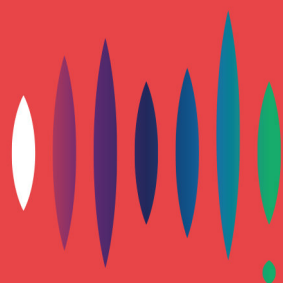


# **Evoenergy and Australian Gas Networks (SA) Gas access arrangement proposals 2021-26**

Submission

August 2020



**ENERGY  
CONSUMERS  
AUSTRALIA**

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## Version history

VERSION	DATE	COMMENTS
1	11 August 2020	Final

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## Overview

Consumers have told us that a better energy future is affordable, simple, easy to manage, clean and inclusive.

Transitioning the gas network for the future requires joined-up thinking and whole-of-sector leadership.

### Introduction

Energy Consumers Australia is the national voice for residential and small business energy consumers. Established by the former Council of Australian Governments Energy Council in 2015, our objective is to promote the long-term interests of consumers with respect to price, quality, reliability, safety and security of supply.

We appreciate the opportunity to provide the Australian Energy Regulator (AER) with a detailed response in this submission to the gas distribution access arrangement proposals for 2021-26 submitted by Evoenergy for the Australian Capital Territory (ACT, including some parts of NSW); and Australian Gas Networks (AGN SA) for South Australia.

We are separately providing our technical expert's advice on the details of the individual access arrangement proposals.

### Summary

In this submission, we focus on the most important issue addressed by both proposals, in relation to the future of gas, including:

- how satisfied consumers are with the current system and their confidence levels about the future;
- what consumers are telling us they want for the future;
- how to put consumers at the centre of a re-imagined energy system; and
- whether the current regulatory framework is designed to contemplate the scenario of complete electrification of energy in a jurisdiction.

In our review of the access arrangement proposals and our one-on-one engagement with Evoenergy and AGN SA, we can see that there is substantial alignment between the distributor proposals and the interest of household and small business gas consumers.

We have also identified several evidence gaps in the proposals which we believe need to be addressed before we can consider the proposals to be capable of acceptance. Both Evoenergy and AGN SA have welcomed discussions and our questions and we will continue to engage with them on the evidence gaps post-submission. These evidence gaps are summarised later in this submission.

## Our approach

Energy Consumers Australia welcomes the commitment by Evoenergy and AGN SA to engage with consumers and advocacy groups, and the efforts made so far to find the right balance between affordability and transitioning to the future energy system.

Evoenergy's Citizen's Jury approach identified the following themes that are important to its consumers:

- Environmental sustainability
- Responsible transition
- Safe and reliable service; and
- Affordability and fairness.<sup>1</sup>

AGN SA's four-staged engagement program resulted in the following customer workshop findings:

- Price and affordability are the most important issues for customers, and customers welcome the proposed price cut
- 96 per cent of customers support AGN SA's draft plan and investment proposals
- AGN SA is trusted for its delivery of safe, reliable gas and customers support investment levels to maintain these standards
- Customers value current customer service levels but expect digital services to be introduced in a cost-effective way
- Environmental sustainability is a high priority for customers and there is a high level of support for investment in renewable gas to replace unaccounted for gas (UAFG)
- Customers support AGN investment in innovation
- Customers support investment in a Vulnerable Customer Assistance Program (VCAP) and consider this responsible business; and
- Customers consider education is important, but initiatives considered by AGN SA must be accessible and funding models need to be further explored.<sup>2</sup>

Common to both groups of consumers is a focus on affordability, environmental sustainability and an underlying theme of moving forward in an ordered and well-planned way.

In seeking the right balance of outcomes, our principles are:

- **Affordability** must be a constraint on investment and decisions about energy – an explicit criterion in decision making up and down the supply chain.

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<sup>1</sup> Evoenergy, *Overview. Access arrangement information ACT and Queanbeyan-Palerang gas network 2021-26*, page 14. Accessed from <https://www.aer.gov.au/system/files/Evoenergy%20-%202021-26%20-%20Overview%20-%20June%202020.pdf>

<sup>2</sup> AGN SA, *Five year plan for our South Australian network July 2021-June 2026*, page 35. Accessed from [https://www.aer.gov.au/system/files/AGN%20-%20AGIG%20-%20Final%20Plan%20-%20201%20July%202020\\_0.pdf](https://www.aer.gov.au/system/files/AGN%20-%20AGIG%20-%20Final%20Plan%20-%20201%20July%202020_0.pdf)

- Energy services must be built around individuals to reflect their own use and costs – whether that is consumers who are innovating and engaged; or the majority of consumers who are focused on affordability and costs; or consumers with vulnerabilities.
- Investment in the power system – networks, generation and retail – must be *optimised* together with consumers' investments on their side of the meter.

In reviewing the revenue proposals and network tariffs proposed by Evoenergy and AGN SA, we start with consumers and the decisions they make that have implications for their gas bills.

Energy Consumers Australia undertakes research into the consumer experience in the energy market today, and consumers' expectations about what a future energy market could deliver to them.

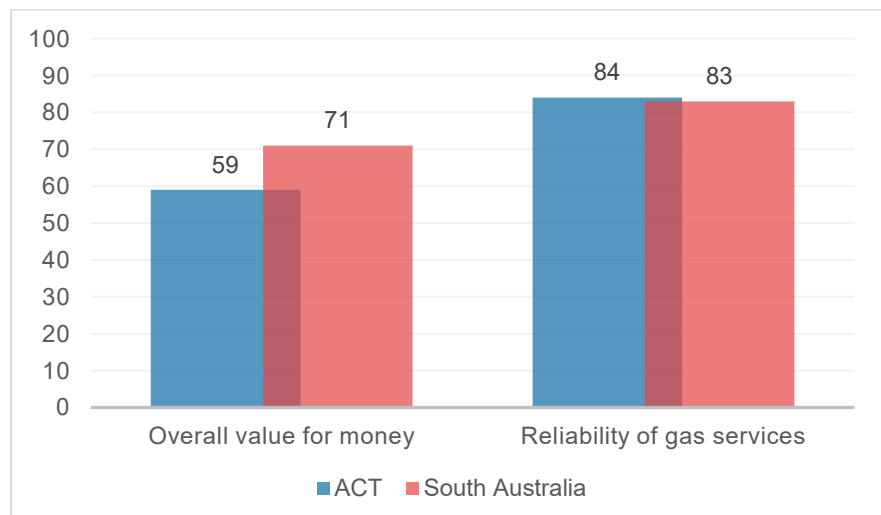
### What consumers are telling us

Our Energy Consumer Sentiment Survey (ECSS) reports trends over time with a range of consumer metrics, expressed as a percentage reporting positive scores of more than seven out of 10.

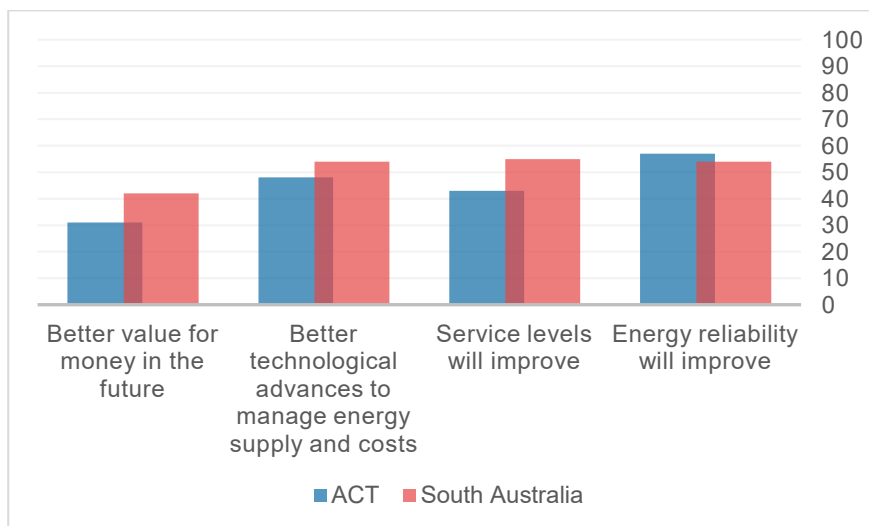
Figure 1 shows us the level of satisfaction with gas from residential consumers in the ACT and South Australia. While consumers are satisfied with the level of reliability, there are opportunities to improve satisfaction scores about the value for money.

Figure 2 looks at consumers' confidence in long-term outcomes. While the figures for the July 2020 survey all show improvement in the confidence levels, almost half of consumers are telling us that they are not confident that the energy market will deliver a better outcome for them in the future. This speaks to a question of trust – whether consumers can trust that businesses are making decisions; and policy is being made with their long-term interests at heart.

**Figure 1: Residential consumer satisfaction with gas**



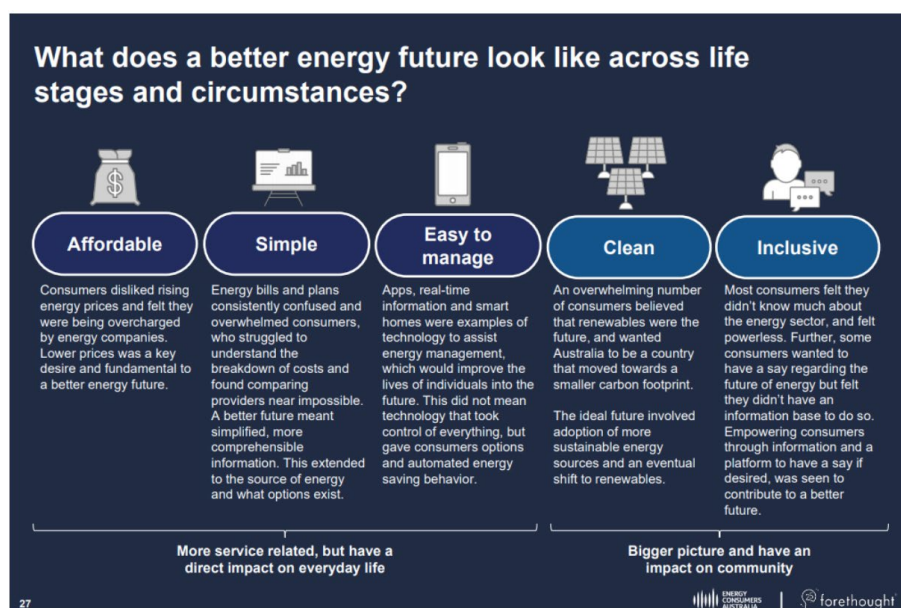
**Figure 2: Residential consumer confidence in long-term outcomes**



Of particular relevance to the discussion about the future of gas, is whether this future will deliver better value for money. We also recently commissioned Australia-wide consumer expectations research that explored the lives and energy needs of household and small business consumers. Specifically, we asked consumers how energy fits into their lives now, what the future of energy should look like and what Australians want from the sector.

Figure 3 shows that as well as a better service, and a ‘clean’ energy future, consumers also wanted a say in the evolution of the energy market but feel that they lack the information and platform to be heard.

**Figure 3: Findings from 2019 consumer expectations research**



## The future of gas

We have observed that the future of gas often reverts into a discussion about whether or not to accelerate depreciation (that is, the rate of recovery of the capital cost) for new and/or existing assets.

The discussions have failed to consider the technological and policy advancements that can happen within a relatively short period to deliver a planned, joined-up transition program that puts the long-term interests of consumers at its heart.

In thinking about the future of gas, we have had regard to:

- What is the problem to be solved?
- Are there different frameworks for thinking about the problem, that allow consideration of the uncertainty and consumers' needs?

### What is the problem to be solved?

While the national policy spotlight is on ensuring the security and safety of the national electricity network, individual jurisdictions are facing significant challenges around the future of gas and the policy framework that should apply to deal with uncertainty.

From a regulated distribution network owner's perspective, this is a problem about ongoing commercial viability. This includes questions around how to ensure businesses continue to have the opportunity of recovering their investment in assets under a scenario that sees the network become redundant; and whether this uncertainty can be mitigated now. We saw in NSW, and we are seeing it with Evoenergy's proposal, that the attempt to mitigate this uncertainty was addressed by shifting the cost to current consumers through the use of accelerated depreciation of new assets in the first instance, with a plan to accelerate depreciation for all assets in subsequent regulatory periods.

From a policy-maker's perspective, this is a problem about delivering on environmental commitments; and creating opportunities for new industry and other value streams for the state.

From a small consumer's perspective, the issue is affordability and how are consumers without alternative options protected from unsustainable increases in costs caused by increased capital recovery and a decreasing customer base from whom to recover these costs?

### Frameworks for thinking about the problem

Looking at the above, we can see that this is a multi-faceted complex problem. The answer will depend on how a number of developments outside the control of the business or consumers unfold and this should also lead to further work to explore more specific questions such as:



- What are the options for the future?
- Are the existing National Gas Law and Rules capable of addressing the problem to be solved? And if not, what needs to change within this regulatory framework to allow for other options to be pursued?
- Who will lead this transition? For example, would it be appropriate for the AER to lead this broader review?

We commend both Evoenergy and AGN SA for tackling this complex problem and bringing consumers into the discussion in their respective consumer engagement activities. Each network has used different frameworks for thinking about the problem, which we discuss below.

### Evoenergy

Evoenergy took a binary approach to thinking about the future of gas by exploring two alternate futures: one with renewable gas and the other without gas - that is, complete electrification of the energy network in the ACT.

The limitations with this binary approach is that it locks consumers into having to support one or the other. It does not provide for broader options analysis.

We welcomed Evoenergy's invitation to observe a weekend of consultation with its Citizens' Jury prior to the release of its Draft Plan. We noted that consumers did briefly mention the option of other ways to recover the cost of investment under the full electrification option, rather than have consumers pay for this entirely.

This is an important consideration when making decisions now about an uncertain future, particularly when the ACT has a total customer base of 152,000<sup>3</sup> most of which are residential and small business customers.

A "back-of-the-envelope" assessment of cost impacts to consumers from dividing Evoenergy's proposed opening capital base of \$326.88 million by the total number of customers would see consumers pay \$2,150 per customer up front for the retirement of the network if consumers were required to pay for the cost.

However, this is not the only cost. This does not take into consideration the augmentation costs required for the electricity network to absorb the displaced gas load; and the costs to consumers for home appliance changes. We note that the ACT has the second highest gas usage per customer when compared to Victoria, NSW, Queensland and South Australia; and the second highest electricity consumption per customer in

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<sup>3</sup> Evoenergy Access Arrangement proposal – Table 7.1 of Attachment 7 – Demand Forecasts. Accessed from <https://www.aer.gov.au/system/files/Evoenergy%20-%20Attachment%207%20-%20Demand%20forecasts%20-%20June%202020.pdf>

the National Electricity Market.<sup>4</sup> Adding in a potential future that sees greater penetration of distributed energy resources in the ACT (and augmentation costs to ensure security of the low voltage network), the cost impacts for consumers of the two options become more complex.

Evoenergy's proposal tells us that:

- While it investigates options for a responsible transition (including activities around the interaction of hydrogen gas in the Evoenergy network), it will focus on minimising its ongoing costs.<sup>5</sup> However, it proposes to accelerate depreciation of some assets. In so doing, it is shifting the costs of avoiding stranded assets (that is, the cost of the uncertainty of asset lives) to today's consumers. We maintain that it may well be too premature to take any action but that even if it is not too early, distribution network businesses are best placed to manage this risk.

It is also important to note that consumers are dealing with other risks external to the energy market right now, especially risks around health, income and employment. While it may be too premature to accurately quantify the impact of COVID-19 over the next five-year period, we know that the ACT has not been spared economic impact. One of Evoenergy's largest customers, the Australian National University, has openly communicated the financial impacts on its business, relying on deferrals of pay rises, voluntary separations and a review of the casual and temporary staff to save money in the short and medium term.<sup>6</sup>

Evoenergy would be more likely than a gas network operator in another jurisdiction to know sooner about changes to environmental policy in the ACT. While operational staff may not have been aware, the ACT Treasurer, being the Minister responsible for the *Territory-owned Corporations Act 1990* and therefore a shareholder of Evoenergy, would likely have been aware of pending policy changes that could have an effect on the ongoing viability of the gas distribution network. Given the risk stems from a change in government policy, rather than a change in how consumers use the network, it is inappropriate for ACT (and NSW) gas consumers to carry this risk.

- Evoenergy is working with the ACT Government, industry, researchers and community to develop a road map to net zero emissions from natural gas; and that the access arrangement proposal provides a stable

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<sup>4</sup> Australian Energy Market Commission, *2020 Retail Energy Competition Review*, Tables 6.2 (page 109) and 4.3 (page 53) respectively. Accessed from [https://www.aemc.gov.au/sites/default/files/documents/2020\\_retail\\_energy\\_competition\\_review\\_-\\_final\\_report.pdf](https://www.aemc.gov.au/sites/default/files/documents/2020_retail_energy_competition_review_-_final_report.pdf)

<sup>5</sup> Evoenergy, *Overview. Access arrangement information ACT and Queanbeyan-Palerang gas network 2021-26*, page 17. Accessed from <https://www.aer.gov.au/system/files/Evoenergy%20-%202021-26%20-%20Overview%20-%20June%202020.pdf>

<sup>6</sup> See "06-24 Message from VC" and "06-24 Financial Health FAQs". Accessed online at <https://www.anu.edu.au/covid-19-advice/campus-community/financial-health>.

platform from which to consider and progress the road map pending the ACT Government's decision on the future of the gas network by 2024.<sup>7</sup>

We support Evoenergy's goal of developing a responsible transition to the future. A responsible, planned transition will build consumer trust and confidence in the future. However, our concern is that the approach proposed by Evoenergy does not appear to consider options outside the current regulatory framework, or that the current regulatory framework cannot be changed to accommodate other options that do not see consumers bearing the entire cost of the network.

The regulatory framework was not designed to consider the retirement of an entire network, at one time, where consumers pay the cost of the retirement in one regulatory period. Rather, the framework may contemplate the stranding of some assets, but it would be unreasonable to assume that this would extend to an entire network.

It is also unclear why Evoenergy would need to take action now, given it does not know what the ACT Government's roadmap for 2024 will look like. The direct consequence of Evoenergy's proposal is that current consumers may be required to pay more than necessary, given we do not know what the ACT Government's roadmap will look like. This appears to be imposing costs and risks onto today's consumers based on a pre-determined outcome about the future of gas in the ACT. Any deferral for this period in making any decision to change is unlikely to result in a significant adverse impact for the service provider or tomorrow's customers. Moreover, it not only ensures that the price of energy for today's customers remains sustainably affordable, it also allows time for technological and policy advancements to occur to provide greater certainty as to the future of gas and the role of networks in the provision of energy services to consumers. We only have to look at the technological and policy advancements over the last 5-10 years with renewable electricity generation that have resulted in the cost of electricity generated from renewable sources becoming extremely competitive and affordable for consumers.

#### AGN SA

AGN SA has taken a two-pronged approach to thinking about the future.

Instead of taking action that increases costs for today's consumers, AGN SA is implementing the first of four stages of the Gas Vision 2050: Hydrogen Innovation, Delivering on the Vision developed by Energy Networks Australia, which included AGN. The purpose of this plan is to demonstrate the viability of hydrogen gas technologies and the blending of this gas into networks by the mid-2020s.

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<sup>7</sup> Evoenergy, *Overview. Access arrangement information ACT and Queanbeyan-Palerang gas network 2021-26*, page 16. Accessed from <https://www.aer.gov.au/system/files/Evoenergy%20-%202021-26%20-%20Overview%20-%20June%202020.pdf>

This approach does not assume to know the future, but instead investigates the commercial viability of potential options before committing today's consumers to too much cost. We commend AGN SA for meeting consumers' needs about not spending a dollar more than necessary, a day earlier than needed.

While AGN SA does not have the same legislated goals for emissions reductions actions as Evoenergy does, the South Australian government is keen to explore the role that renewable hydrogen gas could play in a decarbonised energy future.<sup>8</sup>

For the second prong, AGN SA has used its proposal to call for a risk assessment based on a real options framework approach. We support this approach, though the question remains what scenarios should be used in assessing the alternative course of action.

#### The Oxford Scenario Planning Approach

As part of our Foresighting Forum 2020, we engaged Dr Matt Finch from Mechanical Dolphin to help us identify potential futures for the Australian energy market using the Oxford Scenario Planning Approach (OSPA). These four scenarios and the approach are outlined in our report [Futures of Heat, Light and Power: Scenarios for the Australian Energy Sector in 2050](#).

The OSPA does not try to predict the future or pick a winner. Instead, it provides an alternative framework for thinking about the future during times of uncertainty and enables the development of plausible futures. Box 1 provides a brief explanation of the approach and outcomes of scenario planning activities using the OSPA methodology.

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<sup>8</sup> See information on the Australian Hydrogen Centre and the Hydrogen Action Plan. Respectively accessed respectively from <https://www.premier.sa.gov.au/news/media-releases/news/australian-hydrogen-centre-gets-the-green-light> and <http://www.renewablessa.sa.gov.au/topic/hydrogen#:~:text=The%20Hydrogen%20Action%20plan%20sets,by%20the%20Marshall%20Liberal%20Government.>

### Box 1: Summary of OSPA<sup>9</sup>

“Scenario planning does not try to map the entire contextual environment in one go. Instead it analyses a few (typically three or four) cuts through the future system which focuses on a few highly relevant and dominating issues of concern to the strategic planner. The decision of what constitutes such a key issue at the time of analysis is made on the basis of the institutions of the stakeholders involved. Even though the scenario analysis does not cover all possible movements of the ecological system, generally the analysis will come up with one or more new insights based on mappings that have not been seen before, which may provide indications of new ways forward to create novel strategy on which coping behaviour can be based. And if these are not immediately forthcoming, as is common in this work, scenario planning provides for the possibility to add further iterations on the basis of a different cut through the system. The OSPA in fact provides for the possibility to add more iterations until participants feel that reasonable balance has been achieved between the scenarios and the ecological system issues in need of being addressed.”

What we know is that developing scenarios for an uncertain future requires a different way of thinking about the problem compared to the usual planning approach taken for a revenue reset process. Planning should not simply be an economic exercise based on one view of the future, but rather a way to help identify which options should be subject to that economic analysis.

The lack of this type of scenario planning is an evidence gap for both proposals. Before we lock in options that commit today's and tomorrow's consumers to additional costs, this work needs to be undertaken, and this should happen outside the access arrangement reset process, as it would for other significant, structural reviews such as reviews around the rate of return and incentives.

At the AER's public forum on the Evoenergy proposal in August 2020, we asked whether this type of approach to navigating a business through uncertainty had been considered. While the documentation is not public, we were pleased to hear from Evoenergy that they had used a similar approach to the OSPA. For us to be assured about the robustness of this process, we would appreciate this information being made available for our review. Critical to this type of exercise is what actor or question is made the focus of the exercise. We would like to better understand how consumers were considered in this exercise.

We have started thinking about options for how as a sector we could engage on the future of gas issue and are happy to discuss this with the AER as well as the interaction of this work with the current access arrangement proposal processes.

<sup>9</sup> Excerpt from *Strategic Reframing: the Oxford Scenario Planning Approach*, Ramirez, R and Wilkinson, A, 2018, page xi.

## Analysis of the building blocks

Our analysis is informed by advice from the consulting firm TRAC Partners, who we engaged to provide a technical perspective on the proposals. Table 1 summarises TRAC Partners' technical reports at:

- Attachment A: technical report of Evoenergy's proposal
- Attachment B: technical report of AGN SA's proposal.

**Table 1: Summary of evidence gaps**

BUILDING BLOCK	EVOENERGY	AGN SA
Forecast capital expenditure (capex)	<ul style="list-style-type: none"> <li>• No forecast connection of gas customers in new developments in ACT.</li> <li>• Lower forecast rate of new connection within the existing network.</li> <li>• Level of forecast capex is 28 per cent below allowed capex for 2016-20.</li> <li>• Increased forecast meter replacement capex for end-of-life meters.</li> </ul>	<ul style="list-style-type: none"> <li>• Capex cost allocation methodology should be tested by the AER in light of the Australian Gas Infrastructure Group (AGIG) 2017 merger.</li> <li>• Need for integrity dig-ups if in-line integrity systems are being implemented</li> <li>• 300 per cent increase in "Other capex".</li> </ul>
Actual capex between 2016-21		<ul style="list-style-type: none"> <li>• AER to review the adequacy of the capex cost allocation methodology from the AGIG merger, particularly for IT capex.</li> <li>• AER to closely review the connections capex unit rates.</li> <li>• Benchmark the rate of replacement of meters instead of refurbished ones against replacement rates for other networks with similar meters.</li> </ul>
Future of gas	<ul style="list-style-type: none"> <li>• Actioning Evoenergy's transition roadmap before the ACT Government's is finalised in 2024.</li> <li>• Accelerated depreciation of new, long-lived assets.</li> <li>• Working with stakeholders to understand the needs of vulnerable customers &amp; assistance measures.</li> </ul>	<ul style="list-style-type: none"> <li>• Cost benefit analysis and risk assessment to inform whether it would be more prudent to continue with the mains replacement program or deferring some/all of the program until more is known in 2022 about hydrogen.</li> </ul>

BUILDING BLOCK	EVOENERGY	AGN SA
Operating expenditure (opex)	<ul style="list-style-type: none"> <li>Impact of Jemena's opex savings from its transformation program on Evoenergy's forecast opex and productivity improvements.</li> <li>Is 2019-20 the appropriate base year to adopt in the base-step-trend methodology.</li> <li>Justification for increasing forecast costs for insurance, unaccounted for gas; and derivation of the IT Asset Utilisation Fee.</li> </ul>	<ul style="list-style-type: none"> <li>Forecast opex is around 8 per cent higher than what AGN SA expects to incur in this period.</li> <li>Is it appropriate to source up to 20% of unaccounted for gas from biomethane.</li> </ul>
Assisting Vulnerable Customers	<ul style="list-style-type: none"> <li>Further work is required, particularly in light of COVID-19</li> </ul>	<ul style="list-style-type: none"> <li>Are the four initiatives to assist vulnerable customers reduce the financial barriers to greater gas efficiency; and safe and reliable appliances the most effective initiatives.</li> </ul>
Inflation	<ul style="list-style-type: none"> <li>Encourage the AER to complete its current consultation process in relation to inflation in time for its position to be adopted in the Draft Decision</li> </ul>	
Demand	<ul style="list-style-type: none"> <li>Customer numbers are forecast to grow by three per cent with a total of 157,300 customers forecast by 2025-26.</li> </ul>	Forecast demand associated with the extension to Mt Barker should be based on the information used in the AER's final decision for this extension, but with modifications to take into account any updates that have occurred since that decision
Depreciation	<ul style="list-style-type: none"> <li>Shorten asset lives for some new investment to ensure fair recovery of costs from consumers.</li> </ul>	
Tariff variation	<ul style="list-style-type: none"> <li>Proposing an intra-year tariff variation mechanism.</li> </ul>	
COVID-19 impacts	<ul style="list-style-type: none"> <li>Forecasts have not been adjusted to address impacts of COVID-19. We note this will be done in response to the Draft Decision.</li> </ul>	

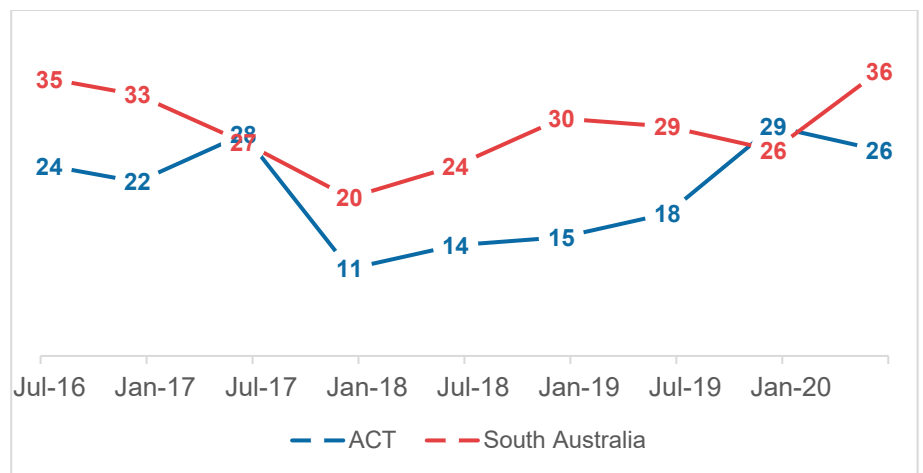
BUILDING BLOCK	EVOENERGY	AGN SA
Incentive mechanisms	<ul style="list-style-type: none"> <li>The introduction of a Capital Expenditure Sharing Scheme (CESS) should match the features of the CESS approved for JGN Plan</li> </ul>	<ul style="list-style-type: none"> <li>The introduction of a Network Innovation Scheme.</li> </ul>
Price path and revenue smoothing		<ul style="list-style-type: none"> <li>We would expect the AER to fully test the claims about financeability of the price path and revenue smoothing being proposed, taking into account AGN SA's actual situation with respect to factors such as tax, other revenue earned and actual financing structures.</li> </ul>



## Conclusion

Since we began the ECSS in 2016, consumers in the ACT and South Australia have continually reported low confidence that the energy market is working in the long-term interests of consumers. Figure 4 shows us the volatility in confidence levels, with positive confidence scores never reaching greater than 36 per cent in South Australia and 29 per cent in the ACT.

**Figure 4: Confidence that the energy market is working in the long-term interests of consumers**



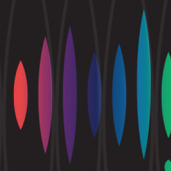
It is unreasonable that consumers should have to incur additional costs from actions like accelerated depreciation when there are proven methodologies for planning during times of uncertainty which could be utilised for the purpose of this round of access arrangement proposals.

This limited consideration of the issues does not appear to be in the long-term interests of consumers. Rather, the implications for consumers in the longer-term could be higher costs, lack of choice of fuel, being forced to change how they “home” and how they “work”. Constraining thinking about how to deal with the uncertain future of gas within the confines of the current regulatory framework is not in the long-term interests of consumers.

To discuss the issues raised in this submission, please contact Shelley Ashe, Associate Director – Networks via email at [shelley.ashe@energyconsumersaustralia.com.au](mailto:shelley.ashe@energyconsumersaustralia.com.au).

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# **ECA RESPONSE TO AGNSA'S 2021-26 ACCESS ARRANGEMENT PROPOSAL**



# EXECUTIVE SUMMARY



# OVERARCHING OBJECTIVES THAT SHOULD FRAME AGNSA'S 2021 PLAN

- We have approached our review of AGN SA's 2021 Plan by focusing on the following objectives, as they are all relevant to the long-term interests of consumers with respect to price, reliability, quality and security of supply:
  - Network tariffs must be **affordable**, a function of **individualised** services and provided within an **optimised** system.
  - Gas prices must be kept as low as possible for today's household and small business consumers.
  - Current and future consumers should be paying no more than they need to for the quality of service they require - "Not one dollar more is spent than necessary; Not one day earlier than needed".
  - There should be sufficient information made available to demonstrate that the proposal promotes the long-term interests of customers.
  - There has been meaningful consumer engagement in developing key aspects of the proposal.
- Achieving these objectives will:
  - help keep network prices as competitive as possible;
  - maximise the incentive for consumers to continue usage of the network for the foreseeable future; and
  - align very closely with the interests of network investors to give them the best chance that they will be able to recover their investment and earn a return on that investment.
- This is in the long term interest of today's and tomorrow's consumers and investors in infrastructure.



# KEY FEATURES OF AGNSA'S PLAN THAT ALIGN WITH ECA OBJECTIVES

There is substantial alignment between AGNSA's Plan and the interests of household and small business energy consumers.

2021 Plan Feature	Relevant ECA Objective
<ul style="list-style-type: none"><li>• An upfront price cut of 6.5% from 1 July 2021 (for the first year), although for following years, there are annual price increases of 2.8%pa for the remainder of the 5 year plan</li></ul>	Long term consumer interest with respect to price
<ul style="list-style-type: none"><li>• Sharing of initial year's tariff reductions across all customer classes</li></ul>	Long term consumer interest with respect to price
<ul style="list-style-type: none"><li>• AGNSA is not proposing any changes to its current approach to depreciation in response to the energy transition, instead preferring to wait for more information to become available on the role of gas in a low carbon future</li></ul>	Long term consumer interest with respect to price
<ul style="list-style-type: none"><li>• Adoption of the AER's Rate of Return guidelines position, corporate tax position and inflation position</li></ul>	Long term consumer interest with respect to price








However, in our view there are outstanding features of the Plan where there are areas for improvement or aspects which we believe requires further investigation by the AER, before the Plan could be considered capable of acceptance by the AER.

The following slides comment on each of the aspects of AGNSA's 2021 Plan:







-  - consistent with key objectives
-  - further work or analysis required before ECA should accept that it is consistent with key objectives and capable of acceptance by AER



# RESPONSE TO AGNSA'S 2021 PLAN FEATURES







Focus Area	AGNSA's Proposal	Our Position
Actual Capital expenditure	<ul style="list-style-type: none"> <li>AER should satisfy itself of the adequacy of the capex cost allocation methodology as a result of AGIG merger, particularly for IT &amp; overheads capex</li> </ul>	 (slides 11 & 12)
	<ul style="list-style-type: none"> <li>Connections capex unit rates need to be scrutinized more closely by AER</li> </ul>	 (slides 9 & 10)
	<ul style="list-style-type: none"> <li>The rate of replacement of meters with new meters instead of refurbished ones should be benchmarked against replacement rates for other networks with similar meters</li> </ul>	 (slides 10 & 11)
Inflation	<ul style="list-style-type: none"> <li>Support the adoption of the AER's position on inflation but we encourage the AER's current consultation process on inflation to be completed in time for the issuing of the Draft Decision</li> </ul>	
Depreciation	<ul style="list-style-type: none"> <li>No change to current approach to depreciation in response to the energy transition, instead AGNSA will wait for more information to become available on the role of gas in a low carbon future</li> </ul>	
Rate of return	<ul style="list-style-type: none"> <li>Accept AER's approach in guidelines</li> </ul>	
Tax (and gamma)	<ul style="list-style-type: none"> <li>Calculated in line with the AER's final tax decision and rate of return instrument</li> </ul>	

# RESPONSE TO AGNSA'S 2021 PLAN FEATURES

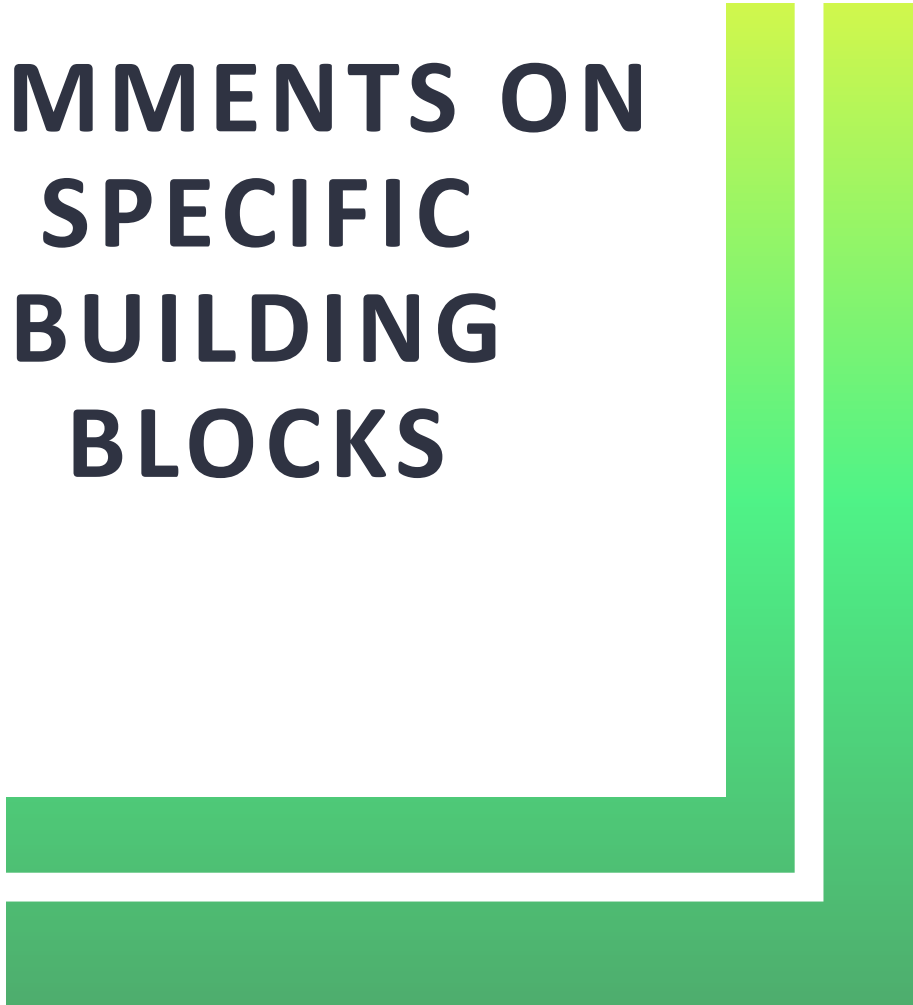
Focus Area	AGNSA's Proposal	Our Position
<b>Forecast Capital expenditure</b>	<ul style="list-style-type: none"> <li>A cost/benefit analysis and risk assessment should be submitted to inform whether it would be more prudent to carry on with the mains replacement program as proposed or deferring some or all of this project until more information is known in 2022 about hydrogen.</li> </ul>	 (slide 12)
	<ul style="list-style-type: none"> <li>Capex cost allocation methodology needs to be retested by the AER in light of the AGIG merger in 2017, particularly with respect to the overheads capex and capex associated with IT projects such as the IT strategy and roadmap</li> </ul>	 (slides 11 & 12)
	<ul style="list-style-type: none"> <li>Further analysis required as to why integrity dig ups are required if in line integrity systems are being implemented</li> </ul>	 (slide 12)
	<ul style="list-style-type: none"> <li>Further analysis required as to why an almost 300% increase in the "Other capex" category of expenditure is being proposed.</li> </ul>	 (slides 12)
<b>Operating expenditure</b>	<ul style="list-style-type: none"> <li>Total forecast opex (\$357m) is around 8% (\$27 million) higher than what AGN expects to incur in the current AA period</li> </ul>	 (slides 13-15)
	<ul style="list-style-type: none"> <li>Offset a portion of unaccounted for gas (UAFG) with biomethane, which is a net carbon neutral gas.</li> </ul>	 (slide 14)



# RESPONSE TO AGNSA'S 2021 PLAN FEATURES

Focus Area	AGNSA's Proposal	Our Position
Operating Expenditure	<ul style="list-style-type: none"> <li>Propose to use 2019-20 opex levels as the base year in the base-step-trend methodology</li> </ul>	
	<ul style="list-style-type: none"> <li>4 key initiatives to assist vulnerable customers reduce the financial barriers that some may face in terms of utilising gas more efficiently and/or ensuring their appliances are operating in a safe and reliable manner</li> </ul>	 (slides 16–17)
Demand	<ul style="list-style-type: none"> <li>Continuation of the demand forecasting methodologies accepted by the AER for AGNSA's 2016 Plan and in the most recent Vic AGN plan</li> </ul>	
COVID Impacts	<ul style="list-style-type: none"> <li>Forecasts haven't been adjusted to address impacts of COVID. This will be done in response to the Draft Decision</li> </ul>	 (slide 26)
Pricing and service levels	<ul style="list-style-type: none"> <li>upfront price cut of 6.5% (after inflation) for the first year of the 2021 Plan but a 1.25% pa (nominal) increase for the remaining years of the Plan</li> </ul>	
Incentive Mechanisms	<ul style="list-style-type: none"> <li>Propose to continue with a CESS and EBSS but also introduce a Network Innovation Scheme</li> </ul>	 (slide 24)

# COMMENTS ON SPECIFIC BUILDING BLOCKS





# ROLL FORWARD OF RAB – ACTUAL CAPEX

- While total actual/estimated capex between 2016-21 is well below the AER approved total (by 8%), there are significant divergences in most line items.



Capex Category	Actual 16-21 Expenditure (\$m)	Variance from AER approved forecast (%)
Connections	143.735	↑50%
Mains Augmentation	11.072	↓34%
Mains Replacement	262.114	↓15%
Telemetry	0.961	↓21%
Meter Replacement	22.231	↑19%
ICT	40.997	↓33%
Capitalised overheads	46.559	↓21%
Other	27.987	↓32%

- We expect the AER's capex expert will revisit the business cases and request more detailed information in support of AGNSA's actual expenditure levels and, in some cases, unit rates. We have raised some issues with some specific capex issues in the next slides.
- These divergences also raise an issue the AER should consider in more detail - how reliable are past capex levels as a guide for assessing the prudence and efficiency of AGNSA's forecast capex in the 2021 Plan? This is particularly important if a CESS is to apply.





# ACTUAL CAPEX ISSUES

Actual Capex Issue		Our Comments
Connections		<p>We would expect more information to be made available to substantiate the key reasons for higher unit rates as outlined in the <u>Capex Supporting information document</u>, in particular:</p> <ul style="list-style-type: none"> <li>- Why are actual contractor rates for new mains capex in areas close to CBD higher, particularly given the amount of work that AGNSA has undertaken on new mains and mains replacement over the last few years? We would have expected that this would not only have given AGNSA detailed information to ensure that its forecast approved by the AER in 2016 was fairly accurate but it would also have delivered AGNSA significant leverage in negotiating rates with contractors for connections.</li> </ul> <p>Also, we would expect the AER to explore how AGNSA's actual unit contractor rates for new mains capex are higher but yet its rates for mains replacement for forecast capex is lower (compared with the unit rates approved by AER in 2016).</p>
Mains augmentation		<p>We would have expected AGNSA to be providing the AER with the details of a risk assessment that demonstrated there were no safety or integrity risks as a result of deciding not to undertake this augmentation work.</p>

# ACTUAL CAPEX ISSUES

Actual Capex Issue		Our Comments
Meter replacement		The AER should look to compare the rates with the replacement rates of other networks that have similar meters to AGNSA.
IT System capex - incurred to nationalise and consolidate major IT applications, leveraging the capability of these systems through AGNSA's application renewal program and building digital capability		<p>While it is noted that actual ICT expenditure levels for 2016-20 are 33% less than the forecast approved by the AER for that period, we would expect the AER to inquire as to what was involved in nationalising the IT applications and the extent to which the costs have been allocated between the various AGIG businesses given that:</p> <ul style="list-style-type: none"> <li>- Its not clear which of the projects incurred (as summarised on p20 of Attach 8.6) relate to nationalising and consolidating;</li> <li>- It is not apparent that this was an assumption when the AER assessed the forecast for the 2016-20 plan; and</li> <li>- The cost allocation methodology that the AER would have relied upon in assessing the forecasts for 2016-20 would not have assumed an allocation across all of the businesses that now make up AGIG (given that AGIG was not established until 2017).</li> </ul>




# FORECAST CAPEX ISSUES

Forecast Capex Issue		Our Comments
\$389m for safety and reliability projects (including mains replacement program for 860km)		Given AGN is of the view that, by 2022, it will have more information available to determine the viability of renewable gas in the network, the AER should consider undertaking a cost/benefit analysis and risk assessment to inform whether it would be more prudent to carry on with the mains replacement program as proposed or perhaps deferring some or all of this project until that information is to hand.
Forecast growth expenditure		There appears to be an inconsistency in the Plan as to the total of forecast growth related expenditure. Section 8.6.6 of the Plan refers to a forecast of \$149m whereas sections 8.5.2 and figure 8.3 refer to a forecast of \$159m.
Forecast IT expenditure - \$13.5m for the AGIG IT Strategy & Roadmap (SA138)		Similar comments apply for the forecast ICT capex as were mentioned in the section of this report relating to actual capex for IT expenditure. In addition, we would expect the AER to inquire as to the basis for the cost allocation methodology adopted to derive the percentages of the total capex for this project to be allocated to firstly the AGN overall business and then to AGNSA (see Figure 1.1 and Appendix C of Attachment 8.8 for project SA138).
Other forecast capex of \$62m		We would expect the AER to make further inquiries as to why integrity dig ups are required to the same extent as in the 2016 Plan if in line integrity systems are being implemented during the 2021 Plan.

# OPERATING EXPENDITURE (OPEX) ISSUES




- AGNSA's opex levels generally appear to be around average compared with other Australian & NZ gas network operators, based on a number of benchmarking indicators presented in the Economic Insights report:
  - While AGNSA has higher opex per customer, when compared to the five largest networks, this can be fully explained by its smaller scale, lower customer density and differences in the other identified cost drivers
  - AGNSA's normalised real opex per customer is below the sample average and at a similar level to the normalised average of the five largest Australian GDBs.
- However, AGNSA is proposing a total forecast opex of \$357m which is ~8% (\$27 million) higher than what AGN expects to incur in the current AA period.
- While the proposed methodology for setting the forecast opex for the Plan is largely consistent with the AER's methodology adopted in current plan, we have some comments on the following slides.

# OPERATING EXPENDITURE ISSUES

Step		Our Comments
Establish an efficient base year		<ul style="list-style-type: none"> <li>We support the use of 2019/20 opex as the base year given that it's the year with the lowest level of opex in the current 5 year plan.</li> </ul>
No movement of capitalised overheads to opex during the 2021 Plan		<ul style="list-style-type: none"> <li>We support the change in approach on this issue from the Draft Plan to the 2021 Plan given that forecast opex levels are already proposed to be 8% higher than current levels. This focuses on the need to keep prices as low as practicable for consumers.</li> </ul>
Unaccounted for Gas (UAFG)		<p>We would expect the AER to require further information on:</p> <ul style="list-style-type: none"> <li>- Why the expert report concludes that the Market Price for UAFG, for an organisation like AGNSA (which has size (as part of AGIG) and both distribution and transmission pipeline experience), should be assumed to be purchased entirely from a retailer (rather than purchased directly from a producer), and therefore should include a retail margin (which adds between 9.7% -11.7% to the cost of UAFG)</li> <li>- what competitive tension exists in terms of suppliers of renewable or carbon neutral gas (relative to suppliers of fossil fuel gas)</li> <li>- Whether AGNSA would be required to purchase renewable gas under a long term contract that extends beyond the 5 years of the 2021 Plan.</li> </ul>



# OPERATING EXPENDITURE ISSUES (CONT'D)

Step		Our Comments
Trending base year forward		<ul style="list-style-type: none"> <li>• Rate of change approach is consistent with regulatory precedent.</li> <li>• The annual input cost escalator of 0.5% would seem reasonable, although in light of COVID-19, wages increase assumption may need to be tested further towards the end of CY2020.</li> <li>• While we support the adoption of a productivity growth factor at the upper end of the range provided by the expert (ie 0.4% pa), given the 8% increase in opex being proposed for the first year of the 2021 Plan, the AER should satisfy itself that the factor should not align with the factor used by the AER for electricity businesses (ie 0.5%) including, by identifying differences in the technology and complexity of electricity and gas that may warrant a different factor being adopted by AGNSA.</li> </ul>
Forecast of step change items = \$8.1m during the 2021 Plan		<p>While it appears that the case has been made for step changes in insurance premiums and the proposed digital customer experience project, the AER should:</p> <ul style="list-style-type: none"> <li>- make further enquiries in relation to the proposal to include expenditure for the VCAP initiatives (see slides 16-17); and</li> <li>- give consideration to including changes in insurance premiums as part of the tariff variation mechanism (rather than just an insurance cap or credit risk event) so long as the base year is efficient.</li> </ul>
Cost allocation methodology		<ul style="list-style-type: none"> <li>• We would expect the AER to make further enquiries to be satisfied that the cost allocation methodology appropriately allocates costs as a result of establishing AGIG in 2017 and to ensure that the full benefits of this new business have been passed on to AGNSA customers.</li> </ul>

# VULNERABLE CUSTOMER ASSISTANCE PROGRAM

- AGNSA proposes to adopt four initiatives to assist vulnerable customers reduce the financial barriers they face in utilising gas more efficiently and/or ensuring their appliances are operating in a safe and reliable manner (total cost ~\$4m):
  - establish a dedicated vulnerable customer service role within AGNSA
  - implement an upgraded Customer Relationship Management (CRM) system that will include a priority services register
  - provide funding for safety checks and emergency repairs
  - provide rebates to help access more efficient appliances.
- While we recognise that these were developed following co-design workshops, we would encourage the AER to require a cost/benefit analysis be undertaken to determine whether it's more efficient to require retailers to expand on their existing programs rather than a network operator (such as AGNSA). The analysis should consider such issues as:
  - Who the customer interfaces with the most on vulnerability issues?
  - Are the current initiatives that AGNSA undertakes adequate?
  - Is there a double up between initiatives being undertaken by other organisations (such as retailers and charities) and those proposed by AGNSA?

# VULNERABLE CUSTOMER ASSISTANCE PROGRAM (CONT'D)

- We would encourage the AER to consider whether all of the initiatives being proposed are the most appropriately targeted measures to assist vulnerable customers because:
  - How do the initiatives align with those that retailers already have in place?
  - Is the additional role overlapping to what might be achieved through the proposed upgraded CRM?
  - Could an existing CRM system already capture the information required for a priority services register?
- We would also encourage the AER to identify whether other initiatives, which might be more suited to vulnerable customers and which would appear to better align with the Energy Charter, have been considered such as:
  - Products and services that are tailored to vulnerable customers.
  - Training programs for frontline staff.
  - Further dispensation for disconnections if affordability issues arise.

# DEPRECIATION & ASSET LIVES

- AGNSA is not proposing any changes to its current approach to depreciation in response to the energy transition, instead preferring to wait for more information to become available on the role of gas in a low carbon future.
- While this approach is consistent with that followed by the AER for AGIG's other networks, and it is the approach we support (as it best aligns with the ECA's key objectives), it is not consistent with what is being proposed by Evoenergy in its 2021 plan – accelerated depreciation is being proposed.
- We have made submissions in response to the Evoenergy plan to not support Evoenergy's proposal. However, if the AER is inclined to support Evoenergy and apply that approach in respect of the AGNSA 2021 Plan, we would not support that for the reasons outlined in the following slides.
- There is no demonstrable increase in the risk of asset stranding compared to 2016 when this would have last been considered by the AER. In fact, new connections continue to increase during the 2021 Plan.

# DEPRECIATION & ASSET LIVES (CONT'D)

- A more detailed cost/benefit analysis would need to be undertaken to assess the impact on today's and tomorrow's customers of the following scenarios:
  - Accelerating depreciation of existing and new long lived assets from 2021 onwards.
  - Accelerating depreciation of long lived assets from 2026 onwards.
  - Accelerating depreciation of new assets from 2021 onwards and for existing assets from 2026 onwards.
- Even if there is an increased risk of asset stranding, now does not appear to be the time to act to address it because:
  - The SA Government has not outlined any timeline for its roadmap to transition to its net zero 2050 aspiration. This should be known before taking pre-emptive action.
  - Because gas is a fuel of choice in SA, ensuring gas is as affordable as possible today maximises the incentives for continued asset utilisation . This maximises the likelihood of continued use of the network and minimises the risk that the asset may become stranded in the future.
- Furthermore, keeping prices as low as possible during the 2021 Plan period and waiting to re-assess the position on asset lives until the next re-set of 2026 will have other benefits:
  - It will give time to provide further clarity around alternatives to natural gas for the use of the network – if hydrogen can be commercialised and has a role to play in the network, any risk of asset stranding diminishes significantly and so there should be no need to make a change to asset lives at that point in time;
  - Any additional cost to “tomorrow's” consumers (ie those in the next 2026 Plan) will not be significant.

# DEPRECIATION & ASSET LIVES (CONT'D)

- While there is a forecast reduction in average usage and a decline in new industrial connections, AGNSA is forecasting increasing numbers of new residential (1% pa) and commercial (0.6% pa) customers by 2026. This was a critical issue relied on by the AER in the JGN 2020 reset for why shortening of asset lives was not allowed in that case.
- We would expect a cost benefit analysis to be undertaken to show the price impacts of deferring a decision on accelerated depreciation on new assets versus taking the action in this AA plan. Also, increasing prices for today's customers has a bigger impact now with the impact of COVID-19 on vulnerable customers.
- There are other options which the AER should consider such as:
  - Subsidies by government to the business to fully or partly address the impact; or
  - Creating a notional account so that the amount that would otherwise be included in the total revenue (by accelerating depreciation) is placed in it and so that it accrues interest over time. Should a viable renewable gas option be developed, the amount in the account gets added to the total revenue in subsequent years until the account is depleted.

# OTHER BUILDING BLOCK ISSUES

- Forecast demand:
  - We support the continuation of the demand forecasting methodologies accepted by the AER for AGNSA's 2016 Plan and also the most recent Victorian reviews.
  - We would assume that the forecast demand associated with the extension to Mt Barker is based on the information used in the AER's final for this extension, with modifications to take into account any updates that have occurred since that decision.
- Forecast inflation – we encourage the AER to complete its current consultation process in relation to inflation in time for its position to be adopted in the Draft Decision.
- Price Path – while we support the upfront reduction of 6.5% (nominal).

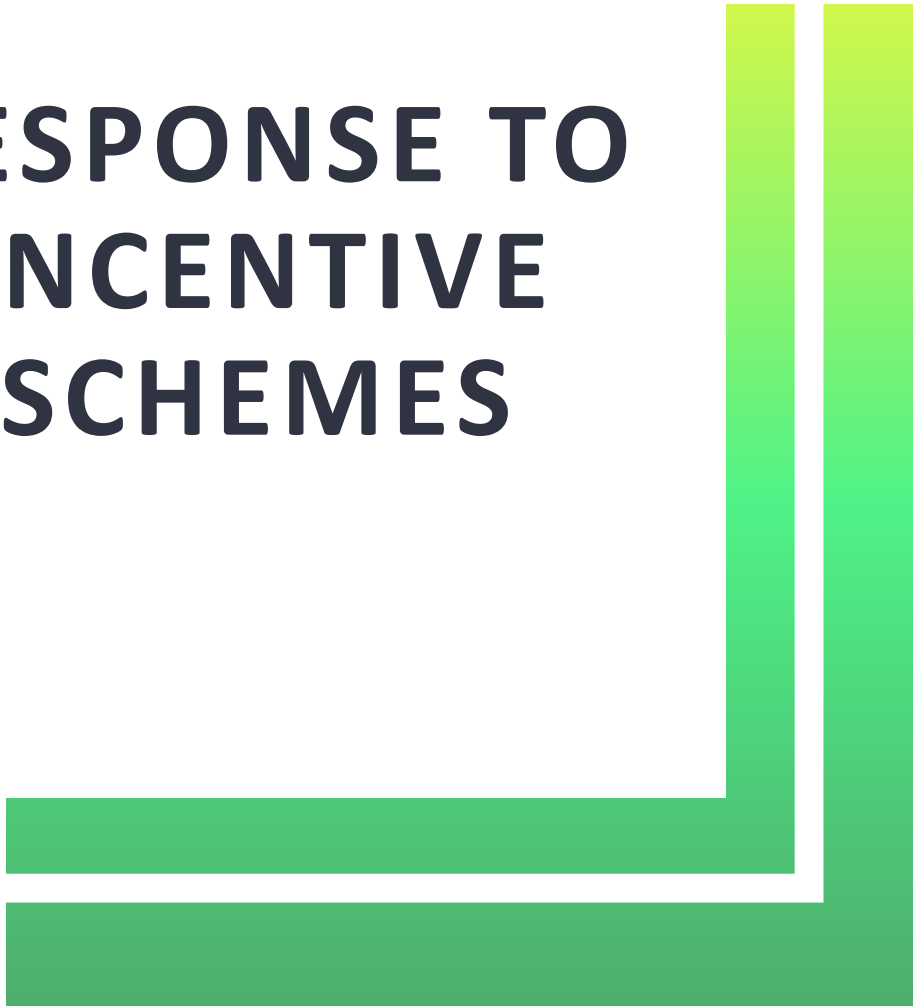


# OTHER BUILDING BLOCK ISSUES (CONT'D)

- Financeability of pricing decision
  - AGNSA claims that its proposal will deliver an average FFO to debt outcome of 9% that will just be sufficient to maintain a weighted average credit rating of between A- and BBB+.
  - We would expect the AER to test this and to focus on a number of factors, including:
    - The extent to which other revenue earned by AGNSA is factored into this assessment (in addition to reference service revenue) – eg revenue from the application of any incentive mechanisms.
    - The tax treatment to be adopted in this analysis – noting that “FFO” is revenue less opex and tax.
    - How AGN’s actual financing arrangements are structured.



# RESPONSE TO INCENTIVE SCHEMES



# INCENTIVE MECHANISMS

- AGNSA is proposing to continue the EBSS for opex that exists in the 2016 Plan. We note that the AER proposed modifications to the standard EBSS in the JGN 2020 Plan. It is not clear if these modifications are to be applied to the 2021 Plan for AGNSA.
  - If they are being incorporated in the 2021 Plan, we would support these modifications.
  - If they are not being incorporated, the AER should inquire why not.
- The proposed Capital Expenditure Sharing Scheme (CESS) is intended to mirror the Contingent CESS that was approved by the AER for the Vic AGN Plan (including the API measures, targets and weightings). This is different to the CESS that was approved by the AER in the JGN 2020 Plan. We note that the JGN decision was only just before the AGNSA plan was submitted and we would therefore encourage ongoing engagement to align with the CESS in JGN.
- There is a proposal to introduce a network innovation scheme/allowance that would allow between \$2.5m - \$5m in costs over the 2021 Plan. But the details have yet to be outlined. Before ECA could support such a scheme, it would need to be satisfied that other mechanisms outside of the NGL (eg ARENA funding) aren't sufficient to incentivise the adoption of the type of innovation projects being considered.

# **OTHER ISSUES RAISED BY AGNSA'S 2021 PLAN**



# COVID 19 IMPACTS

- AGNSA has indicated that many of their inputs into their operx forecasting methodology (such as HIA forecast of housing starts and BIS Oxford's forecast of real labour cost escalation) already take into account the impact of COVID-19. However, we think that there is a real risk that COVID is still evolving and therefore the forecasts may require updating at the time of the draft decision if there is a better understanding of the impact of COVID-19 on these forecasts at the time.
- This raises a potential procedural fairness issue for consumers, particularly if the COVID related adjustments are substantive in nature.
- It means that while consumers will be able to make submissions on the revised proposals that the businesses submit, they will not have an opportunity to make submissions on the AER's thinking on the COVID related adjustments because this will only be outlined in the Final Decision. But the process under the NGR does not prescribe for consultation in response to the AER's final decision.
- AER should give consideration to how procedural fairness is afforded to consumers – options include:
  - Option 1 - the AER could require any COVID related adjustments to be submitted by the businesses prior to the Draft Decision and open up a round of mini consultation on these adjustments before the draft decision is issued. Then the AER's draft decision can take into account both the COVID related adjustments and any submissions consumers make in response.
  - Option 2 – the AER could maintain the status quo until after submissions have been received in response to the revised proposal submitted in response to the Draft Decision. The AER could then issue a preliminary position paper on the COVID related adjustments and request submissions from consumers on its position. Following consideration of these submissions, the AER would then make its final decision.