17 February 2017

Australian Energy Regulator
Level 35, 360 Elizabeth Street
Melbourne VIC 3000

By e-mail: VicGAAR2018-22@aer.gov.au

**Victorian Gas Access Arrangement Review- 2018-22**
**Response to Gas Distribution Business' proposals**

Origin Energy (Origin) welcomes this opportunity to comment on the proposals lodged with the Australian Energy Regulator (AER) by the three Victorian gas distribution businesses – AusNet Services (AusNet), Australian Gas Networks (AGN) and Multinet Gas (herein "the distributors") relating to their access arrangements for the period 2018-22.

In general, Origin is supportive of the distributor's proposals to reduce network tariffs in the first year of the access arrangement period (2018, in the case of AGN and AusNet) and the capital expenditure proposed for their respective mains replacement programs, noting that Energy Safe Victoria and other stakeholders (including retailers) have been presented with reasons for the mains replacement program of each distributor.

We are not convinced that a change from weighted average price cap (WAPC) to a revenue cap model proposed by Multinet is warranted, though we understand the views articulated by Multinet that this form of variation of reference tariffs would better reflect an environment of declining demand and lower connections in the Multinet network. (and the dependence on demand forecasts to support WAPC) and align the approach applied to distribution network service providers (DNSPs) in electricity.

Origin does support the trial of remotely read gas meters utilising advanced metering infrastructure put forward in Multinet proposal and a related investment being considered by AusNet.

The range of rates of return proposed by each of the distributors reflect changed market conditions since the beginning of the current access arrangement period and the extent to which the AER's *Rate of Return Guidelines* have been followed. While noting that value of imputation credits (gamma) is subject of judicial review currently, Origin supports AGN's stance of adopting parameters from the Guideline and basing cost of capital decisions on previous AER approvals, but understands each business will interpret variables according to its own independent advice and review.

We would welcome further discussion with the AER on this response. In the first instance, please contact David Calder on (03) 8665 7712.

Yours sincerely

Keith Robertson
Manager Wholesale and Retail Regulatory Policy
(02) 9503 5674– Keith.Robertson@Originenergy.com.au

## 1. Demand and customer growth forecasts

A theme across all of the distributors is the declining average consumption of gas per connection (particularly among residential customers who constitute the bulk of consumption). This has been taking place over an extended period of time and has a number of well understood drivers (weather and climatic conditions, appliance efficiency and substitution to electricity as a source of energy).

In general, we consider the demand and customer forecasts put forward in the distributors' proposals reasonable. Specific comments on forecasts of gas demand and customer numbers is set out below.

<u>AusNet</u>

Like AGN, but unlike Multinet, growth in customer numbers is likely to be consistent with the forecasts made by AusNet. Like AGN, AusNet benefits from new housing construction. Origin agrees that the growth in residential connections is likely to offset falling average consumption per customer due to climatic effects and improvements in appliance efficiency. The modest total growth figure of 0.6% in gas consumption of the period 2018-22 is realistic given this.[1]

<u>AGN</u>

Origin supports the demand and customer number forecasts set out in chapter 13 of AGN's proposal. While AGN's consultants forecast a more gradual decline in annual consumption for residential customers of 0.2% relative to AEMO's 0.7% over the 2018-22 period, we believe this figure is reasonable.

As with AusNet's distribution area, AGN is expected to connect a material number of new homes within the suburban growth corridors within its network.

<u>Multinet</u>

Origin accepts the forecast demand and customer data set out in chapter 9 of Multinet's Access Arrangement Information. Appliance efficiency, substitution and and the impact of the downward trend in effective degree days are impacting on average consumption.

## 2. Reference services and variation of reference tariffs

<u>AusNet</u>

*Haulage Reference Services*

A service similar to that proposed by Multinet's new 'addition of a service valve' ancillary service would be supported by Origin.

*Tariffs and variation of reference tariffs*

<u>AusNet</u>

Origin notes that AusNet intends to maintain its current reference tariff structure for Tariff V, M and D customers. We have no objections to this approach. In addition, Origin supports the retention of the WAPC tariff basked approach in the AusNet gas distribution network.

---

[1] AusNet Services (2016), 'Gas Access Arrangement Review 2018-22: Access Arrangement Information', page 52.

AGN

*Haulage reference services*

Origin supports the maintenance of the current reference services and ancillary services from the current to the 2018-22 access arrangement period. Again, an alternative to street disconnection similar to that proposed by Multinet would be welcome for sites with limited or no access to effect disconnection of supply.

Multinet

*Haulage reference services*

Origin supports the inclusion of “addition of a service valve” in Multinet’s list of Ancillary Reference Services. This new service will revolve issues relating to disconnection where access to a customer’s property is not possible or difficult.

*Tariffs and variation of reference tariffs*

As noted above, Origin is not convinced that a change from WAPC to a maximum revenue cap is warranted for the forthcoming access arrangement period. While we support Multinet being able to recovery its efficient costs and noting that in an environment of declining demand it is difficult to maintain a WAPC approach as effectively as might have been the case in the past, further justification for the change in approach is warranted in our view.

## 3. Forecast Capital Expenditure

AusNet

*Mains replacement*

We note that mains replacement and new connections comprise more than 60% of AusNet’s forecast capex over the period 2018-22. Origin supports the mains replacement program, similar to other distributors on safety and reliability grounds.

*Metering*

Origin is supportive of opex step changes to support digital metering of gas in the future (and discusses Multinet’s trial below).

AGN

*Mains replacement*

Consistent with the other distributors, AGN’s mains replacement program reflects efforts to upgrade existing pipeline assets to improve safety and reliability. A simple measure of calculating the cost per kilometre of forecast mains replacement over the 2018-22 period reveals a relatively high marginal cost compared with AusNet and Multinet. Origin understands however that some of this variation can be explained by mains replacement in the central business district of Melbourne.

Multinet

*Mains replacement*

While noting that the mains replacement program of all the distributors is a long term project, Multinet's proposal sees a material expansion of capital expenditure from $139.2m for the current access arrangement period to $266.9m for the period 2018-22. While this is a material increase, Origin supports the mains replacement program of each of the distributors on safety grounds, however, it would have been preferable if more of the capital could have been allocated in the current access arrangement period.

*Metering*

As indicated during our attendance at Multinet's retailer forum, we support the investigation (and associated expenditure) on a trial of remotely read gas meters utilising existing advanced meters in the United Energy electricity distribution network. Further exploitation of this infrastructure will add to the benefits and remote reading to enable faster retail transfer is an important initiative that Origin supports.

## 4. Forecast Operating Expenditure

AusNet

*Joint Marketing Initiative*

The step change due to marketing ($21.8m over five years), as with the other distributors, is a principle contributor to forecast opex of $304.7m over the period 2018-22 (up from $267.7m). Origin recommends that the effectiveness of the joint marketing initiative be reviewed at intervals and at the end of the access arrangement period to examine its effectiveness (for example, number of rebates claimed for new appliances). We are supportive of the aims of the joint marketing initiative, but are of the view that it is important that the distributors review its effectiveness and share the findings with stakeholders including the AER.

AGN

*Joint Marketing Initiative*

See comments above on the AusNet proposal.

Multinet

See comments above on the AusNet proposal.

## 5. Weighted Average Cost of Capital

Origin supports the distributors' stance (noting they are not uniform in their approach) to adopt AER recommendations and parameters contained in the Guideline where possible, while leaving matters of contention to be determined independently as required is an approach that should reduce the costs of regulatory oversight and effort for both AGN and the AER in reaching a final determination on the access arrangement.

We acknowledge that AusNet and Multinet will also apply elements of the Guideline, but with differing sources of data than those applied by the AER.

## 6. Incentive mechanisms

Origin supports the proposal by the distributors to introduce innovation schemes as part of their incentive scheme arrangements. We endorse the recovery of any costs associated with a network innovation scheme following actual expenditure, committing the distributors to invest in projects before these are recovered from customers.

AGN's and AusNet's proposals to introduce a capital expenditure sharing scheme (CESS) is supported (with a counterbalancing performance Service Target Performance Incentive Scheme) as this will align capex expenditure incentives with the regulation of electricity distribution networks. Origin also supports the retention of the Efficiency Benefit Sharing Scheme (EBSS) applying to opex suggested by each of the distributors..

## 7. Terms and conditions

AGN's merging of its Victorian and Albury terms and conditions for access and use of its distribution network supported and will reduce administrative and legal costs for both distributors and retailers over the forthcoming access arrangement period.

We agree with the distributors' views that terms and conditions have evolved over the previous access arrangement periods and support their continued engagement and willingness to negotiate minor elements of these as required.