

Consumer
Challenge
Panel

AGN South Australia Gas Access Arrangement 2021 - 2026

AER Public Forum
27 July 2020

CCP24
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AGN's head office is located on Kaurana Land, their network traverses the lands of many Indigenous nations, we respect these lands and honour the associated cultures.



AER Consumer Challenge Panel – our role:

Consumer
Challenge
Panel

- advise the AER on whether the network business's proposal is in the long-term interests of consumers; and
- advise the AER on the effectiveness of network business's engagement activities with their customers and how this is reflected in the development of their proposals.
- CCP24 was appointed in July 2019 to review AGN SA and Evoenergy (ACT) Access Arrangement 2021-26 resets

Reset Context – significant challenges:

- Resets occurring in the context of the most fundamental challenge to the gas market in decades
 - how do gas networks respond to Governments moving towards net zero emissions policies in a timeline considerably less than the asset life of a large part of the existing and proposed asset base?
- CCP24 is presented with the 'Tale of two networks' both of which are investing heavily in a potential hydrogen future but which have taken quite different approaches to their 2021-26 proposal
 - AGN presenting a 'business as usual' plan, with a future hydrogen vision
 - Evoenergy operating with an explicit ACT Government policy for net zero emissions by 2045
 - The Future of Gas is here, now. These AA proposals (and JGN) reflect major questions re "future of gas"
- COVID-19

COVID-19 – expected impacts

- Financial impacts for residential and small business customers will be ongoing, higher unemployment expected
- Difficulties in paying utility bills will continue
- Strong focus on price reduction is even more important
- Regular reviews of forecasts eg demand, labour costs, connections, and the changing environment will be necessary
- Engagement needs to continue, it's more important than ever
- Embrace uncertainty, be flexible try good ideas and accept the inevitable mistakes.
- Consider the triggers and process for re-openings

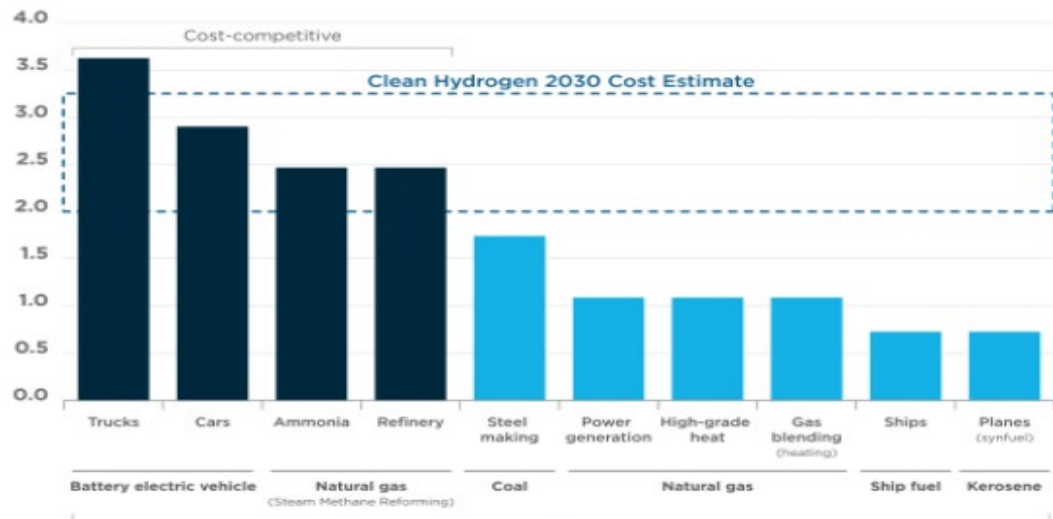
AGN Leadership – future hydrogen vision

- AGN is playing an active leadership role in the development of hydrogen as a 'green' reticulated gas for future use
- Tonsley hydrogen feed-in trial
- Installation of an electrolyser and HyP SA
- Part of tender to 'buy' future hydrogen
- ARENA projects
- Active collaborator with other gas businesses and research

Hydrogen and stranded asset risk

- Optimistic view in National Hydrogen Strategy – by 2030 will know if hydrogen is competitive for some applications – unlikely for gas reticulation
 - Stranded asset risk if net zero emissions target by 2045-2050 and no accelerated depreciation
 - Gradual approach to accelerated depreciation not a binary decision and consistent with a 'real options' framework
- AGN proposes to leave consideration of accelerated depreciation until the 2026-31 period
 - By which time we will have a good idea if 10% blend works technically. Iron mains replaced

Figure 1.3 Breakeven cost of hydrogen against alternative technology for major applications, in 2030.

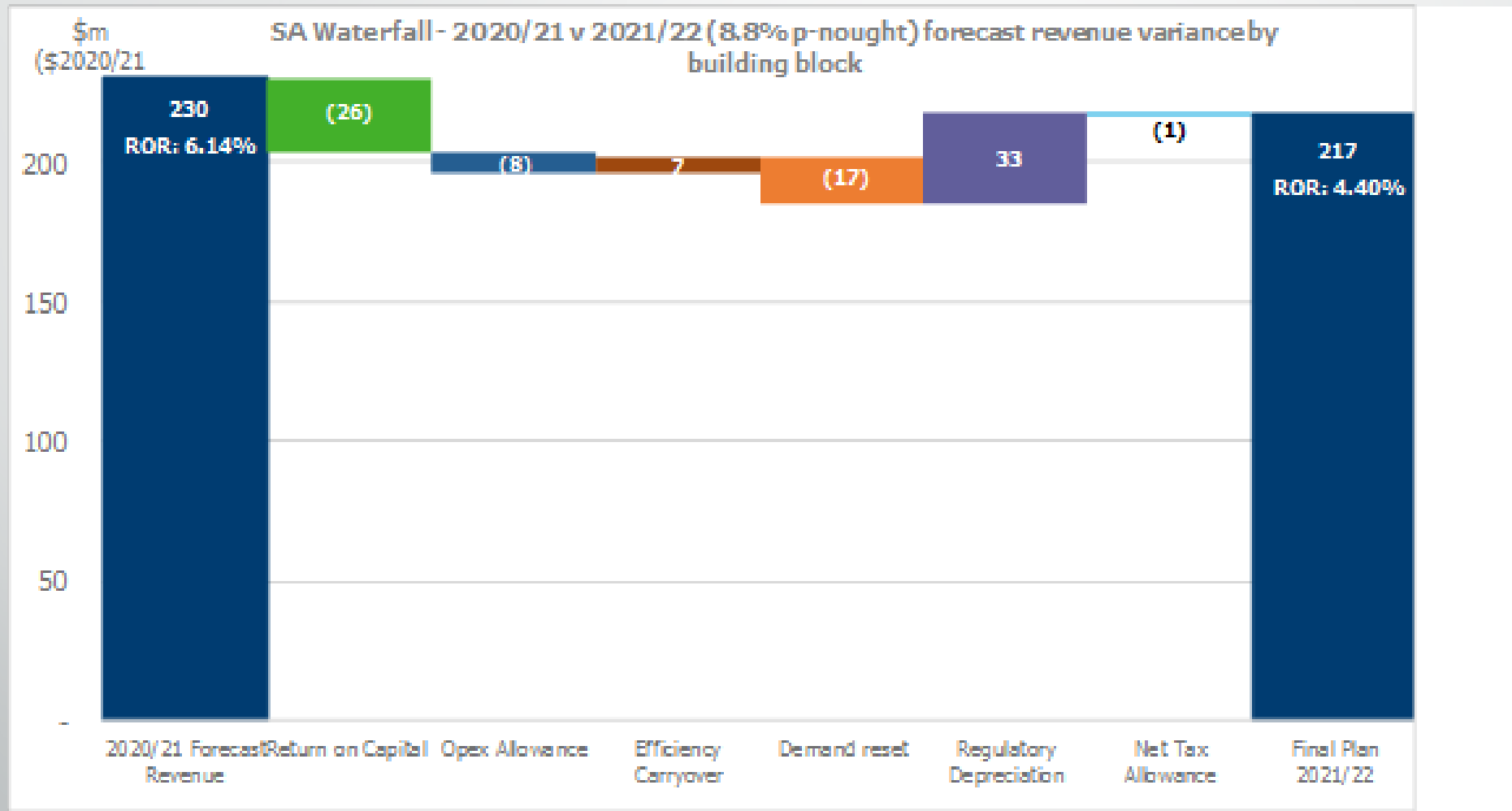


Objective	Recommendations
(i) Given AGN is not proposing accelerated depreciation, how should consumers assess AGN's proposed \$160m expansion capex where it has an asset life greater than the likely date of a zero emissions target?	Matters that AGN should consider including in the next stage of its consumer engagement to ensure its consumers are supportive of its approach
(ii) Examine at a high level the suitability of the National Gas Law and Rules to consider stranded assets in the changing Government policy environment	A holistic review by the AER of these rules to assess whether they are fit for purpose for the next 10-20 years

AGN: Key aspects of Proposal

- Nominal price fall of 7% on 1 July 2021 then annual increases of 1.2% pa (plus inflation)
- Price would have risen without fall in WACC – which partly offsets large rise in regulatory depreciation from mains replacement
- Opex 8% higher than current period
- \$8 million in step changes, and increase in UAFG costs
- Productivity growth factor 0.4% pa
- Capex 3% lower than current level
- RAB increase of 14%, RAB per customer increase of 8%
- New Capital Efficiency Sharing Scheme, Network Innovation Scheme

Price would have increased without WACC fall



AGN Consumer Engagement



Stage 1 Strategy and research

Feb - May 2019

Purpose

We engaged with stakeholders to better understand customer needs and to consult on our proposed engagement approach.

IAP2 Spectrum
CONSULT/INVOLVE

Key Deliverables

Stage 1 Engagement Report

We published our engagement strategy: Stage 1 Stakeholder Engagement Report.



Stage 2 Developing our Draft Plan

May 2019 - Feb 2020

Purpose

In this stage we ran a series of engagement activities designed to inform the development of our Draft Plan.

IAP2 Spectrum
INVOLVE/COLLABORATE

Key Deliverables

Stage 2 Engagement Report

We published summary reports of customer and stakeholder input into developing our Draft Plan and outcomes of our co-design workshops.



Stage 3 Consultation on our Draft Plan

Feb - Apr 2020

Purpose

In this stage we focussed on public consultation on our Draft Plan.

IAP2 Spectrum
CONSULT/INVOLVE

Key Deliverables

Draft Plan

We reported on all customer and stakeholder feedback and how feedback influenced our plans.



Stage 4 Refinement and engagement

Apr - June 2020

Purpose

Consultation feedback from Stage 3 was used to finalise our plan.

IAP2 Spectrum
INFORM/INVOLVE/CONSULT

Key Deliverables

- Final Plan to the AER on 1 July 2020
- Final Customer Engagement Report
- Final Plan Customer Overview

Major Engagement Topics

Price & affordability

Hydrogen / Future of gas

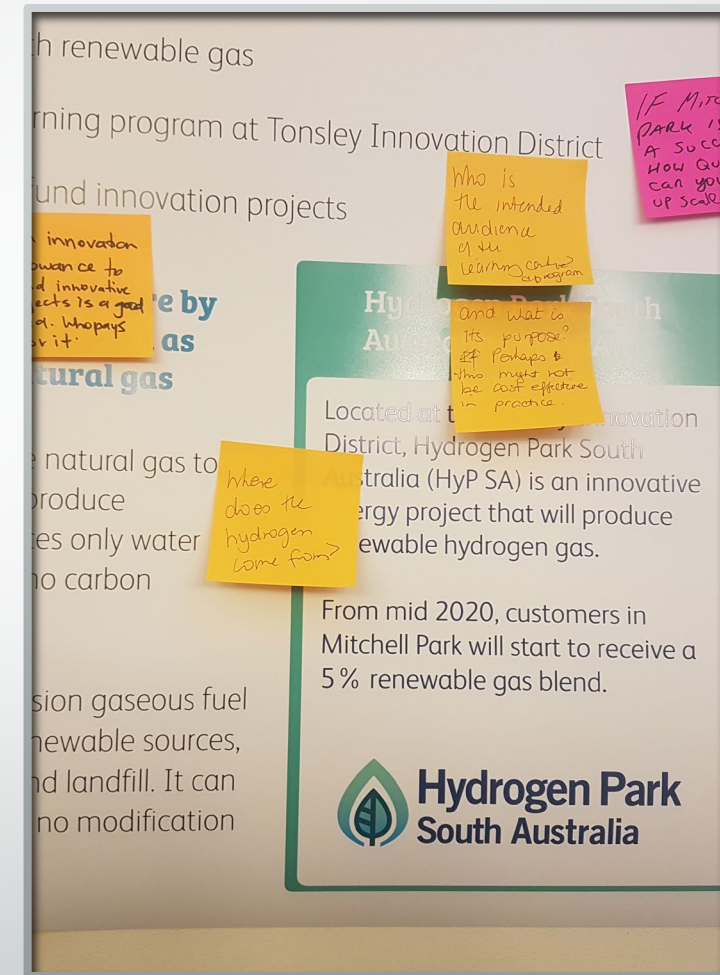
Unaccounted for gas

Education Centre

Connecting with Customers

Vulnerable Customers

Innovation



CCP Overview of AGN Engagement

- AGN delivered the engagement program that they have claimed
- Obvious and ongoing involvement of CEO and senior staff
- Consumer and stakeholder input heard and acted upon
- “Nothing Flashy” rather a high-quality engagement program very well delivered
- Ongoing engagement commitments including re Vulnerable Customers and the future of gas / hydrogen

Capex

AGN CAPEX Priority (\$2020/21)	Current AA (draft Plan)		Draft Plan	Next AA
Safety and Reliability	388.3	(375.5)	387.4	389.0
Growing the Network	175.9	(194.1)	159.9	159.0
Customer Service	35.1	(40.3)	32.1	30.9
Total	599.3	(609.8)	579.4	578.8

- Lodged AA very similar to Draft Plan – consistency
- Lodged AA about 3% lower than current AA expenditure
- Main Capex Drivers
 - *Mains replacement aka "Safety and Reliability"*
 - *Demand*
 - *Market Expansion*
 - *"Customer Services"*

System Capex – CCP comments

- There is a strong case for approaching capital as a finite resource, asking at every point “what impact will this expenditure have on affordability for all customers over the longer term?”
- Mains replacement program is established and this AA will see the end of this substantial work
- Falling demand (and COVID uncertainty potentially further reducing demand, industrial in particular) leads to asking whether demand related capex could be pared back further.
- Market Expansion! We understand AGN argument that no network to major new subdivisions means blocking out future developments from gas, and (hopefully) an affordable hydrogen future. But what is reasonable cost and who is shouldering the cost burden?

“Customer Service” is largely meter replacement. Initial inspection suggests this is reasonable – though nomenclature a little confusing.

Non System Capex

- **IT Systems, \$36.5m - more modest than current AA period, but**
 - Have benefits from previous period IT Systems expenditure been recognised?
 - Are deferrals from current period allowance included?
 - Are all IT System investments necessary in the next period?
 - Are cost estimates reasonable?
 - Are allocations between AGIG group members appropriate?
 - Are allocations between AGN SA and service provider APA appropriate?

Opex

	2016-21 (\$21m)		2021-26 (\$21m)	
	Allowance	Forecast	Draft	AA
Excluding UAFG	\$340	\$290.3	\$281.3	\$310.2 (+ 8% on forecast)
UAFG	\$62.5m (\$15)	\$40.3	\$48.8	\$47.2
Overheads capex to opex			\$23.4	0
Total	\$363.6	\$330.5	\$353.6	\$357.4

- Applies AER approach of base/step/trend
- Benchmarking indicates proposed base year 2019/20 is efficient
- Three step changes - Draft Plan had none – ‘we intend to absorb these step changes into our cost base’
 - Vulnerable customer assistance programme (\$3.9m) - look at more closely in our submission
 - Digital customer experience (\$1.4m)
 - Increased insurance premiums (\$3m) – common issue across networks – holistic AER approach?
- Trend
 - Growth in customer numbers – how does this sit with the potential for stranded asset risk?
 - Average of Deloitte/BIS labour cost growth + zero materials growth
 - ACIL Allen analysis basis for proposed 0.4%/year productivity vs zero in Draft Plan – look to AER analysis of robustness of this given AER yet to develop gas network productivity measures
- UAFG – what is controllable by AGN? What is impact of mains replacement?
 - Incentives for reducing controllable UAFG (AIA report)?
 - Examine increased cost - Core Energy price assumptions out of date?

Incentives

➤ Opex

- Support application of EBSS in 2021-26
- No productivity offered (and none expected by the AER) in current period – opex forecast expected to result in EBSS credit to AGN in 2021-26
- AGN proposing 0.4% for 2021-26 vs 0.74% for Jemena NSW and 0.5% for Evoenergy
- Key issue around productivity assumption is “how much goes 100% to consumers and how much is shared 70/30 between consumers/networks?”
- Two aspects to efficiency (i) movement out of the efficiency frontier and (ii) movement toward that efficiency frontier – electricity network productivity only concerned with (i)
- Look forward to the AER’s forthcoming work on gas network productivity on both (i) and (ii)

➤ Capex

- Support introduction of ‘contingent’ CESS with performance measures/targets/weightings
- Question around capex included eg what if SA government announces a net zero emission target?

➤ Network Innovation

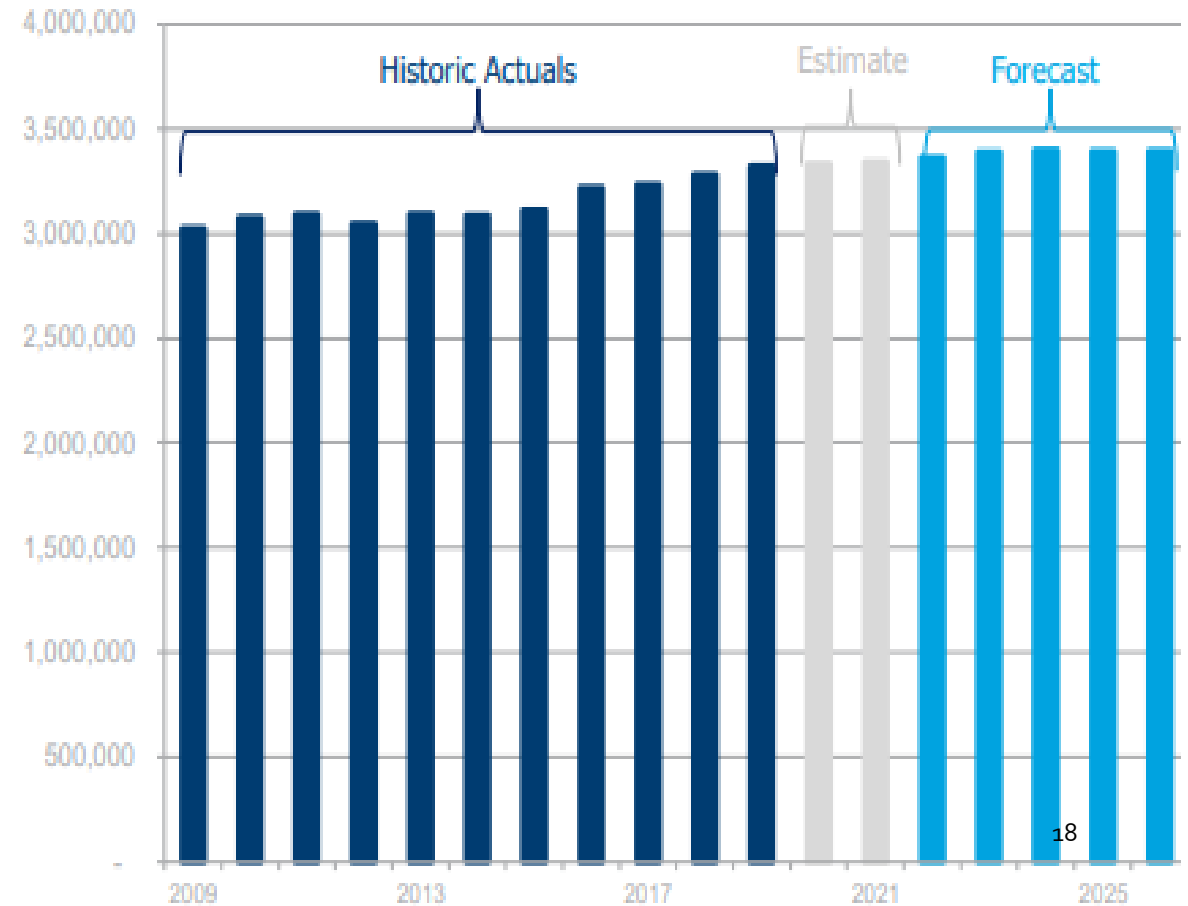
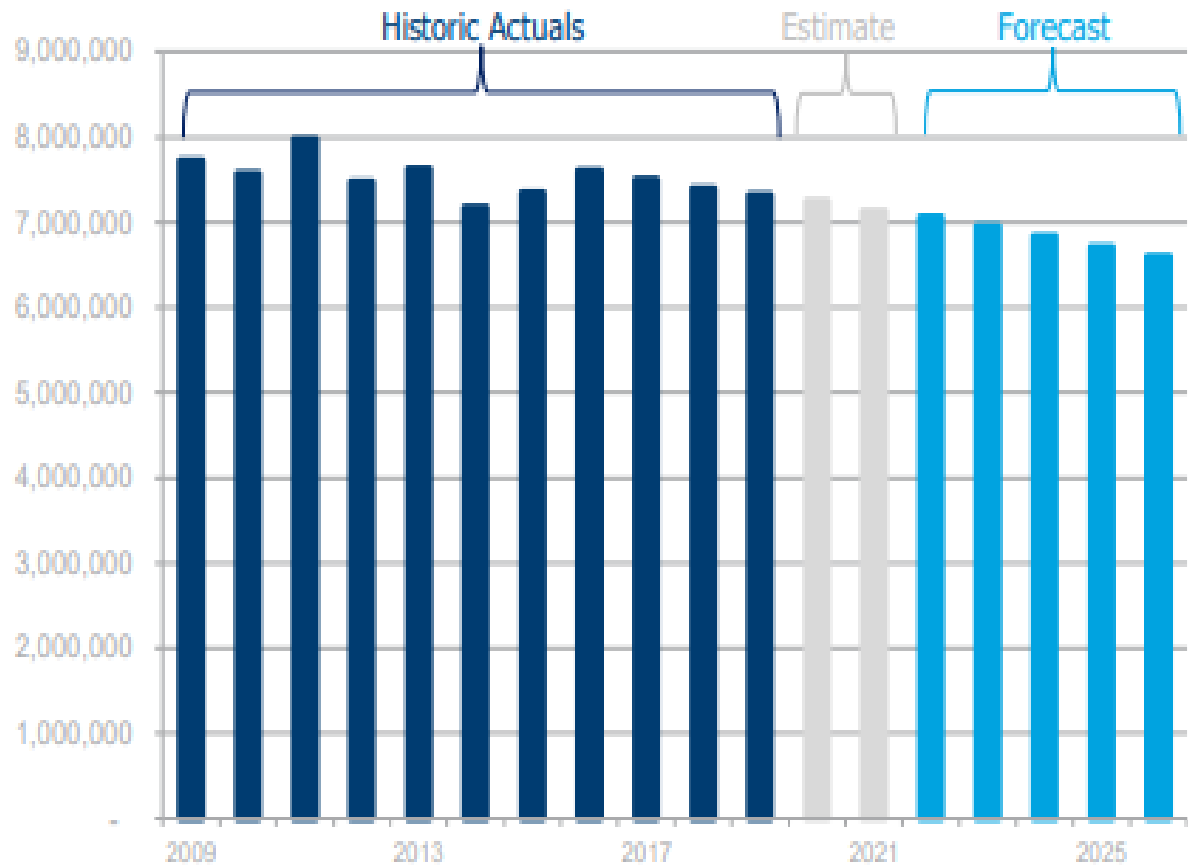
- Support it in principle but await more details on actual cost and extent of AGN contribution as engagement proceeds

Demand:

Residential Falling, Commercial too optimistic?

Total Residential Demand

Total Commercial Demand



Demand forecasts

- Very comprehensive approach taken to forecasting customer numbers and demand
 - Consistent with the methodology accepted by the AER for current period for AGN's SA/Victorian and Albury networks; and with AEMO GSOO forecasts
- As expected the rate of growth of new connections continues to fall as well as average consumption for customers on volume tariffs
 - Out of a sample of 7 distribution networks AGN has the second lowest rate of growth of residential connections and second highest annual decline in residential connection consumption
 - Suggests that the strong support in SA for a move to renewable electricity is being reflected in gas consumption trends
- Note there is no COVID impact in the commercial demand customer forecasts
 - Core "notes the potential for material downside in commercial connections and demand."(p.44)

We look to the AER to make a detailed assessment of forecasts and compliance with the rules

Tariffs

- Support for proposed price path with large price fall in year 1 and then CPI + 1.2% for years 2-5
 - Supporting AGN's credit metrics
 - Good to see representation in terms of nominal changes – clear to consumers
- Support the proposed “New Towns” tariff applying to Mount Barker reflecting higher costs of provision
 - Draft Plan submission raised the option of a differential tariff to reflect some degree of accelerated depreciation for the Mount Barker extension
- The different objectives of declining block tariffs
 - consistent with prices reflecting marginal costs and increasing asset utilisation
 - Inconsistent with a zero net emissions target that will involve reduced gas consumption
 - Potential conflict highlighted in our Draft Plan submission on need for AER review of gas rules

Access Arrangement

- Unique engagement with Retailer Reference Group
- Consultation on reference services and terms & conditions
- Alignment of terms and conditions of access across AGN businesses is supported

Further Considerations: AGN

- The tough questions: we've put them to AGN
- AGN has tied much of its future to hydrogen: what are the key stages and associated viability indicators?
- Ongoing consumer and stakeholder input into "Future gas issues and options."
- What if hydrogen doesn't work?
- Market Expansion (capex)
- Risk sharing between legacy customers, expansion customers and future customers – what is equitable?

Vulnerable Customers Program, further engagement

Is the AGN AA proposal “Capable of Acceptance” –

AGN’s aim was to lodge an Access Arrangement that would be “Capable of Acceptance” by the AER, customers and stakeholders – indicative criteria we will use in our submission:

- Demonstrated consumer support across the diversity of consumer interests, particularly with the ‘hydrogen journey’
- Addresses affordability concerns
- Follows AER guidelines and regulatory models
- Efficient business expenditure
- Demonstrated, responsive leadership engagement
- Further engagement re market expansion capex, Vulnerable Customer Strategy, Innovation Incentive Scheme



QUESTIONS?