 2013 to 2017 Access Arrangement period. The AER however has indicated the potential to only approve an additional 271km of mains replacement for a total of 636km.

Whether additional mains replacement of 331km or 271km is ultimately approved by the AER will have no impact on the calculated x-factor of -5.1 per cent. This situation arises as the 60km difference in mains replacement will fall in the final year (2017) of the current Access Arrangement period, and as such, will only be reflected in the RAB from 1 January 2018.

This approach is also consistent with the implementation of the mains replacement program, with the process for tendering works through to 30 June 2016 either complete or close to being completed. Therefore any impact of the decision to approve 331km or 271km on x-factors, and subsequently prices, will be reflected in the next 2018-2022 access arrangement period, not the current 2013-2017 access arrangement period. This explains why there is only one set of tariffs to consider for both a total volume of 696km or 636km.

Reference Tariffs: Domestic, Commercial and Demand Haulage Reference Services

The analysis presented below is based on the x-factor as approved with the AER's Further Final Decision, which x-factor is -2.0 per cent.

The proposed adjustments to the Reference Tariffs for domestic (Tariff R), commercial (Tariff C) and demand (Tariff D) Haulage Reference Services to apply from 1 January 2015 are being made pursuant to clause 4.3 of the Access Arrangement. This allows Reference Tariffs to vary in accordance with a weighted average tariff basket mechanism, as detailed in section 4.4 and Annexure D of the Access Arrangement. Annexure D contains a Reference Tariff Control Formula and a Rebalancing Control Formula.

In broad terms, the Reference Tariff Control Formula allows Envestra to change its tariffs so that the revenue derived from each of the Haulage Reference Services does not increase by an amount that is greater than $(1+CPI)x(1-X)x(1+L)$. The CPI is the change in the CPI for the 12 months to September 2014, which CPI is 2.3 per cent. The Licence Fee factor is 0.00% and X factor -2.0 per cent. The combination of the CPI, L factor and X factor results in an allowed change in Reference Tariffs for 2014 of 4.3 per cent.



The Rebalancing Control Formula allows Envestra to change its tariffs so that the change in the revenue derived from an individual tariff within a particular category of Haulage Reference Service is no greater than $(1+CPI) \times (1-X) \times (1+L) \times (1+2\%)$. This allows a particular tariff to increase by no more than 6.4 per cent.

Envestra's proposed 2015 Reference Tariffs comply with both the Reference Tariff Control Formula and the Rebalancing Control Formula. This has been demonstrated by the model provided to the AER setting out the application of the above formulae and the resultant Reference Tariffs. The models, tariff schedules and Licence Fee advice comprise attachments 1 to 5 respectively of this submission.

The Reference Tariff Control Formula and the Rebalancing Control Formula require the quantities used to be the period two years prior to the year that the proposed tariffs take effect, which in this case is 2013. An independent review verifying the gas quantities has been undertaken and the associated report is provided as attachment 6.

Impact on Users

The table below shows the average impact on end users of the proposed change in tariffs on a GST exclusive basis.

Change in Average Customer Charge

Central Zone

Component	2015 (\$)	2014 (\$)	Quantity (p/a)	Cost Change (\$)
Tariff R	314.7	301.1	48.2 GJ	13.6
Tariff C	1,221.4	1,185.7	323.0 GJ	35.7
Tariff D	21,917.6	21,003.1	21.4 GJ MHQ	914.5

North Zone

Component	2015 (\$)	2014 (\$)	Quantity (p/a)	Cost Change (\$)
Tariff R	269.3	257.3	44.2 GJ	12.1
Tariff C	904.1	876.3	250.9 GJ	27.9
Tariff D	31,230.1	29,927.0	33.1 GJ MHQ	1,303.1



Murray Valley Victoria Zone

Component	2015 (\$)	2014 (\$)	Quantity (p/a)	Cost Change (\$)
Tariff R	243.3	231.3	33.2 GJ	12.0
Tariff C	857.4	830.1	195.7 GJ	27.3
Tariff D	28,753.0	27,524.6	24.7 GJ MHQ	1,228.4

Bairnsdale Zone

Component	2015 (\$)	2014 (\$)	Quantity (p/a)	Cost Change (\$)
Tariff R	395.9	376.3	27.5 GJ	19.6
Tariff C	3,494.0	3,401.5	804.6 GJ	92.5
Tariff D	17,576.4	16,843.1	8.2 GJ MHQ	733.3

Reference Tariffs: Ancillary Reference Services

Envestra has also varied its Ancillary Reference Tariffs in a manner that is consistent with clause 4.4.2 of the Access Arrangement. Ancillary Reference Tariffs are to be adjusted by the annual change in the CPI, which is also calculated as the change in CPI for the 12 months ending September 2014. The calculation and resultant tariffs also form part of attachments 1 and 2.

Carbon Pass Through Tariffs

The carbon tax repeal legislation received the Royal Assent on 17 July 2014, taking effect retrospectively from 1 July 2014. AGN ceased applying the carbon element of the tariff from 1 September 2014. AGN has used Formula 4 of Annexure D of the Access Arrangement to determine the 2015 Carbon Pass Through. Due to an under recovery of the carbon permit expense for 2013/14 a small positive carbon tariff will continue to apply for 2015.

The Carbon Pass Through Tariff calculation and resultant tariffs also form part of attachments 1 and 2. The supporting "S22 Liable Entity Report 2012/13" and the draft of "S22 Liable Entity Report 2013/14" comprise attachments 7 and 8.

Summary

Attachment 1 comprises the model demonstrating the derivation of the proposed Reference and Carbon Pass Through Tariffs while attachment 2 comprises the tariff schedule detailing the proposed tariffs to apply from 1 January 2015 for the current approved x-factor of -2.0 per cent. Attachments 3 and 4 comprise the same model and tariff schedule but for an x-factor of -5.1 per cent, which x-factor reflects AGN's mains replacement pass through.



Attachment 5 provides the licence fee advice while attachment 6 comprises the findings of the independent review of the 2013 quantities. Attachments 7 and 8 comprise S22 Liable Entity reports for 2012/13 and 2013/14 in support of the carbon tariff calculation.

Please contact me on 08 8418 1112 should you wish to discuss this matter further.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Peter Bucki', written in a cursive style.

Peter Bucki
Manager Regulatory Strategy

