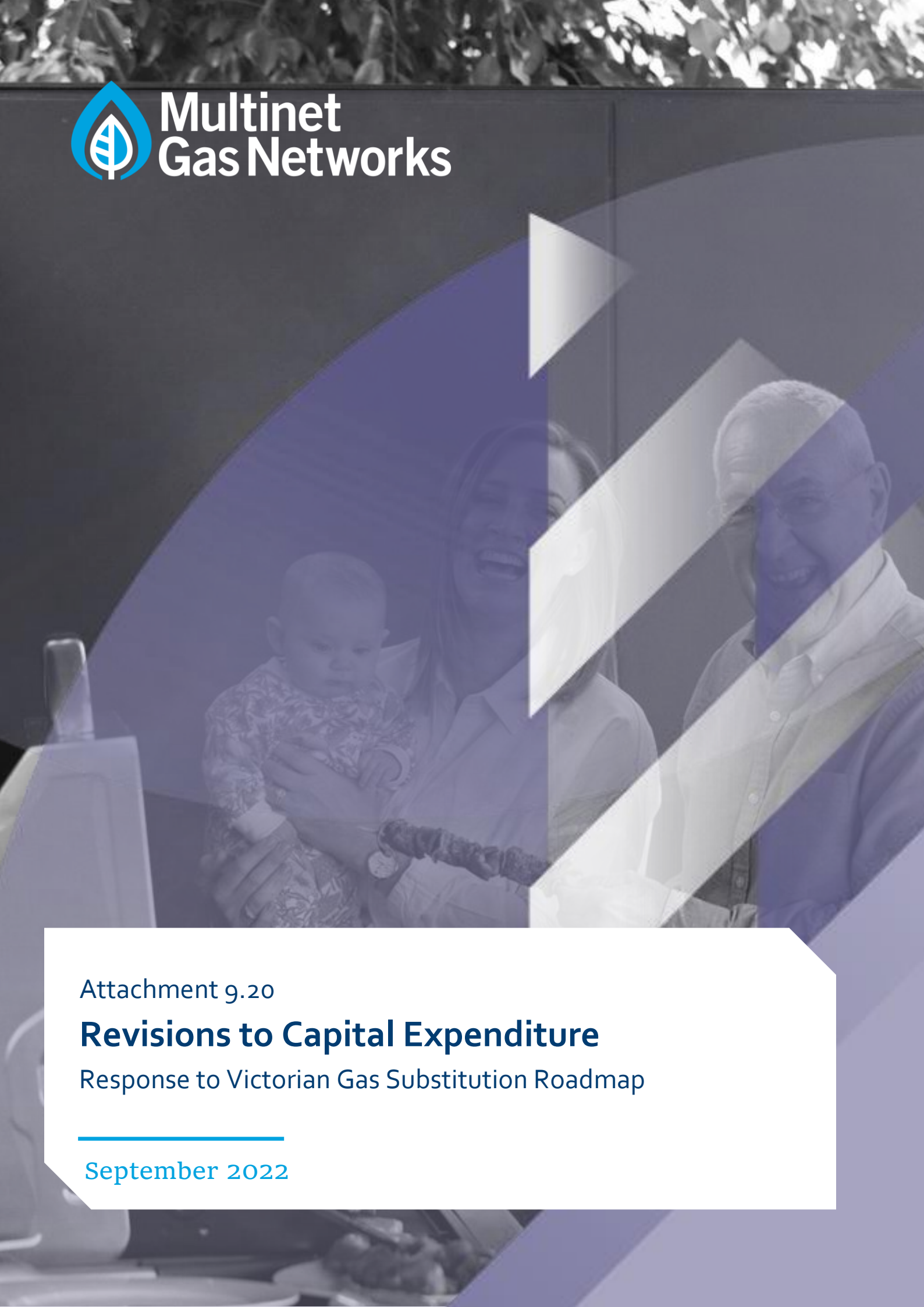


Multinet Gas Networks

Attachment 9.20

# Revisions to Capital Expenditure

Response to Victorian Gas Substitution Roadmap

September 2022

# 1 Revisions to Capital Expenditure

**We are investing $669 million in our Multinet Gas network in the next AA period.**

## 1.1 Overview

This attachment sets out revisions to our Final Plan capital expenditure (capex) proposal for the Multinet Gas distribution network over the next (2023/24 to 2027/28) Access Arrangement (AA) period in response to the Victorian Government's Gas Substitution Roadmap (GSR). In the next AA period we propose to invest $669 million, which is $53 million (or 7%) lower than our Final Plan.

The GSR provides a number of incentives and policy measures to encourage electrification of some gas loads, particularly in the residential sector. Much of our capex is required to ensure ongoing safety and reliability of our networks, compliance with our obligations, and meeting the customer service expectations of our customers. This will not change. However, the GSR measures will impact the way some of our existing customers use gas in their homes and businesses, as well as the number of new homes and businesses connecting to our gas networks in the future. In particular, the GSR will encourage:

- Greater uptake of reverse cycle air-conditioning and electric heat-pump hot water systems through increased incentives to purchase these appliances and removal of existing incentives for equivalent natural gas appliances; and
- More new homes and sub-divisions going "all-electric" through changes to planning codes and a new 7-star home program.
- The focus of our response to the GSR therefore relates to those few areas where revisions to our Final Plan are required. In terms of capex, the key revisions are:
- A significant reduction in growth capex to $97 million ($19 million or 16% lower than our Final Plan), reflecting a reduced forecast of new customers connecting to our network over the next AA period of 28,000 (down from 36,000 in our Final Plan);
- A reduction in augmentation capex to $2 million ($8 million or 82% lower than our Final Plan), and some changes to timing of projects, reflecting the impacts of increasing disconnections over the next AA period above;
- Minor reductions to a number of areas reflecting the impacts of higher disconnections forecast over the next AA period, including:
  - meter replacement capex ($1 million or 2% lower than our Final Plan); and
  - proactive service replacements as part of proactive mains replacement ($2 million or 0.5% lower than our Final Plan); and
  - reactive service replacements capex ($0.1 million or 2% lower than our Final Plan); and
- A change to the application of CPI between June 2021 and June 2023 in our capex model in line with discussions with the AER following submission of our Final Plan ($24 million or 3% lower than our Final Plan).

All other aspects of our Final Plan capex remain unchanged.

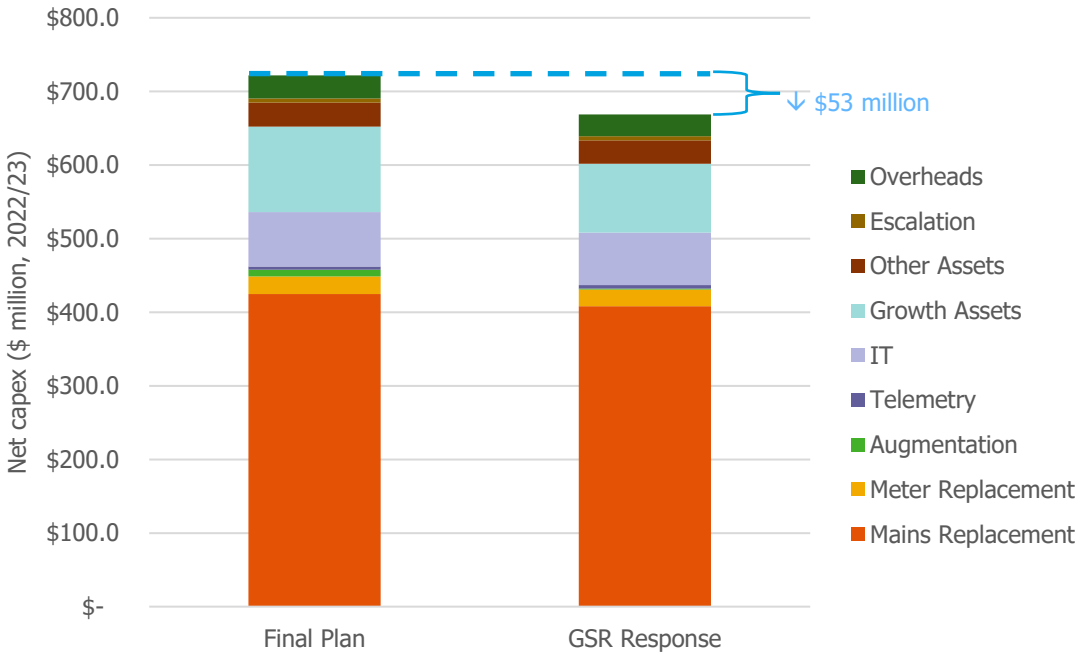
Table 1.1 provides an overview comparing our GSR Revisions capex forecast to our Final Plan capex forecast for the next AA period.

Table 1.1: Comparison of our revisions to capex for the next AA period with the Final Plan ($ million, 2022/23)

| | Final Plan | GSR Response* | Key drivers |
|---|---|---|---|
| Mains Replacement | 424.8 | 408.3 | • GSR has no impact on safety and integrity drivers<br>• Additional existing customer disconnections see minor reductions to proactive and reactive service replacements |
| Growth Assets | 115.8 | 93.7 | • Significant reduction in the forecast number of new residential connections |
| IT | 73.9 | 71.4 | • GSR has no impact on the integrity and customer service drivers for our IT program |
| Meter Replacement | 23.7 | 22.4 | • Additional existing customer disconnections see minor reduction to meter replacements |
| Augmentation | 9.1 | 1.5 | • Additional existing customer disconnections and lower new residential connections growth sees only two of the proposed augmentations still required within the next AA period |
| Telemetry | 4.7 | 4.5 | • GSR has no impact on the integrity drivers of our telemetry capex. |
| Other assets | 32.9 | 31.8 | • GSR has no impact on the safety and integrity drivers of our other capex |
| Escalation | 5.7 | 5.3 | • Lower escalation on account of lower capex |
| Overheads | 31.0 | 29.7 | • Lower overheads on account of lower capex |
| **Total** | **721.6** | **668.7** | |

*Our GSR Response capex also incorporates a change to the application of CPI between June 2021 and June 2023 in line with discussions with the AER following submission of our Final Plan. This change reduces the Final Plan capex by around $24.1 million.

Figure 1.1: Total net capex by driver, Final Plan vs GSR Response




## 1.2 Customer and stakeholder feedback

### 1.2.1 Customers

As highlighted in our Final Plans, we found customers' key priorities are affordability, safety and reliability, customer service and preparing for the future. Customers trust our track record of strong safety and reliability performance and 91% of customers were comfortable with our proposed mains replacement to maintain our safety and reliability performance. There was also strong support from customers for our plans to prepare our networks for a renewable future.

Our GSR response maintains all of our safety, integrity and customer service driven programs, as well as our small capex programs to prepare for the potential future for renewable gases to be used in distribution networks. This will ensure we continue to meet the expectations of our customers over the next AA period.

### 1.2.2 Stakeholders

As highlighted in our Final Plan, stakeholders agreed safety and reliability should be maintained. Many also stressed the need for discretionary capex to be minimised to ensure customers aren't paying any more on their bills than they need to. This was particularly stressed given the relative uncertainty of the future of the gas networks.

The absence of clear policy at the time of our Final Plan meant stakeholders and retailers found it challenging to form a view on whether our Final Plans were capable of acceptance. This resulted in 'a holding point rather than a landing point' in respect of key aspects of our Plans: Challenges included consistency of our proposed accelerated depreciation with growth capex and investments in hydrogen readiness.

Since the release of the GSR, we have engaged with stakeholders on how we interpret the measures in the GSR and what impacts it has on our plans. In the sessions to date we have heard stakeholders expect to see changes like the 7-star new home program take some time to filter through. Stakeholders have

also asked if we would change our mains replacement program and hydrogen readiness in light of the electrification push in the GSR.

Table 1.2: Summary of relevant customer and stakeholder insights

| What we heard | Our response |
|---|---|
| **Final Plan** | |
| • Customers trust our track record of strong safety and reliability performance and 91% of customers were comfortable with our plans to maintain our safety and reliability performance.<br>• Stakeholders have indicated a preference for discretionary capex to be minimised and some struggled to support parts of our capex proposals (e.g. growth capex and augmentation) given the uncertain policy position. | Our GSR response ensures we can maintain current levels of safety and reliability. Specifically, many of our programs which have safety and integrity drivers are unchanged, and we will continue to prioritise the replacement of our remaining older material low pressure mains.<br>Our GSR response responds to the policy position set out in the Roadmap and stakeholder feedback received on our capex before the Roadmap was released by reducing growth capex and network augmentation, as well as making minor adjustments to meter replacement and service replacement volumes related to existing customer disconnections. |
| **GSR Engagement** | |
| • Stakeholders asked whether we were revising our mains replacement program in light of the GSR.<br>• Stakeholders questioned whether we were reconsidering hydrogen readiness expenditures, given the strong push towards electrification under the GSR.<br>• Stakeholders commented they expected changes to the 7-star new home would take at least 12 months to filter through. | Our GSR response maintains our position on mains replacement, as the safety drivers of the program have not changed. We have however made a small top-down adjustment to our proactive and reactive service replacement costs on account of forecast customer disconnections under the GSR.<br>Our GSR response maintains our small hydrogen adaptation capex which we consider is important in preparing for the potential future for renewable gases to be used in distribution networks and the consideration or renewable gas targets foreshadowed in the GSR. This is discussed at 1.4.7 below.<br>Our GSR response demand forecast sees a phased decline in new connection volumes over the next AA period. |
| **GSR Outcome** | |
| We have reduced our proposed capex by around $53 million in response to the GSR. Our GSR response meets the expectations of our customers and stakeholders by:<br>• significantly reducing our connections and augmentation capex in line with the policy positions set out;<br>• maintaining our proposed small capex programs to prepare for the potential future for renewable gases to be used in distribution networks foreshadowed; and<br>• maintaining our capex programs which ensure ongoing safety and reliability of our networks, compliance with our obligations, and meeting the customer service expectations of our customers.<br>We have provided detailed supporting information on our changes to our augmentation program and in the revised capex model in Attachments 9.6A and 9.11A. | |
| Customers were highly supportive of our capex plans, including efforts to prepare the network for renewable gas. | |
| We have reflected the GSR policy positions in our capex plans which should address the difficulty stakeholders were having with accepting some parts of our plans. | |

## 1.3 Our Approach

### 1.3.1 Background

Our capex forecast for the next AA period is developed using a bottom-up approach, with the cost of undertaking each project and program estimated separately. The proposed projects and programs are built up having regard to our overarching Business Plans such as our Asset Management Strategy, Asset Management Plan, risk management framework, regulatory obligations, projected network growth and the expectations of our customers.

### 1.3.2 Remodelling

Most of our investment reflects the continuation of existing programs that we undertake to ensure strong safety and reliability of our network and compliance with our obligations. Much of this remains unchanged.

Our growth capex is the sum of new connections, by type, multiplied by the cost of each connection type. We have remodelled our growth capex using new connection volumes in line with our revised demand forecast. For more information on our revised demand forecast refer to Attachment 13.1A Core Revised demand forecast.

Our augmentation capex is developed on a bottom-up basis utilising network pressure modelling for each of our high pressure networks where we are and will continue to experience connection and load growth. We have reviewed each of the projects in our augmentation capex based on the connection and load growth changes in our revised demand forecast. For more information on our revised augmentation capex refer to Attachment 9.11A Addendum to Augmentation Business Cases.

Finally, we have applied a top down adjustment to a number of programs to account for the increased forecast of existing customer disconnections as a result of the GSR over the next AA period. These programs include:

- Time expired, reactive and 'hard to read' meter replacement; and
- Proactive and reactive service replacement.

### 1.3.3 Assumptions

Table below outlines the key assumption changes in our GSR Response that have been used in revising our capex forecasts.

Table 1.3: Key assumptions for revising our capex forecasts

| | Final Plan | GSR Response |
|---|---|---|
| Gross residential new connections | 34,384 | 27,928 |
| Existing residential customer disconnections | 21,930 | 97,603 |

## 1.4 Our capex in response to the GSR

In the next AA period we propose to invest $669 million, which is $53 million (or 7%) lower than our Final Plan. The reduced investment is primarily driven by lower new connection growth. The increased forecast of existing residential customer disconnections also has a small impact on a number of ongoing programs such as meter replacement and proactive and reactive service replacements.

Table 1.4 below provides a summary by capex driver category of the revisions we have made to our plans in response to the GSR. It also shows areas of our plans which do not change.

Table 1.4: Summary of our GSR Response by capex driver

| Capex driver category | GSR response | Key drivers |
|---|---|---|
| Mains Replacement | Revised | We have revised down our proactive and reactive service replacements to take account of the forecast increase in disconnection rates for existing customers. We expect existing customer disconnections will reduce the number of services on the network, and therefore the number that are likely to fail and require replacement over the next AA period.<br>See section 1.4.1 below for more information on our GSR Response Mains Replacement capex. |
| Growth Assets | Revised | We have revised down our growth capex to take account of the lower forecast of new residential connection growth in the next AA period.<br>See section 1.4.2 below for more information on our GSR Response Growth capex. |
| IT | No Change | We have not made any changes to our IT capex in the next AA period in response to the GSR.<br>See section 1.4.3 below (and our Final Plan) for more information on our IT capex. |
| Meter Replacement | Revised | We have made a small top-down adjustment to our meter replacement capex to take account of the forecast increase in disconnections rates for existing customers. We expect existing customer disconnections will reduce the number of meters on the network, and therefore the number that will fail or come up for time expired replacement over the next AA period. We have made a similar adjustment for our hard to read digital meter proposal.<br>See section 1.4.4 below for more information on our GSR Response Meter Replacement capex. |
| Augmentation | Revised | We have revised down our augmentation program to take account of the lower forecast of new residential connection growth and forecast increase in disconnection rates for existing customers. While many of the planned augmentations will no longer be required in the next AA period, there are a couple which will still be required – particularly where they are also important for security of supply.<br>See section 1.4.5 below and Attachment 9.11A Addendum to Augmentation Business Cases for more information on our augmentation capex. |
| Telemetry | No Change | We have not made any cost changes to our telemetry capex in the next AA period. This is because the integrity drivers for these programs do not change as a result of the GSR.<br>See section 1.4.6 below for more information on our telemetry capex. |

| Capex driver category | GSR response | Key drivers |
|---|---|---|
| Other Assets | No Change | We have not made any changes to our other assets capex in the next AA period. This is because the safety and integrity drivers for these programs do not change as a result of the GSR.<br>Our GSR response maintains our small hydrogen adaptation capex which we consider is important in preparing for the potential future for renewable gases to be used in distribution networks and the consideration or renewable gas targets foreshadowed in the GSR.<br>See section 1.4.7 below for more information on our other capex. |

### 1.4.1 Mains Replacement

Our GSR Response includes $408 million of Mains Replacement capex. As noted above, our Mains Replacement program is largely unchanged from our Final Plan. The program is the single most important thing we can do to ensure we can maintain safety and reliability for our customers.

The GSR recognises the importance of maintaining reliability through the transition, therefore, our program is consistent with the priorities of the GSR.

We have made a small adjustment (-$2 million or -0.5%) to our proactive and reactive service replacements. This adjustment revises down the costs for the number of service replacements we expect to undertake in the next AA period to take account of the forecast increase in disconnection rates for existing customers. We expect existing customer disconnections will reduce the number of services on the network, and therefore the number that will need to be renewed when we are undertaking mains renewal and the number that are likely to fail and require replacement over the next AA period.

The reduction to the cost of service replacements in our GSR Response is summarised in **Error! Reference source not found.** below.

Table 1.5: Mains Replacement revised forecast costs in the next AA period $'000 real 2022/23

| $'000 real 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 | 2027/28 | Total |
|---|---|---|---|---|---|---|
| Annual percentage of existing customer disconnections due to GSR | 0.87% | 1.64% | 2.41% | 2.85% | 3.28% | 11.05% |
| **Mains Replacement Program** | | | | | | |
| MRP – Final Plan | 78,283 | 88,469 | 81,268 | 85,407 | 91,395 | **424,821** |
| MRP – Revision | (2,806) | (3,322) | (3,193) | (3,439) | (3,766) | **(16,527)** |
| **MRP – GSR Response** | **75,476** | **85,148** | **78,075** | **81,967** | **87,628** | **408,295** |

Further detail on our mains replacement program can be found in our Distribution Mains and Services Strategy which is provided at Attachment 9.7 to our Final Plan

### 1.4.2 Growth Assets

Our GSR Response includes $94 million of Growth capex. This is a reduction of $22 million (or 19%) compared to the $116 million included in our Final Plan. The driver of this reduction is lower new residential connections as a result of the measures promoting electrification of new homes in the GSR (new planning laws and 7-star efficiency rating). Gross new residential connection numbers have been

revised down to 28,000 in the next AA period (down from 34,000 in the Final Plan). There has been no change to commercial or industrial new connections at this time.

Table 1.6: Revised Growth volumes

| Volumes | 2023/24 | 2024/25 | 2025/26 | 2026/27 | 2027/28 | Total |
|---|---|---|---|---|---|---|
| Annual percentage of existing customer disconnections due to GSR | 0.87% | 1.64% | 2.41% | 2.85% | 3.28% | 11.05% |
| **New Residential Connections** | | | | | | |
| New Residential Connections – Final Plan | 7,752 | 6,857 | 6,570 | 6.602 | 6,603 | **34,384** |
| New Residential Connections – GSR Response | 7,206 | 6,283 | 5,525 | 4,872 | 4,041 | **27,928** |
| **New Residential Connections – Variance** | **(546)** | **(574)** | **(1,045)** | **(1,730)** | **(2,562)** | **(6,456)** |

For more information on our new customer connections forecast and our calculation of growth capex, please see Attachment 13.2A Core GSR Response Demand Forecast Model, Attachment 9.6A Revised Capex Model – GSR Response and Attachment 9.8 Unit Rates Report (of our Final Plan).

### 1.4.3 IT

Our GSR Response includes $71 million of IT capex. As noted above, our IT capex remains unchanged from our Final Plan, except for a change in the application of CPI as noted above. Our IT program is largely driven by the lifecycle of the IT applications and infrastructure we use to run our business. We have also maintained our digital customer experience program, as while we are forecasting to see some reductions in our customer numbers over the next AA period as a result of the GSR, it is still important that we meet the customer service expectations for the over 600,000 customers we will continue to service over the next AA period.

For more information on our IT Capex, please see Attachment 9.9 IT Investment Plan and Attachment 9.19 IT Business Cases to our Final Plan.

### 1.4.4 Meter Replacement

Our GSR Response includes $22 million of meter replacement capex. The GSR does not change our compliance obligations to maintain accurate metering.

We have made a small adjustment (-$1 million or -5%) to our time expired, reactive and hard to read meter replacement programs. This adjustment revises down the number of meter replacements we expect to undertake in the next AA period to take account of the forecast increase in disconnection rates for existing customers. We expect existing customer disconnections will reduce the number of meters on the network, and therefore the number that reach time expired replacement, fail and require replacement or are replaced through our hard to read digital metering program over the next AA period.

The reduction to the volume of meter replacements in our GSR Response is summarised in Table 1.7 below.

Table 1.7: Revised Meter Replacement volumes due to GSR

| Volumes | 2023/24 | 2024/25 | 2025/26 | 2026/27 | 2027/28 | Total |
|---|---|---|---|---|---|---|
| Annual percentage of existing customer disconnections due to GSR | 0.87% | 1.64% | 2.41% | 2.85% | 3.28% | 11.05% |
| **Domestic Meters** | | | | | | |
| Number of PMCs – Final Plan | 19,163 | 26,407 | 27,024 | 45,179 | 54,911 | **172,684** |
| Number of PMCs – Revision | (154) | (415) | (626) | (1,262) | (1,770) | **(4,226)** |
| **Number of PMCs – GSR Response** | **19,009** | **25,992** | **26,398** | **43,917** | **53,141** | **168,458** |
| **Digital Meters** | | | | | | |
| Remote Meters - HTR – Final Plan | 500 | 500 | 1,550 | 1,550 | 1,550 | **5,650** |
| Remote Meters - HTR – Revision | (4) | (8) | (37) | (44) | (51) | **(145)** |
| **Remote Meters - HTR – GSR Response** | **496** | **492** | **1,513** | **1,506** | **1,499** | **5,505** |

### 1.4.5 Augmentation

Our GSR Response includes $2 million of Augmentation capex. This is a reduction of $8 million (or 82%) compared to the $9 million included in our Final Plan.

The key drivers of the reduced augmentation capex are our lower forecast of new residential connection growth and forecast increase in disconnection rates for existing customers. These forecasts have been applied to each of our high pressure networks that were forecast to require augmentation in the next AA period to determine if under the new conditions, augmentation would still be required. While many of the planned augmentations will no longer be required in the next AA period, there are a couple which will still be required – particularly where they are also important for security of supply.

A summary of the changes to our augmentation capex in response to the GSR is provided in Table below.

Table 1.8: Revised Augmentation forecast costs in the next AA period $'000 real 2022/23

| $'000 real 2022/23 | 2023/24 | 2024/25 | 2025/26 | 2026/27 | 2027/28 | Total |
|---|---|---|---|---|---|---|
| **Augmentation Projects** | | | | | | |
| Augmentation Projects – Final Plan | 3,401 | 3,401 | - | - | 156 | **6,957** |
| Augmentation Projects – Revision | (3,401) | (3,401) | - | - | (5) | **(6,807)** |
| **Augmentation Projects – GSR Response** | **-** | **-** | **-** | **-** | **150** | **150** |
| **Network Regulator Capacity Upgrades** | | | | | | |
| Network Regulator Capacity Upgrades – Final Plan | 572 | 323 | 157 | 529 | 555 | **2,136** |
| Network Regulator Capacity Upgrades – Revision | (233) | (11) | (157) | (324) | (19) | **(743)** |
| **Network Regulator Capacity Upgrades – GSR Response** | **339** | **312** | **-** | **205** | **537** | **1,393** |

See Attachment 9.11A Addendum to Network Capacity Strategy for more information on our augmentation capex, including the approach we have taken to revise our modelling and the outcome for each augmentation project.

### 1.4.6 Telemetry

Our GSR Response includes $5 million of Telemetry capex. As noted above, our telemetry capex remains unchanged from our Final Plan, except for a change in the application of CPI. This is because the GSR does not change the integrity drivers of these programs.

### 1.4.7 Other Assets

Our GSR Response includes $32 million of other capex. Our other capex remains unchanged from our Final Plan, except for a change in the application of CPI as noted above. This is because the safety and integrity drivers for these programs do not change as a result of the GSR.

#### Hydrogen Adaptation

Our GSR Response includes our small hydrogen adaptation program proposed in our Final Plan. We consider the GSR supports this program, given its recognition of the role of renewable gas blending in meeting emission reduction targets.

The Hydrogen Adaptation Plan is required on the basis hydrogen is injected into our network, regardless of the volume. While it is a relatively small program of work, it is important we start in the next AA period to ensure our network is ready, and is not a roadblock, for hydrogen injection, with the GSR foreshadowing additional measures, including a renewable gas blending target, to be introduced in coming years.

For more information on our Hydrogen Adaptation Plan, see Attachments 9.10(1) and 9.10(2) of our Final Plan.

## 1.5 Summary

Our GSR Response sees a moderate reduction in our capex proposal for the next AA period of $53 million (or 7%). This is largely driven by lower growth capex (-$19 million), lower mains replacement capex (-$2 million) lower augmentation capex (-$8 million), other top-down reductions (-$1 million) and a change in the application of CPI (-$24 million).

This responds to the GSR policy positions and aligns with stakeholder feedback on the areas of our Final Plan there was some difficulty accepting on the basis of policy uncertainty (e.g. growth capex).

It is important to highlight that the GSR does not change our obligations to maintain a safe and reliable network, and meet the customer service expectations of our customers. Therefore, a large portion of our capex program in the next AA period, including the continuation of our low pressure mains replacement program, remains unchanged.