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5 October 2022

Mr Arek Gulbenkogl
General Manager Network Expenditure
Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

Submitted via email to: VICGAAR2023@aer.gov.au

Dear Mr Gulbenkogl,

Re: Victorian gas distributors access arrangements proposals 2023-28

In July 2022, the Victorian gas distributors' submitted their access arrangement proposals for the period 1 July 2023 to 30 June 2028. Red Energy and Lumo Energy (Red and Lumo) welcome the opportunity to comment on the Victorian gas distributors' gas access arrangement proposals that have been lodged with the Australian Energy Regulator (AER) for approval.

This access arrangement approval process is occurring following the Victorian Government's release of its Gas Substitution Roadmap (Roadmap). As a result, the access arrangement proposals and subsequent addendums have been submitted during a period where there is risk of downward pressure on gas demand. This creates a consequential potential for asset stranding and pricing risks for both current and future gas consumers. Despite this, potential for a material decline in long term gas demand and the threat of asset stranding risk, the AER has indicated that the regulated Victorian gas monopoly businesses will continue to recover their regulated revenues. The rationale provided by the AER is that the risks associated with changes in environmental government policies like the Roadmap have not been captured in their Weighted Average Cost of Capital (WACC).

Red and Lumo are focused on the impact of this access arrangement decision on consumers. As such, the AER must ensure that it strikes a fair and reasonable balance between the consumer outcome and the costs associated with making sure the Victorian gas distributors recover their regulated revenues. In this regard, we expect that AER will ensure that the Victorian gas distributors provide compelling evidence to justify any proposals where consumers pay for this risk given the potential impact on consumers. Below, we expand on this and comment on other matters.

Accelerated depreciation

The Victorian gas distributors have proposed accelerated depreciation in an attempt to ensure a fair allocation of asset stranding risk between current and future gas consumers. Red and Lumo strongly object to the Victorian gas distributors' proposals for accelerated depreciation allowances.

In principle, we have no objections to the use of accelerated depreciation as a policy mechanism to ensure a fair allocation of asset stranding risk between current and future gas consumers. Nevertheless, as we have argued throughout the consultation process, it is important for any accelerated depreciation proposal to align with other aspects of the regulatory submission. In this regard, it is irreconcilable with the Victorian gas distributors' proposals to include capital expenditure in their regulatory submissions with any proposal for accelerated depreciation. To put it simply, it makes no sense to argue there is a need to spend money on the network for both growth and safety when claiming accelerated depreciation to mitigate asset stranding risk. This is contradictory and therefore unclear how they can both be included together in any regulatory proposal.

Demand forecasts

Red and Lumo do not support the Victorian gas distributors' revised demand forecasts as submitted in their addendum. The Victorian gas distributors argue that in response to the Roadmap that there will be a reduction in demand over the next regulatory period with a price impact (after inflation) relative to the June 2022 proposals of about +5-10%. In particular, they argue that the:

- Victorian Energy Upgrades (VEU) scheme will include new incentives for electrification and remove incentives for gas appliances from 2023
- Victorian Planning Provisions will remove the requirement for new housing developments to be connected to gas
- Introduction of a 7-star standard for new homes will provide incentives to use electricity over gas.

While acknowledging that there will be a reduction in demand as a result of these changes, based on the evidence that was submitted during the Victorian Gas Distributors' consultation process, there are serious questions about whether the decline in gas demand will be as large as projected by the Victorian gas distributors. Hence, we recommend that the AER only accept the demand forecasts if there is further credible evidence to support them.

Price path

Red and Lumo do not support the Victorian gas distributor's current price path. The Victorian gas distributors price proposals seek to transfer the upfront real price reductions from the beginning of the new access arrangement period allowing consumers to benefit from the price decreases as soon as possible. The lower network costs have the potential to be passed through to consumers in the first year of the new access arrangement for the benefit of all consumers.

In contrast, we would prefer that the Victorian gas distributors change this approach and try to smooth the price path over the entire regulatory period. If this means reducing the size of the price cuts in the first year of the access arrangement, then we would be comfortable with this approach. In our view, it is important for the Victorian gas distributors to deliver a smooth price path that includes price cuts over the entire regulatory period for the benefit of consumers. This is because price spikes in the later part of the access arrangement can be serious leading to:

- increased complaints regarding the affordability of bills
- an increase in the level of disconnections
- adverse impacts on the consumers who are already struggling with energy costs
- incorrect price signals being sent to consumers to use energy inefficiently.

Priority Service Program

Red and Lumo do not support the Priority Service Program proposals that have been submitted by the Victorian gas distributors in their access arrangement proposals.

The Victorian gas distributors have submitted a Priority Service Program as part of their regulatory proposals to better support the Victorian gas customers facing vulnerable circumstances. The Priority Service Program program initiatives include basic things like a dedicated customer support team, check-ins and additional support during outages, gas appliance safety checks and meter self reads.

In our view, compensating the Victorian gas distributors for these activities is inefficient and unnecessary. This is because we consider the Victorian Gas distributors should be undertaking these activities as part of business as usual. For example, meter self reads have been occurring for some time hence it is not clear to us that more money should be spent on this activity. Furthermore, additional support during outages have always occurred for customers that have sought assistance.



In addition, retailers already have customer hardship programs in place that specifically target vulnerable customers. We spend considerable resources on these programs to ensure that vulnerable customers get the support they require from their retailers through the payment difficulty framework. As customer facing entities with significant experience in dealing with these matters it is not clear to us that the Priority Service Program program will add any value in this regard.

Finally, while the AER has approved a Priority Service Program in South Australia for AGN we have unfortunately yet to see any benefits for consumers from this program. In the absence of any evidence from AGN operating this in SA, we strongly recommend the AER refrain from approving the funding for a Priority Service Program for the Victorian gas distributors.

About Red and Lumo

We are 100% Australian owned subsidiaries of Snowy Hydro Limited. Collectively, we retail gas and electricity in Victoria, New South Wales, Queensland, South Australia and in the ACT to over 1.2 million customers.

Red and Lumo thank the AER for the opportunity to respond to this consultation. Should you wish to discuss aspects or have any further enquiries regarding this submission, please call Con Noutso, Regulatory Manager on 0481 013 988.

Yours sincerely

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