evoenergy

Evoenergy gas network 2021 plan **Summary for consumers**

Evoenergy gas network 2021–26 access arrangement proposal

June 2020

Summary of our GN21 draft plan

- Evoenergy owns and operates the gas distribution network in the ACT and in the Queanbeyan-Palerang local government area of NSW
- Our network charges account for about one quarter of your total retail gas bill
- Our plan for the gas network for the 2021-26 period (GN21 plan) has been submitted to the Australian Energy Regulator

Our GN21 plan has been shaped by:

Climate change policy

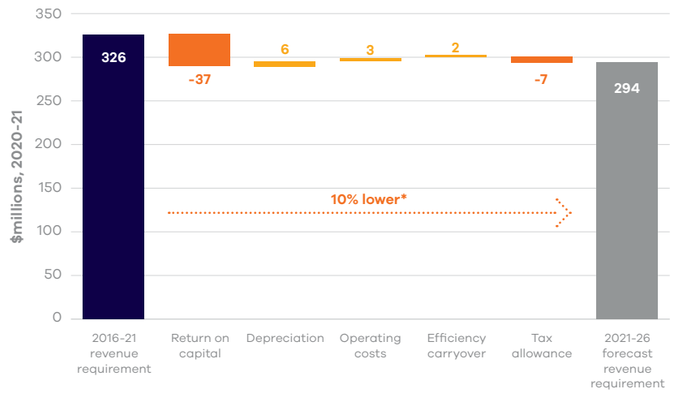
- The ACT Government has committed to achieving net zero greenhouse gas emissions by 2045 in the ACT
- Climate action is a focus of our planning and we are making sure we determine the right course of action that includes thorough community consultation and detailed assessment of alternative options
- While we work towards a roadmap for the future of the gas network, we propose to limit expenditure during the 2021–26 period

Consumer feedback

Consumers told us that they:

- Support environmental sustainability
- Want us to plan for the transition to a net zero energy supply future in a responsible way by:
  - involving consumers in the assessment of costs and impacts of future energy options before decisions are made
  - minimising capital expenditure while we plan the transition
  - taking the expected response to climate change policy on board when making assumptions about market expansion and gas usage expectations
  - keeping consumers informed at all stages of research, planning and transition
  - considering transition impacts on vulnerable consumers
- Are concerned about the affordability of gas and want tariffs that are fair, especially for vulnerable customers
- Value a safe and reliable gas supply, and expect us to continue to prioritise reliability and safety, and to maintain infrastructure while we consider the future of the gas network

Our plan delivers lower network costs for the business and customers



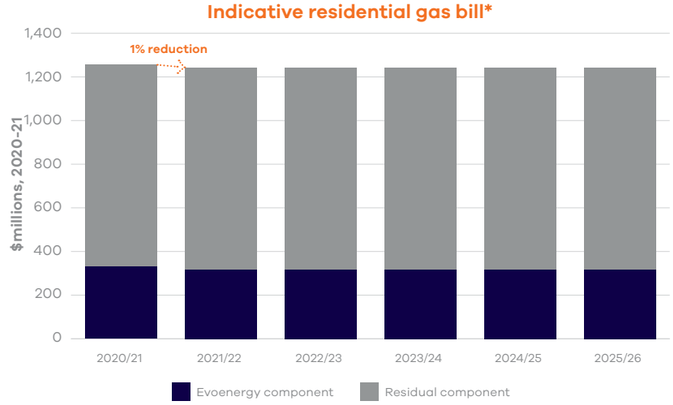
Average annual revenue per customer

*Based on unsmoothed revenue requirement

We expect network prices to reduce by about 4% in 2021/22, followed by stable prices for the remaining 4 years. Holding other components constant, this results in about a 1% reduction in a typical residential bill, excluding the impacts of inflation.

Network prices won't decrease at the same rate as our costs because we expect average gas usage per customer to decline.

Indicative residential gas bill*



*Including other components constant

For customers our plan delivers:

- Safe and reliable gas supply while costs are minimised
- Reduced expenditure, resulting in lower network charges
- A declining value of our assets, which is good news for future bills
- Time to progress our transition roadmap for achieving net zero emissions by 2045
- Responsible market expansion and gas usage assumptions while we plan the transition
- Simplified tariffs
- Capital and operating expenditure sharing schemes to further promote efficiency

About our GN21 plan

Like most energy distribution network businesses in Australia, the prices we charge are regulated by the Australian Energy Regulator (AER)

This plan sets out our proposed services and network investments, the revenue we propose and resulting prices we would charge to deliver this plan. We submitted this proposal, called our GN21 plan, to the AER at the end of June 2020. The AER evaluates the proposal to ensure the prices we charge are reflective of our costs and that we are managing our business efficiently.

This summary provides consumers with an overview of our GN21 plan. You can find out more information about our plan on Evoenergy's GN21 web page and the AER's GN21 web page. Throughout this summary we have provided references to the relevant sections of the plan where you will find further details.

More information on the regulatory framework can be found in section 1 of the *Overview* of our GN21 plan

Citizens' Jury members tour Evoenergy's gas facilities

About Evoenergy

Evoenergy owns and operates the gas distribution network in the ACT and in the Queanbeyan-Palerang local government area of NSW.

Natural gas is extracted and processed by producers in remote gas fields, and transported through high pressure transmission pipelines to local distribution network 'city gate' facilities. There, the gas pressure is lowered from transmission pressure and the gas is injected into Evoenergy's distribution network. We then transport the gas through our network to our customers' homes and businesses, where gas usage is measured through gas meters.

Energy retailers operating in the ACT and surrounding areas purchase our distribution services and combine them with the other components in the supply chain, such as the purchase of wholesale gas, to deliver a final gas service to consumers.

Evoenergy's services make up around one quarter of the total retail gas bill for an average household or small business. Evoenergy's role in the gas supply chain and the contribution of each part of the supply chain to a typical household gas bill is shown in Figure 1.

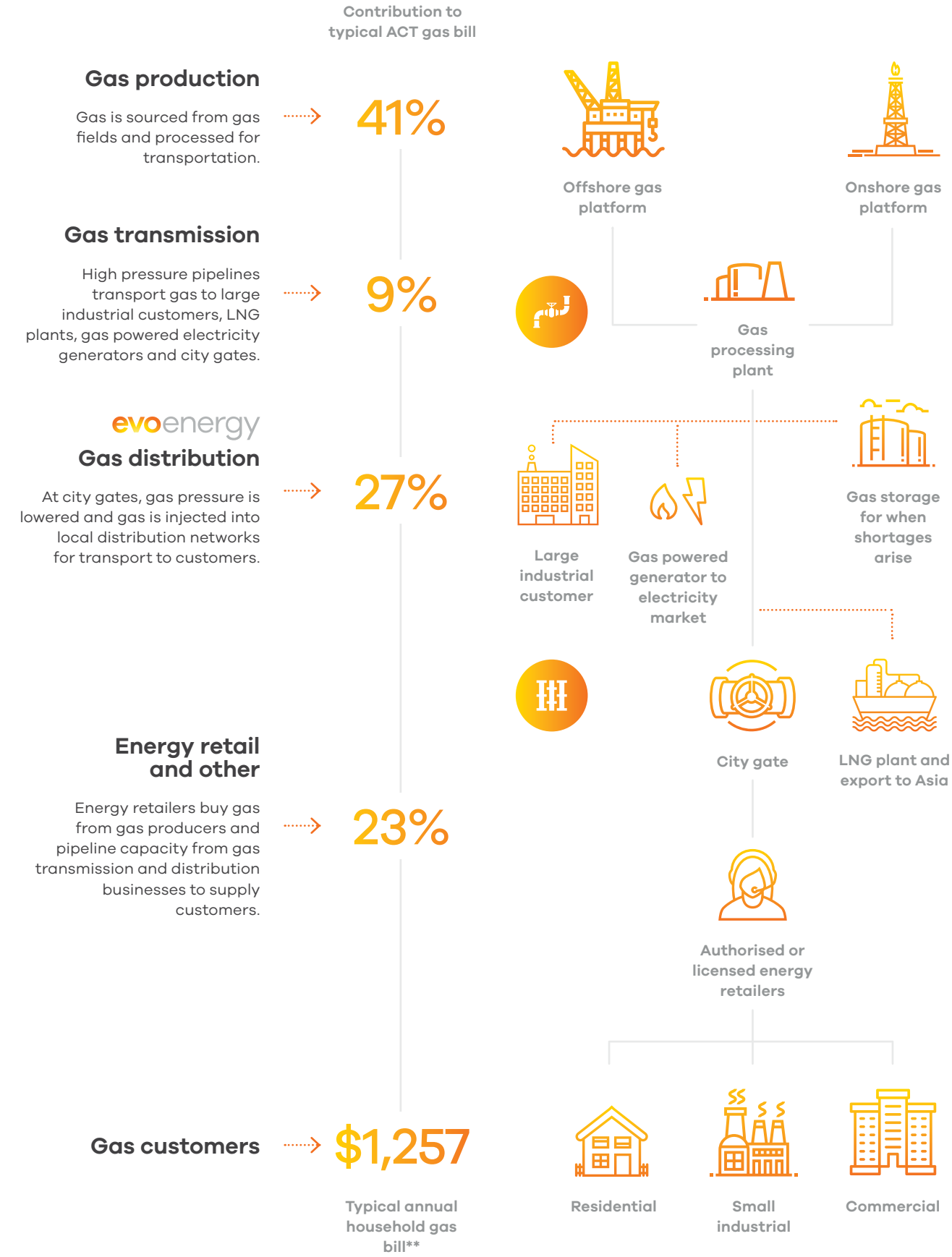
In addition to distributing gas through our network, we also connect new customers to the network, respond to emergencies, read meters and receive and resolve customer enquiries about network issues.

More information about Evoenergy can be found in section 1 of the *Overview* of our GN21 plan

Energy Consumer Reference Council members discuss the GN21 plan

Figure 1: Gas supply chain and contribution to total gas bill

Gas supply chain



* Other costs include costs associated with storage and the costs of participating in AEMO-operated Wholesale markets

** Sources: ACCC 2018, Gas Inquiry 2017-2025 interim report - December, p118, ActewAGL standing home natural gas plan and Evoenergy 2010-20 approved gas pricing.

What our GN21 plan means for customers

During the consultation period on our draft plan, we learnt more about what consumers want and need from the gas network over the next five years, while we prepare to transition the network to meet the ACT Government's target to achieve net zero emissions by 2045.

We heard that consumers care about environmental sustainability and want those with a stake in the region's future energy transition – Evoenergy, governments, and consumers – to put the necessary time and resources into arriving at the best solution for achieving net zero emissions from gas by 2045, while minimising transition impacts, especially for the vulnerable members of the community. This plan allows us to maintain the safety and reliability of gas supply that consumers told us they value over the next five year plan period while we explore ways to achieve this.

We also heard consumers' concerns around affordability and fairness, especially for vulnerable members of the community.

We are acutely aware of the pressure energy prices put on household and business budgets for many of our customers.

Bill impacts

In response to these concerns, our plan minimises expenditure where possible to deliver reduced network prices over the next five years while we continue to develop a roadmap to achieving net zero emissions by 2045.

We have proposed to pass on the network price reduction in the first year, so our customers see an immediate benefit.

To provide an indication of how our proposed network charges are likely to impact the average retail bill, we have adjusted the distribution component (Evoenergy's share) of the bill and held all other components constant, without adjusting for inflation. In reality, other elements of the retail bill outside Evoenergy's control, such as the cost of gas, are also likely to vary over the 2021–26 period and impact the final retail bill.

Table 1 shows the indicative bill impacts for the 2021–26 access arrangement period for an average household consuming about 28 GJ a year. Table 2 shows this for an average small business consuming about 470GJ a year.

Table 1: Indicative typical residential gas bill

	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Residential annual gas bill	1,224	1,210	1,210	1,210	1,210	1,210
Evoenergy component	337	323	323	323	323	323
Residual component	887	887	887	887	887	887
Annual change $		-14	0	0	0	0
Annual change %		-1.1%	0.0%	0.0%	0.0%	0.0%

Based on 28 GJ per year, excluding the impacts of inflation

Table 2: Indicative typical small business gas bill

	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Small business annual gas bill	13,527	13,402	13,402	13,402	13,402	13,402
Evoenergy component	3,043	2,918	2,918	2,918	2,918	2,918
Residual component	10,485	10,485	10,485	10,485	10,485	10,485
Annual change $		-125	0	0	0	0
Annual change %		-0.9%	0.0%	0.0%	0.0%	0.0%

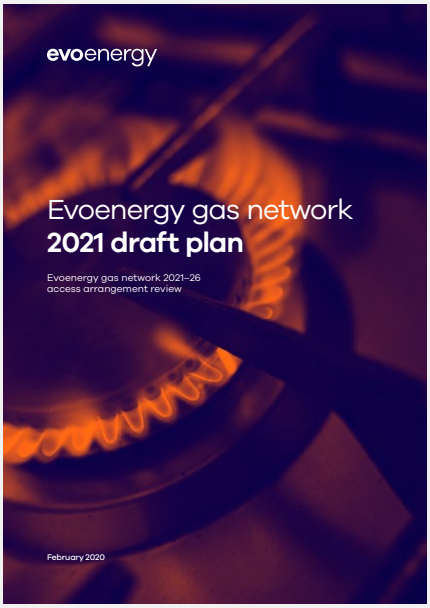
Based on 469.8GJ per year excluding the impacts of inflation. May not sum due to rounding.

How the plan compares to our GN21 draft plan

Since we published our GN21 draft plan in February 2020, we have continued to refine our plan, with a focus on updating forecasts as more up to date information comes to hand, and addressing the feedback we received from consumers.

Our forecast of the revenue we need to recover over the 2021–26 period has gone down from $300 million to $294 million (in constant 2020/21 dollars). This has been driven mainly by a lower expected rate of return due to financial market conditions. The decrease is partially offset by slightly higher operating costs due mostly to updated forecast assumptions for government charges.

We have also refined our customer number and demand forecasts, and, with input from consumers on what they value most, determined the performance measures to include in the proposed capital expenditure sharing scheme (CESS).



COVID-19 impacts

The final four months of refining and finalising our GN21 plan have been a difficult period as we navigate the unprecedented and unpredictable impacts of the COVID-19 health and economic crisis.

Most of the inputs and assumptions that have informed our forecasts for the plan were developed before the crisis escalated. It is difficult to predict what its impact will be over the 2021–26 period, so our GN21 plan does not generally take account of the impacts of the crisis.

We will continue to assess the impacts as more information comes to hand and incorporate any adjustments into our revised proposal at the end of 2020.

How our GN21 plan has been shaped

Early in the process of developing our GN21 plan, we realised that we could not simply take a 'business as usual' approach for the 2021–26 period. The need for action on reducing greenhouse gas emissions means that we need to give due consideration to what the future of Evoenergy's gas network will look like as we work with the government and community to achieve the net zero emissions by 2045 target. As we do not yet know what the future holds for the gas network, we prepared a plan that allows us to continue to provide safe and reliable gas services to our customers, while minimising our expenditure over the period as we take the time to consider and develop a pathway for the future.

It is important that our GN21 plan reflects the views and expectations of our community. In preparing our GN21 plan, we engaged with a range of consumers and community representatives to understand consumers' expectations and ensure we are responding to the challenges and opportunities they identify.

Net zero emissions future

In September 2019, the ACT Government released its *Climate Change Strategy 2019–2025*. The strategy outlines the work currently underway and plans to investigate opportunities for embedding climate emergency considerations across government operations and decisions, as the ACT works towards achieving the net zero by 2045 target.

The strategy commits the government to specific actions to reduce emissions from gas. Achieving net zero emissions from gas, either by transitioning to electricity or by using the gas network for renewable gas, will require a multifaceted approach that factors in major strategic, technical, social and operational considerations. These issues must be considered carefully and include thorough community consultation.

Throughout our engagement program we heard that consumers expect the costs and benefits of alternative options to be quantified. They also want clear information about the transition options, and to be involved in discussion about how the associated costs will be funded.

As Evoenergy continues to work with the ACT Government and the community to achieve zero net emissions by 2045, we must also continue to provide safe, secure, reliable and affordable energy services.

More information about the ACT Government's Climate Change Strategy 2019-2025, actions to reduce gas usage, and what this means for Evonenergy can be found in section 2 of the *Overview* of our GN21 plan

What we heard from our consumers

More information about how we engaged with consumers to develop this plan and what we heard can be found in *Attachment 1 – Consumer engagement* of our GN21 plan

To understand what the community's expectations and views are about Evoenergy's gas network for the 2021–26 period and beyond, we undertook a comprehensive engagement program with activities designed to suit a range of levels of interest, knowledge and availability. The centrepiece of our engagement program was our Citizens' Jury. We also consulted regularly with our Energy Consumer Reference Council (ECRC), ran a workshop in partnership with the ACT Council of Social Service (ACTCOSS) on issues for vulnerable customers, conducted an online survey, embarked on a community 'roadshow' with our GN21 draft plan, ran two deep dive sessions, and engaged with business consumers at both Evoenergy-run events and a business expo.

Table 3 below provides a high-level summary of the key themes we heard through our engagement and how we are responding to these.

Table 3: How we are responding to what we heard from consumers

Theme	What we heard	How our GN21 plan responds to what we heard
Environmental sustainability 	Supporting environmental sustainability is a key driver for many consumers. This was highlighted as a key driver for Evoenergy to consider as they plan for the future.	The development of the forecasts has been strongly influenced by the climate change policy environment in the ACT and the feedback we heard around the importance of environmental sustainability. Our demand forecast assumes declining average usage per customer, more abolishments (permanent disconnections), and no new connections in new ACT suburbs while we develop our transition pathway for achieving net zero emissions by 2045.
Responsible transition 	**Network expansion** Most consumers expect Evoenergy to limit expansion and some expect us to cease expansion altogether. **Research into future energy options, costs and impacts** Consumers want to gain a better understanding of the costs associated with various future energy options and how to transition to them. Consumers want us to undertake research and invest in understanding future energy options.	Our GN21 plan aims to achieve a responsible transition by making conservative assumptions about the extent of market expansion, minimising our capital expenditure (capex), and proposing to accelerate deprecation of new long-lived assets. Our GN21 plan seeks to provide more information on what our obligations are to customers who want to continue to use gas or connect to gas, and what some of the consequences would be if we took more drastic action to halt expansion more broadly.

Theme	What we heard	How our GN21 plan responds to what we heard
Responsible transition (cont.)	**Accelerated depreciation** Stakeholders held a variety of views on Evoenergy's proposal to shorten lives of new, long-lived assets in response to the potential for assets stranding as a consequence of the ACT Government's foreshadowed phasing out of the gas network. **Transition impacts** Consumers are concerned about wide-ranging transition impacts and are want vulnerable consumers to be supported through the transition	We will continue to investigate the options and their costs as we develop our roadmap to 2045, and share what we find with stakeholders. Until we have greater certainty on the future of the gas network, our GN21 plan takes a conservative approach to accelerating cost recovery in response to the ACT Government's legislated emissions target by only shortening asset lives for some categories of new investment. Further work on cost recovery options will be an important part of the roadmap to 2045.
Affordability and fairness	**Affordability** Consumers are concerned about affordability and are seeking reduced network charges. **Fair tariffs** Some consumers expressed concern that the declining usage rate is not progressive and may not equally benefit low-income households who have lower gas usage per quarter. Consumers supported simplification of our tariffs. **Efficient operations to contribute to bill savings and stability** Consumers expect us to continue to operate efficiently and look for opportunities to drive further efficiency. They support the proposed operating and capital efficiency schemes.	Our plan delivers lower network charges. We have focussed on minimising costs to help achieve this, while also continuing to connect customers who want to continue to use gas. This contributes to affordability by increasing the customer base over which costs are spread. We have also proposed to continue the operation of an operating expenditure efficiency scheme and introduce a capital efficiency scheme to further incentivise the business to drive cost savings.
Safe and reliable service	Consumers value a safe and reliable gas supply and expect us to continue to prioritise reliability and safety, and to continue to maintain infrastructure while we consider the future of the gas network.	Our operating cost forecast will allow us to continue to maintain the level of service consumers told us they value and expect. The key theme of our capital investment program is to efficiently maintain the safety and integrity of the existing gas network.

Our costs

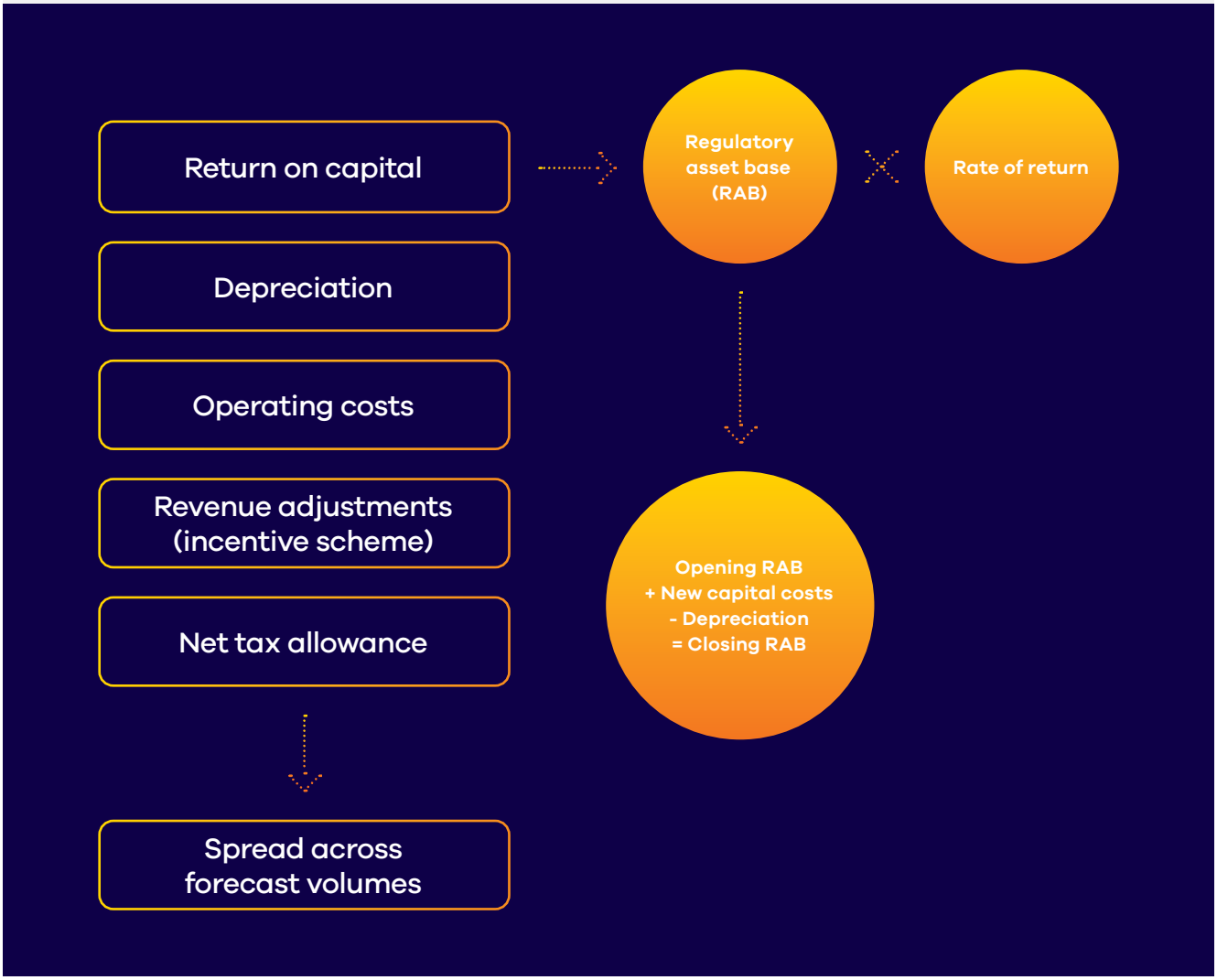
Our proposed network charges are set to allow us to earn just enough revenue to cover our forecast costs.

The AER assesses our proposed network charges against the following 'building block' cost categories:

- **return on capital**, which is a return to the asset owners for their investment in network assets;
- **depreciation**, which is the cost of our assets spread over their useful lives;
- **efficient operating and maintenance costs**, including taxes and levies imposed by the ACT Government;
- a **net tax allowance** to cover our corporate tax liabilities; and
- **revenue adjustments**, which captures the penalties or rewards arising from the AER's incentive schemes.

The building block costs are added together to determine our total revenue requirement. This is then spread over forecast volumes to determine gas distribution network charges, as shown in Figure 2 below.

Figure 2: How our network charges are calculated: revenue building blocks



Return on capital

More information about the return on capital, including our capital base and the rate of return can be found in *Attachment 4 – Capital base and depreciation* and *Attachment 5 – Rate of return* of our GN21 plan

The return on capital building block is calculated by multiplying the value of our capital base (sometimes called the regulatory asset base) by the rate of return.

Capital base

The capital base is the value of our assets and is calculated for every year of the regulatory period by adding new capex and subtracting depreciation from the previous year's capital base. Our capital base is forecast to decrease by three per cent in real terms over the 2021–26 regulatory period. By the end of 2025/26, we expect the capital base to have decreased by 14 per cent per customer since 2015/16 as shown in Figure 3 below.

Rate of return

The rate of return is set according to the AER's rate of return instrument. A placeholder value of 4.68 per cent for 2021/22 has been used in our revenue requirement forecast.

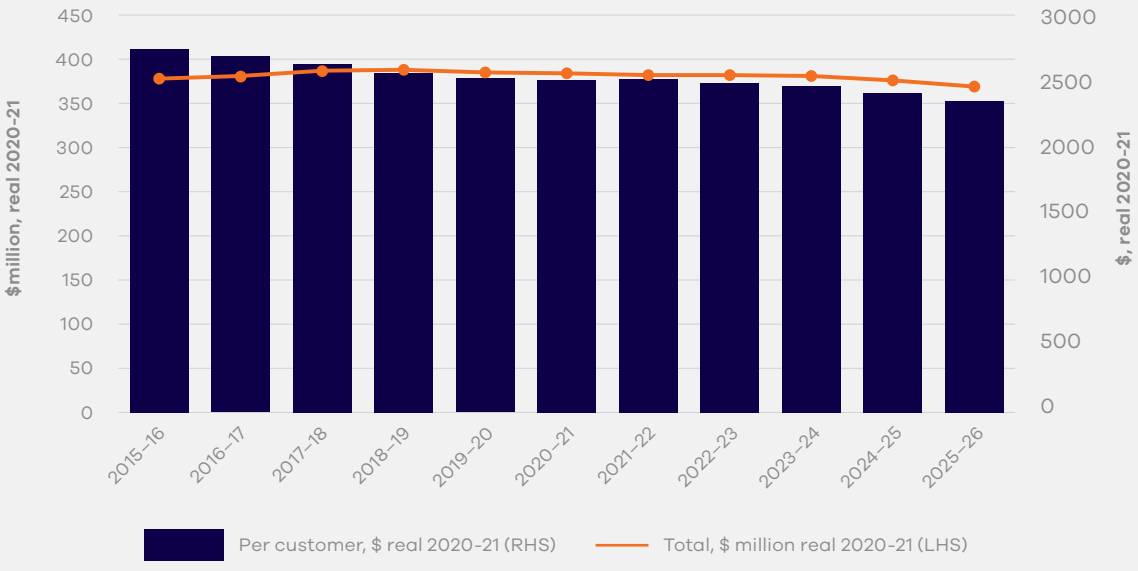
Depreciation

Depreciation is an amount equal to the asset value divided by its expected useful life. In normal operating circumstances, we typically set long asset lives reflecting the assumption that the network will be used for many decades.

But we believe that the current policy environment is not consistent with normal operating circumstances and so we are proposing to shorten the useful lives of some new, long-lived assets for calculating regulatory depreciation to reflect the likelihood that they may become obsolete before the end of their engineering lives.

More information about depreciation can be found in *Attachment 4 – Capital base and depreciation* of our GN21 plan

Figure 3: Capital base ($ million, real 2020-21)



Capital expenditure

Capex is what we spend to build and refurbish assets. We have developed our gas network capex program for the next five years taking on board consumer feedback by minimising expenditure and prioritising projects focussed on the safety and reliability of the network.

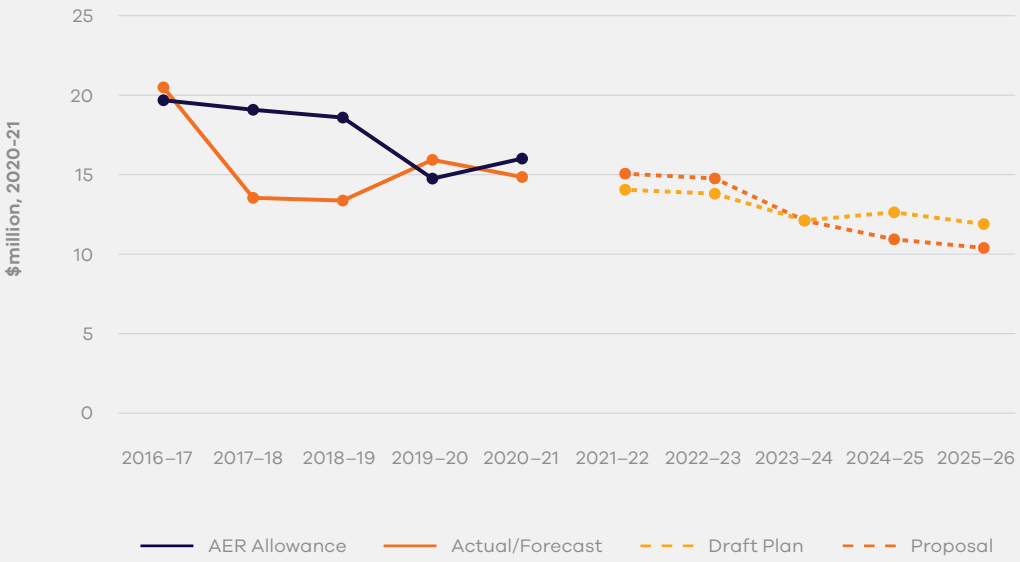
More information about our capex program can be found in *Attachment 3 – Capital expenditure* of our GN21 plan

As illustrated in Figure 4, Evoenergy's forecast capex over the 2021–26 access arrangement period is significantly below both actual and allowed spend in the current access arrangement period (18 per cent and 28 per cent, respectively). This is mainly a result of a much lower market expansion capex than historical levels, reflecting a prudent assessment of the general direction of ACT Government policy and independently assessed connection forecasts. A breakdown of the program by investment type is provided in Table 4.

Table 4: 2021-26 capex forecast by category

($m, 2020/21)	
Market expansion	26.3
Capacity development	0.9
Stay in business - network renewal	12.9
Stay in business - meter renewal	23.6
Gross capex	**63.8**
Capital contributions	0.5
Net capex	**63.3**

Figure 4: Allowed, actual and forecast capex 2016/17 – 2025/26



Operating and maintenance costs

Operating and maintenance costs represent the single largest building block. Our operating costs are generally those costs that recur every year. They include day-to-day expenses such as staff, equipment and training. Over a quarter of our operating costs is made up of costs Evoenergy has no control over, including ACT Government charges and levies like the utilities network facilities tax (UNFT) and energy industry levy (EIL).

We have used the AER's preferred approach to forecasting operating costs for the majority of costs for the 2021–26 access arrangement period, which is known as the 'base-step-trend' method. We have prepared our forecast using a 'bottom-up' category specific approach for government charges and the cost of unaccounted-for gas (UAG), which is a small amount of gas 'lost' in the network as a result of gas measurement and calculation errors and to a lesser extent, physical losses.

More information about our operating costs can be found in *Attachment 2 – Operating expenditure* of our GN21 plan

Tax expenses

We have calculated net tax expenses in line with the AER's approach.

Figure 5: Operating costs forecast, 2021–26

Total operating costs forecast of $175.1 million			
$113.0 million base year operating costs	**$2.0 million to trend base operating costs**	**$2.3 million for a step change**	**$57.9 million category specific forecasts**
• We are proposing 2019/20 as our efficient base year for forecasting purposes	• The rate of change we apply to trend base operating costs includes: • Real labour price growth • Network growth including the number of customers we serve and length of our gas mains • Expected improvement in productivity	• To change treatment of pigging (pipeline monitoring) activities from capex to operating costs	• Costs that we have forecast using specific forecasts for each category and include: • UNFT of $45.3 million • EIL of $3.2 million • UAG of $8.8 million

*May not sum due to rounding.

Incentive schemes

Under the regulation framework, network businesses can be subject to incentive mechanisms to encourage efficiency in the provision of services. Such schemes encouage us to find better ways of delivering services, and reduce costs, ultimately benefiting customers through lower bills.

More information about our proposed incentive schemes can be found in *Attachment 9 – Incentive schemes* of our GN21 plan

We currently operate under an operating expenditure efficiency carryover mechanism (ECM), and our revenue requirement includes $6.1 million returned to customers under this scheme.

In the 2021–26 period, we are proposing to continue the ECM, and also introduce a new incentive scheme applying specifically to capex, a CESS.

Summary of our proposed revenue requirement

Our proposed revenue requirement of $294 million is 10 per cent below the AER's final decision for the current 5-year period, and 13 per cent lower on a per customer basis.

The forecast value of each of the building blocks discussed above and the resulting revenue requirement are summarised in Table 5.

More information about our proposed revenue requirement can be found in *Attachment 8 – Revenue requirement and prices* of our GN21 plan

Table 5: Revenue requirement building blocks

	2021/22	2022/23	2023/24	2024/25	2025/26	Total
Return on capital	17.5	17.0	16.4	15.7	14.9	81.5
Regulatory depreciation	6.6	7.4	8.2	9.0	9.7	40.8
Operating costs	34.6	35.2	34.6	35.3	36.4	176.1
Revenue adjustments	-1.6	-2.3	-0.9	-1.3	0.0	-6.1
Net tax allowance	0.4	0.3	0.2	0.2	0.3	1.4
Revenue requirement (unsmoothed)	57.5	57.6	58.5	58.8	61.3	293.7

*May not sum due to rounding.

In addition to forecasting the building block costs, we must also determine how revenue is recovered in each year of the 2021–26 period. We are proposing to pass on all of the real price reduction to customers in the first year of the regulatory period, followed by zero real price changes in the following years. Given the feedback we have heard from our customers around affordability concerns, we believe it is appropriate to pass on lower prices to our customers as early as possible.

Forecast customer numbers and usage

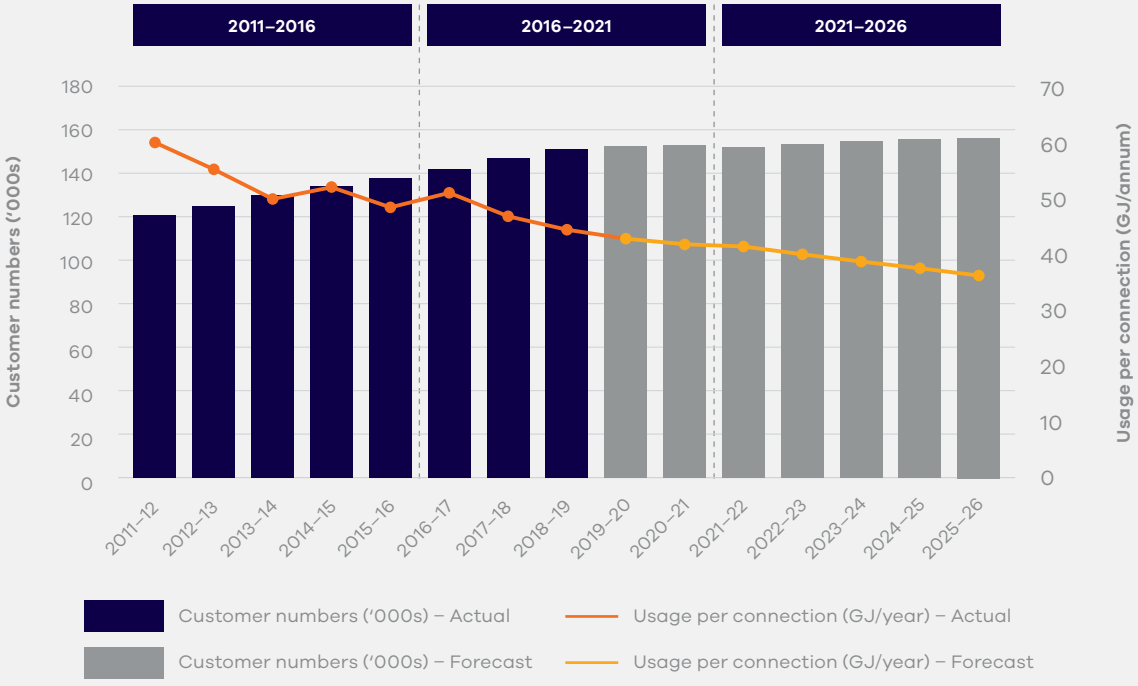
Gas demand forecasts are a critical input into our GN21 plan. The forecasts are used to determine Evoenergy's operating costs and capex requirements, as well as Evoenergy's reference tariffs for the 2021–26 period.

Evoenergy commissioned the Centre for International Economics, as expert consultants to develop an independent and detailed forecast of demand and customer numbers for Evoenergy's gas distribution network.

Based on this forecast, we expect customer connections to increase by about three per cent (which is a much lower rate than in the past) and average gas usage per customer to decline by about 14 per cent over the period. The combined effect is declining total gas usage over the period.

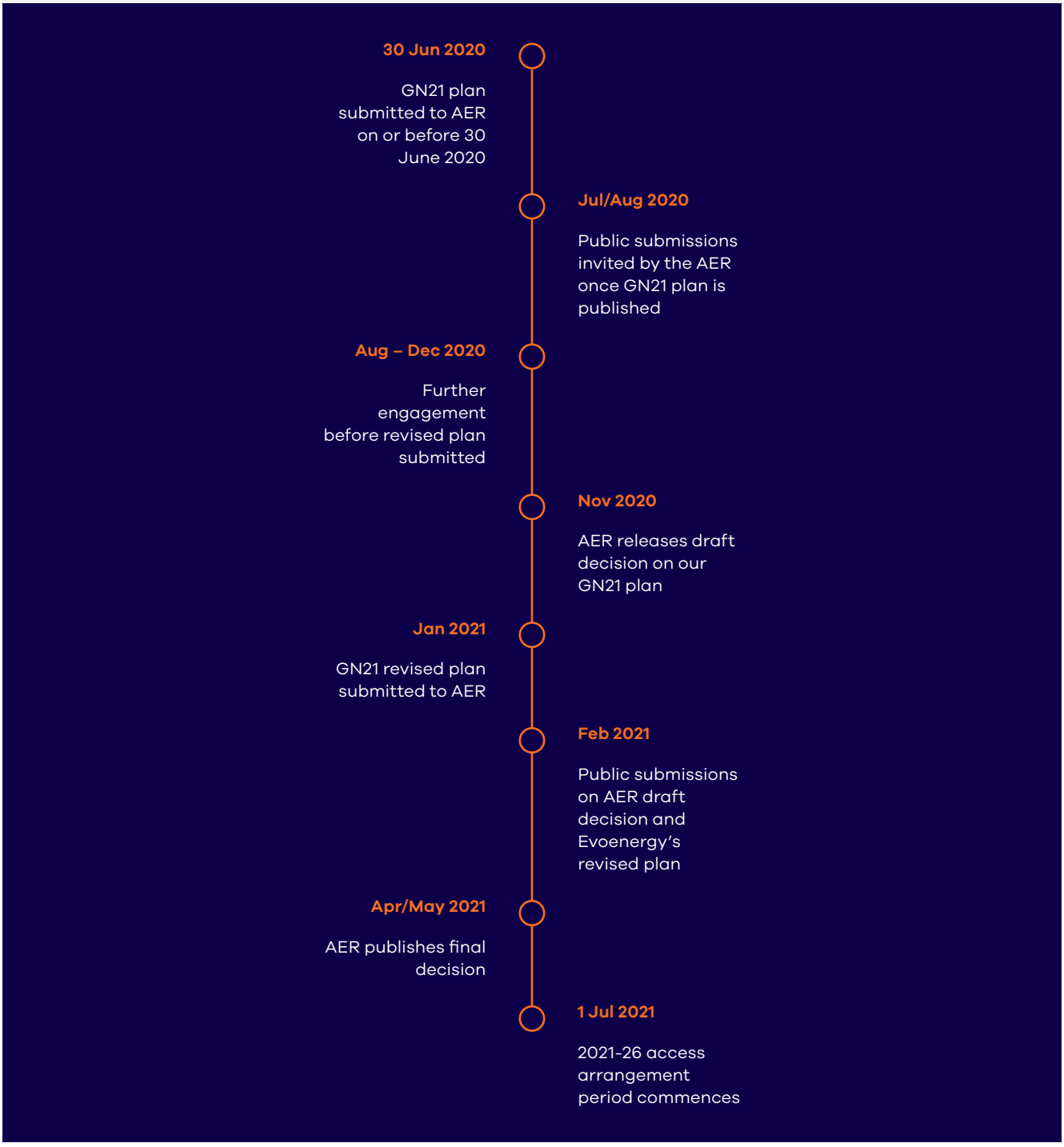
More information about our forecast of customer numbers and usage can be found in *Attachment 7 - Demand forecast and customer numbers* of our GN21 plan

Figure 6: Volume market historical and forecast connection numbers and usage



It's not too late to have your say

While we have now submitted our GN21 plan to the AER for its review, it's not too late to provide feedback. The indicative program for the review is provided below. More information can be found on Evoenergy's GN21 web page and the AER's GN21 web page.



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