Attachment 14.4

Revenue and Pricing

Response to AER Draft Decision

January 2023

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1 Revenue and pricing

We are proposing a 6% (after inflation) increase to our prices from 1 July 2023.

1.1 Overview

This attachment sets out our response to the AER's Draft Decision on revenue and pricing for our Multinet gas distribution network over the next (2023/24 to 2027/28) Access Arrangement (AA) period.

1.2 Stakeholder and Customer Feedback

Table 1.1: Summary of the AER's Draft Decision on revenue and pricing

What we heard	Our response
Customers and stakeholders told us that affordability is their highest priority. Customers told us affordability means fair and transparent prices, manageable risk and forward visibility to avoid 'bill shock' Gas is a significant cost for many major users (commercial and industrial customers) and they stressed the importance of keeping costs low. Stakeholders have also queried the existing declining block tariff structure, which structure reflects the low marginal cost of increasing the supply of gas to customers and is designed to encourage greater network utilisation. Stakeholders have also raised whether encouraging utilisation of our network is appropriate given the current decarbonisation of the energy sector. As a regulated business, we have regard to the NGR when designing our tariffs. In its current form, the NGR encourages us to design tariffs in such a way that network utilisation is maximised such that the cost of our service to each customer is minimised to the greatest extent possible.	In developing our Final Plan we have had regard for the impact individual aspects of the plan will have on the affordability of natural gas. Our tariffs are designed so that a customer's bill does not rise dramatically during peak periods such as winter when space heating in Victoria and Albury drives high consumption. We believe that customers are able to respond to price signals because retailers largely reflect our distribution tariffs in their retail tariffs. The removal of seasonal pricing was tested with customers directly through our customer workshops, with around 80% of participants supporting the change. We therefore see an opportunity to simplify our tariff structures, lowering these transactional costs, sending clearer price signals to customers and providing more transparency for all stakeholders in the long-term. In this Final Plan we propose to remove the seasonality in our prices.

1.3 AER Draft Decision

The AER's Draft Decision in respect of our revenue and pricing is summarised in Table 1.1 below.

Table 1.2: Summary of the AER's Draft Decision on our revenue and pricing forecasts

	AER Draft Decision	AER Comment
Network Revenue		
Building Block Total Revenue	Modify	The AER's Draft Decision revenue was $1,013 million ($2022/23) reflecting the reductions to the proposed building blocks for the return on capital, depreciation, opex and revenue adjustments.

	AER Draft Decision	AER Comment
Price path	Modify	Expressed in real terms, the Draft Decision provided for flat prices (0% price changes) across all years of the next AA period.[1]
Ancillary reference services	Accept	The AER did not accept our proposed classification of small consumer connection abolishments as an ARS. The AER outlined two cost recovery approaches in its Draft Decision and invited AGN's revised proposal and stakeholder submissions to comment on the merits of each.[2]
Prices		
Current Pricing Structure	Modify	Satisfied our proposed structure of the reference tariffs for the next AA period complies with the requirements of the NGR and also consistent with those which applied in the current AA period with one exception, i.e. the proposed abolishment ARS.[3] The AER was satisfied that the retention of the declining block tariff structure is consistent with the price cap form of control. We proposed removing the seasonal aspect to our tariff structure and the AER has accepted this structure in the Draft Decision PTRM and AA document. However in Attachment 9 of its Draft Decision it states that it 'accept(s) the simplification of tariffs by removing the seasonal shoulder charges. MGN submitted that the move to simplified tariffs with only peak and off peak charges was supported by around 80% of its participants in its customer workshops'. Our Final Plan proposed the removal of all seasonal aspects to our tariff structure and instead that one set of prices should apply throughout the year. We acknowledge that it likely was the AER's intention to accept the removal seasonal pricing as the tariffs in the Draft Decision PTRM reflected our proposal in this regard. We have however classified this aspect of its decision as a 'Modify' pending clarification of this matter.
Allocation of revenue and costs	Accept	Satisfied with our approach to allocating revenue and costs between our reference and non-reference services.[4]

[1] Draft Decision, Overview, p.9
[2] Draft Decision, Overview, p.vii
[3] AER Draft Decision, Attachment 9, p.1
[4] AER Draft Decision, Attachment 9, p.5

	AER Draft Decision	AER Comment
Haulage Reference Service Tariff Classes	Accept	Satisfied the proposed tariff classes are consistent with the requirements of the NGR.[5]
Tariff variation mechanism	Accept	Accepted our proposed reference tariff variation mechanism for the next AA period.[6]
Weighted Average Price Cap formula	Accept	Approved the weighted average price cap formula.[7]
Cost pass through mechanisms	Modify	Accepted the proposed cost pass through events but made amendments to the definitions of Insurance Cap Event (changed to Insurance Coverage Event), Insurer's Credit Risk Event, Natural Disaster Event and Terrorism Event.[8]

Note: In this 'traffic light' table, green shading represents the acceptance, orange represents a modification and red shading represents a rejection

1.4 Our response to the Draft Decision

Table 1.3: Summary of our response to the AER's Draft Decision on our revenue and pricing

	AER Draft Decision	Our Response	Our Comment
Revenue & Prices			
Building Block Total Revenue	Modify	Modify	Building Block Revenue has been updated reflecting updates to our Final Plan
Price path	Modify	Modify	Price Path has been updated reflecting updates to our Final Plan. The price path is for a 3% increase in year 1 followed by 1.0% price rises thereafter (in real terms). This is equivalent to a one-off price increase of 8.4% in nominal terms.
Ancillary reference services	Modify	Modify	We accept the AER's Draft Decision to approve the majority of our ancillary reference services for the next AA period. We maintain our position that small customer abolishment should be an ancillary reference service.
Current Pricing Structure	Modify	Modify	We accept the AER's Draft Decision noting the issue outlined above.

[5] AER Draft Decision, Attachment 9, p.6
[6] AER Draft Decision, Attachment 10, p.1
[7] AER Draft Decision, Attachment 9, p.16
[8] AER Draft Decision, Attachment 10, p.8

	AER Draft Decision	Our Response	Our Comment
Allocation of revenue and costs	Accept	Accept	We accept the AER's Draft Decision
Haulage Reference Service Tariff Classes	Accept	Accept	We accept the AER's Draft Decision
Tariff variation mechanism	Accept	Modify	We accept the AER's Draft Decision. We will submit modifications to the Tariff Variation Mechanism to take account of the Safeguard Mechanism in our response to the AER's Draft Decision.
Weighted Average Price Cap formula	Accept	Accept	We accept the AER's Draft Decision
Cost pass through mechanisms	Modify	Accept	We accept the AER's Draft Decision

Note: in this 'traffic light' table, green shading represents the acceptance, orange represents a modification and red shading represents a rejection

1.5 Adjustments to Tariff Variation Mechanism

1.5.1 Safeguard Mechanism

We are proposing an additional factor to be included in the reference tariff variation formulae in relation to the Government's recently announced Safeguard Mechanism.

The Safeguard mechanism, which is legislated as part of the *National Greenhouse and Energy Reporting Act 2007* and *Safeguard Mechanism Rule.* The Safeguard Mechanism requires facilities in Australia which are responsible for more than 100,000 tonnes of carbon dioxide equivalent per annum (a 'Designated Large Facility') to keep their net emissions below an emissions limit (a 'calculated emissions baseline' or simply 'baseline'). Multinet Gas Networks is a Designated Large Facility. To date safeguard mechanism baselines have not provided a binding constraint on emissions. However, reforms in the final stages of development are expected to create a binding constraint on net emissions.

Costs are not known at this time, however, we believe the reforms will most likely impose costs on our business. These costs will either be incurred in reducing emissions or, in the near term, will most likely involve the purchase and surrender of emissions credits to ensure that net emissions from the network remain within the baseline. Net emissions above the baseline would incur civil penalties which are not acceptable to our business.

The costs associated with the Safeguard Mechanism are not yet known and will continue to change as supply and demand for emissions credits (and the relative costs of emissions reductions) evolves over time. We expect the costs may be lower than the materiality threshold for cost pass through events, at least in the near term and therefore we have included amendments to the Reference Tariff Variation Mechanism formulae to capture these additional costs in our reference prices.

We have included the proposed changes to the Tariff Control Formula as Appendix A at the end of this attachment.

1.6 Additional Cost Pass Through Events

1.6.1 Credit Support

A key issue raised by retailers through the engagement process was the alignment of the credit support arrangements in the AA Document with other jurisdictions (where the National Energy Customer Framework (NECF) applies).

In our Final Plan, our primary position is that the current credit support arrangements are appropriate. We remain of the view that if the credit support arrangements in the AA Document were to be changed, given the context noted above, the appropriate way to do so would be through a Rule change process.

However, we acknowledge the stakeholder feedback and AER's Draft Decision and with our revised Final Plan we have provided an alternative approach to credit support in respect of retailers. This approach is closely aligned to jurisdictions where the National Energy Customer Framework (NECF) applies.

Several changes have been made to the Access Arrangement to effect this change. No changes were required to the existing General Terms & Conditions (clause 27 Credit Support).

Clause 4.5 Cost Pass Through Event Adjustment, has been modified so there is no materiality threshold applied to a Retailer Insolvency Event. The definition of Retailer Insolvency Event has also been amended to disconnect it from NECF in the event it is implemented in Victoria.

Clause 4.7 has been amended to include 'Fixed Principle C', which allows AGN to recover costs not fully recovered and incurred from a Cost Past Through Event (ie Retailer Insolvency Event) in the next Access Arrangement Period. Fixed Principle C applies until the end of the Seventh Access Arrangement Period.

Further, AGN has introduced new clause 6.5 AGN's Credit Policy, which has two sections, sub-clause 6.5.1 Gas Retailers and sub-clause 6.5.2 Other Network Users. Clause 6.5.1 makes clear that no credit support will be required of retailers, subject to certain conditions involving the failure to pay statements of charges.

Sub-clause 6.5.2 states a Retailer Insolvency Event Cost Pass Through does not apply to Self-Contracting Users. AGN has widened the definition of 'acceptable credit rating' to include a rating of Baa2 or higher as rated by Moody's Investor Service, in addition to the rating of BBB or higher by Standard & Poors.

1.6.2 Abolishments

'**Unrecovered Abolishment Event'** means that, as at the end of any Financial Year:

a there are any charges which have not been recovered by AGN on account of the Ancillary Reference Service known as Service Abolishment – Residential – or the Non-reference Service known as Service Abolishment – Industrial and Commercial, and which no Gas Retailer has been able to recover from any Shared Customer or which AGN has no reasonable prospect of recovering; or

a there are costs which AGN have incurred in cutting and capping any service and removing assets in circumstances where no Service Abolishment – Residential or Service Abolishment – Industrial and Commercial was requested but the service had to be cut and capped or assets removed because that was required by law or for other reasons relating to the safe and prudent operation of the Network,

(to the extent those charges and costs in aggregate exceed the Materiality threshold).

1.7 Summary

Table 1.4 provides the revised building block total revenue including and excluding ARS.

Table 1.4: Building Block Revenue 2023-24 to 2027-28 ($nominal, million)

	2023-24	2024-25	2025-26	2026-27	2027-28
Return on Capital	76.4	82.4	90.1	96.1	102.2
Return of Capital (Regulatory Depreciation)	41.2	40.3	45.9	50.3	52.7
Opex	87.2	89.2	91.2	92.5	95.4
Incentive Mechanism	-0.3	-6.5	-5.1	-5.2	-7.1
Cost of Tax	7.2	4.7	2.7	3.7	3.8
Building Block Total Revenue (including ARS)	**211.8**	**210.1**	**224.8**	**237.5**	**246.9**
Less ARS	2.6	2.7	2.9	3.0	3.1
Building Block Total Revenue (excluding ARS)	**209.1**	**207.4**	**222.0**	**234.5**	**243.8**

Table 1.5 presents the “smoothed” tariff revenue and price path for Multinet.

Table 1.5: Proposed Price Path, 2023-24 to 2027-28 ($nominal, million)

	2023-24	2024-25	2025-26	2026-27	2027-28
Building Block Revenue	209.1	207.4	222.0	234.5	243.8
Price Revenue	222.0	223.7	224.1	222.2	219.3
Real Price Path	**-3.00%**	**-0.97%**	**-0.97%**	**-0.97%**	**-0.97%**

Appendix A Tariff Control Formula including Safeguard Mechanism

Tariff Control Formula

The following formula applies separately to each of Tariff R, C and D:

$$(1 + \Delta CPI_t)(1 - X_t)(1 + PT_t)(1 + C_t) \geq \frac{\sum_{i=1}^{n} \sum_{j=1}^{m} p_t^{ij} q_{t-2}^{ij}}{\sum_{i=1}^{n} \sum_{j=1}^{m} p_{t-1}^{ij} q_{t-2}^{ij}}$$

where:

ΔCPI_t is the annual percentage change in the ABS CPI All Groups, Weighted Average of Eight Capital Cities from the June December quarter in year t-2 to the June December quarter in year t-1, calculated using the following method:

The ABS CPI All Groups, Weighted Average of Eight Capital Cities for the June December quarter in year t-1

divided by

The ABS CPI All Groups, Weighted Average of Eight Capital Cities for the June December quarter in year t-2

minus one.

If the ABS does not, or ceases to, publish the index, then CPI will mean an index which the AER considers is the best available alternative index.

t is the year for which tariffs are being set;

X_t is the X factor for each financial year of the 2023/24-2027/28 Access Arrangement Period as determined in the PTRM as approved in the AER's final decision, and annually revised for the return on debt update calculated for the relevant year during the Access Arrangement Period in accordance with that approved in the AER's final decision;

C_t is the Safeguard Mechanism adjustment for year t calculated as outlined in Box 5;

PT_t is the cost pass through factor for year t calculated as outlined in Box 2;

n is the number of different Reference Tariffs;

m is the different components, elements or variables ("components") comprised within a Reference Tariff;

p_t^{ij} is the proposed component *j* of Reference Tariff *i* in Financial Year *t*;

p_{t-1}^{ij} is the prevailing component *j* of Reference Tariff *i* in Financial Year *t-1*; and

q_{t-2}^{ij} is the verified annual quantity of component of Reference Tariff *i* sold in Financial Year *t-2* (expressed in the units in which that component is expressed (e.g., GJ)).

The Safeguard Mechanism Factor is:

C_t is the Safeguard Mechanism pass through adjustment to the Distribution price control in Financial Year *t* for the Service Provider as determined below. For the purpose of this formula the Safeguard amount includes all costs incurred in meeting the Safeguard mechanisms set out in the *National Greenhouse and Energy Reporting Act 2007*.

Calculation of the Safeguard Mechanism factor:

The Safeguard Mechanism Factor C_t, for the Service Provider is:

$$C_t = \frac{(1 + C'_t)}{(1 + C'_{t-1})} - 1$$

where:

If *financial year t* is 2023/24

$$C'_t = \frac{cf_{t-1}(1 + realWACC_t)^{\frac{3}{2}}(1+\Delta CPI_t)^{\frac{3}{2}} + \Delta cf_{t-2}(1 + realWACC_{t-1})\ \ (1 + realWACC_t)^{\frac{3}{2}}(1+\Delta CPI_{t-1})(1+\Delta CPI_t)^{\frac{3}{2}}}{(1+\Delta CPI_t)(1-X_t)(1+PT_t)\sum_{i=1}^{n}\sum_{j=1}^{m} p_{t-1}^{ij} q_{t-2}^{ij}}$$

If *financial year t* is any other year in the AA period

$$C'_t = \frac{cf_{t-1}(1 + realWACC_t)^{\frac{3}{2}}(1+\Delta CPI_t)^{\frac{3}{2}} + \Delta cf_{t-2}(1 + realWACC_{t-1})\ \ (1 + realWACC_t)^{\frac{3}{2}}(1+\Delta CPI_{t-1})(1+\Delta CPI_t)^{\frac{3}{2}}}{(1+\Delta CPI_t)(1-X_t)(1+PT_t)\sum_{i=1}^{n}\sum_{j=1}^{m} p_{t-1}^{ij} q_{t-2}^{ij}}$$

C'_{t-1} if financial year *t* is the financial year ending 30 June 2024, the value is zero; and

if financial year *t* is after the financial year ending 30 June 2024, C'_{t-1} is the value of the C_t determined in financial year *t*-1.

cf_{t-1} is the estimate of the Safeguard mechanism costs incurred by the Service Provider for the financial year ending June of the financial year *t*-1.

Δcf_{t-2} is the actual Safeguard mechanism cost for regulatory year t-2 less the estimated Safeguard mechanism cost for financial year *t-2.* For the avoidance of doubt, the estimated Safeguard mechanism cost for financial year *t-2* is the same as cf_{t-1} determined for financial year *t-1*

$realWACC_t$ is the real vanilla weighted average cost of capital as set out in this final decision and updated annually within the PTRM for financial year t

$realWACC_{t-1}$ is the real vanilla weighted average cost of capital as set out in this final decision and updated annually within the PTRM for financial year t-1