Jemena Gas Networks (NSW) Ltd

JGN 2014-15 within-year tariff variation notice

2014-15 reference tariffs

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1. INTRODUCTION

1.1 PURPOSE

Jemena Gas Networks (NSW) Limited's (**JGN**) 2014-15 reference tariffs, approved by the Australian Energy Regulator (**AER**) on 26 May 2014, include an estimated carbon cost of $9.43M. However, the repeal of the Clean Energy Act 2011 (Cth) (**Clean Energy Act**) on 17 July 2014 removed our carbon liabilities, effective from 1 July 2014.[1]

To give timely effect to returning cost-savings back to customers, JGN adjusted its reference tariffs to cease collecting the majority of carbon-related revenue from:

- industrial customers from 1 July 2014[2]
- residential and commercial customers from 1 August 2014.[3]

JGN now submits to the AER this within-year tariff variation notice (**TVN**) to give formal effect under our access arrangement[4] (**AA**) to the reductions in 2014-15 reference tariffs arising from this carbon-related adjustment.

JGN hereby provides:

- its within-year variation notice for 2014-15 reference tariffs in accordance with AA clause 3.4(b)(ii)
- its cost pass-through event application in accordance with AA clause 3.4(f) for within-year carbon pass-through (**CPT**) due to a 2014 Carbon Pollution Reduction Scheme (**CPRS**) event (being the repeal of the Clean Energy Act). In accordance with clause 3.4(e)(i) of JGN's AA, this event was notified to the AER by letter dated 5 August 2014, within the 90 business day period required under the AA,

Other than the variation to 2014-15 reference tariffs arising from the CPRS event referred to above, no other variation is proposed in this submission.

The variation notice:

- demonstrates JGN's 2014-15 CPT cost savings are equivalent to a $0.110/GJ throughput charge to be removed from its haulage reference tariffs
- provides JGN's proposed reference tariff schedule applicable from the effective dates in the 2014-15 financial year that ends 30 June 2015
- outlines how residual revenue collected under previous legislation is proposed to be returned to customers in 2015-16.

1 See *Clean Energy Legislation (Carbon Tax Repeal) Act 2014* (Cth).

2 Industrial ('demand') customers make up around approximately 60% of JGN's consumption.

3 Residential and commercial ('volume') customers make up around 40% of JGN's consumption.

4 The Access Arrangement (post mine subsidence): JGN's NSW gas distribution networks, 1 July 2010 – 30 June 2015, published in September 2011.

1.2 SUBMISSION STRUCTURE AND COMPLIANCE

JGN has structured this submission to demonstrate compliance with relevant requirements in clause 3 of our AA:

- section 2—variation notice (clause 3.4(c))
- section 3— haulage reference tariff annual tariff variation mechanism (clause 3.5A)
- section 4—pass-through event notification, application, tariff adjustments and returning residual cost savings (clauses 3.4(e), 3.4(f)(i) and 3.5C).

1.2.1 SUBMISSION VALUES AND TERMINOLOGY

This submission employs the following standards:

- unless otherwise indicated, all prices are expressed in $2015.
- for the purpose of relevant clauses and formulae in JGN's AA as applicable to this within-year TVN:
  - *financial year t* is the 2014–15 financial year ending on 30 June 2015
  - *financial year t-1* is the 2013–14 financial year ending on 30 June 2014
  - *financial year t-2* is the 2012–13 financial year ending on 30 June 2013
- a reference to a clause is a reference to a clause of the AA
- a reference to a section is a reference to a section of this submission.

1.3 TARIFF CLASSES

JGN's approved tariff classes for all reference services are set out in Table 1–1 and Table 1–2. These are also described in schedule 2 of our AA.

Table 1–1: JGN's Demand tariff classes

Tariff class	Tariff class
Demand capacity (**DC**) 1	DCFR 5
DC 2	DCFR 6
DC 3	DCFR 7
DC 4	DCFR 8
DC 5	DCFR 9
DC 6	DCFR 10
DC 7	DCFR 11
DC 8	Demand major end-customer throughput (**DMT**) 1
DC 9	DMT 2

Tariff class	Tariff class
DC 10	DMT 3
DC 11	DMT 4
DC country	DMT 5
Demand throughput (**DT**)	Demand major end-customer throughput—1st response (**DMTFR**) 1
Demand capacity—1st response (**DCFR**) 1	DMTFR 2
DCFR 2	DMTFR 3
DCFR 3	DMTFR 4
DCFR 4	DMTFR 5

Table 1–2: JGN’s Volume tariff classes

Tariff class
Volume coastal
Volume country

2. VARIATION NOTICE

This submission constitutes JGN's variation notice for the purpose of clause 3.4(b)(ii) of the AA.[5] This section sets out how JGN has complied with each of the variation notice requirements set out in clause 3.4(c) of the AA.

2.1 EFFECTIVE DATE OF VARIATION

The effective date of variation for JGN's 2014–15 reference tariffs, for the purpose of clause 3.4(c)(i) of the AA, is:

- 1 July 2014 for demand tariff classes
- 1 August 2014 for volume tariff classes.[6]

2.2 COMPLIANCE WITH ANNUAL TARIFF VARIATION MECHANISM

For the purpose of clause 3.4(c)(ii), JGN's compliance with the annual tariff variation mechanism is described in section 3 of this submission.

2.3 GAS QUANTITY INPUTS

Clause 3.4(c)(iii) of the AA requires JGN to provide an officer statement to support the gas quantity inputs in the tariff variation formula. JGN provided a statement of gas quantity inputs with its 2014-15 annual TVN submitted on 15 April 2014.[7] Gas quantity inputs do not impact this within-year TVN.

[5] Clause 3.4(b)(ii) of JGN's AA provides for Variation of a Reference Tariff within a Financial Year (as that term is defined in the AA).

[6] These effective dates are the result of the retrospective nature of the repeal of the Clean Energy Act and constructive engagement with the AER and retailers to meet a set of objectives (refer section 4.3.2), including returning cost savings to customers as early as practicable on a voluntary basis, in advance of the formal tariff variation process under the AA. JGN confirms that this approach is as discussed and settled with the AER, and this within-year TVN is submitted following the AER confirming its preferred process via email on 24 October 2014.

[7] JGN, Tariff Variation Notice, 2014-15 reference tariffs, 15 April 2014.

3. HAULAGE REFERENCE TARIFF ANNUAL TARIFF VARIATION MECHANISM

In the context of the within-year variation described in this TVN, this section explains how JGN has complied with the reference tariff variation mechanism for haulage reference tariffs described in clause 3.5A of the AA, and sets out its proposed 2014–15 haulage reference tariffs to apply from the effective dates referred to in section 2 of this submission.

3.1 VARIATION MECHANISMS

JGN's annual tariff variation mechanism as defined in clause 3.5A includes two formulaic tests:

- weighted average price cap
- side constraint.

JGN's proposed reference tariffs remain consistent with these tests and the mathematical proof in the 2014-15 annual TVN still applies. This is because this calculation excludes any cost pass-through adjustments subsequently applied to the 2013–14 charge components or the charge components proposed in the 2014–15 annual TVN.

3.2 PROPOSED 2014–15 HAULAGE REFERENCE TARIFFS

JGN's proposed revised 2014–15 haulage reference tariffs (as adjusted to include the pass-through savings associated with this CPRS event) are set out in its proposed 2014–15 reference tariff schedule at **Attachment** 1.

4. PASS-THROUGH EVENT APPLICATION

4.1 TARIFF ADJUSTMENTS AND PASS-THROUGH EVENTS

This section sets out the cost pass-through applicable to this within-year TVN. This notice only applies a CPRS event to vary 2014-15 reference tariffs from the effective dates outlined in section 2.1.

4.2 CARBON POLLUTION REDUCTION SCHEME

4.2.1 NOTIFICATION OF EVENT

Clause 3.4(e)(i) of the AA requires JGN to advise the AER of a cost pass-through event within 90 Business Days of becoming aware of the event. As noted previously, JGN provided notification as part of its letter to the AER on 5 August 2014.[8] The date on which the cost pass-through event occurred, via the repeal of the Clean Energy Act, was 17 July 2014.

4.2.2 COMPLIANCE WITH APPLICATION REQUIREMENT

Clause 3.4(f)(ii) sets out the requirements for a CPRS pass-through event application. **Table 4–1** explains how the various requirements specified in clause 3.4(f)(ii) are addressed for CPRS pass-through event in this document.

Table 4–1: Elements of CPRS pass-through event application

Clause	Description	Relevant submission references
3.4(f)(ii) A—The details of the Cost Pass-Through Event	A CPRS Event (as defined in clause 3.5C) has occurred because the Australian Government repealed the Clean Energy Act on 17 July 2014. Clause 3.5(a) explicitly recognises that variations may result in both increases and decreases in reference tariffs. In the present case, the CPRS Event resulted in a reduction in JGN's costs, due to the removal of a legislated scheme which places a cost on carbon or carbon-containing emissions.	Section 4.2.2
3.4(f)(ii)B—The date on which the Cost Pass-Through Event occurred	17 July 2014 (with an effective date of 1 July 2014)	Section 4.2.2
3.4(f)(ii)C—The amount the Service Provider proposes to pass-through in relation to the Cost Pass-Through Event	A refund to customers of approximately $8.793M	Section 4.2.3

[8] Letter from Robert McMillan to Chris Pattas, AER General Manager, Network Operations and Development, *Jemena Gas Networks – Removing carbon from 2014-15 Reference Tariffs*, 5 August 2014.

Clause	Description	Relevant submission references
3.4(f)(ii)D(i)—Evidence of the actual and likely increase or decrease in costs arising from the Cost Pass-Through Event	The evidence for this calculation is provided in section 4.2.3.	Section 4.2.3
3.4(f)(ii)D(ii)—Evidence that such costs occur solely as a consequence of the Cost Pass-Through Event	The defined CPT costs are not applicable to other elements of JGN's reference or non-reference services.	
3.4(f)(ii)E—Such other information as may be required under any relevant regulatory information notice	No relevant regulatory information notice has been provided.	
3.4(f)(iii)C—The efficiency of the Service Provider's decisions and actions in relation to the risk of the Cost Pass Through Event, including whether the provider has failed to take any action that could reasonably be taken in respect of that event and whether the Service Provider has taken or omitted to take any action where such action or omission has increased the magnitude of the amount in respect of the event	As the legislative acts which resulted in the repeal of the Clean Energy Act did not take place until some time after 1 July 2014, JGN had already commenced collecting revenue to recover its expected carbon liabilities in the 2014-15 year. Upon repeal, JGN sought to constructively engage with stakeholders, including the AER and retailers, to complete an acceptable and administratively simple approach to pass cost-savings back to customers.	Section 4.3
3.4(f)(iii)D—The time cost of money based on the WACC for the Service Provider	There is no time cost of money for CPT costs for this within-year 2014–15 pass-through. This is because JGN's previously approved approach aligns all material CPT costs with the cost recovery. Please note that section 4.3 outlines that time cost of money will be applied to the cost-savings returned to customers in 2015-16 reference tariffs (which does not form part of this TVN).	Section 4.3
3.4(f)(iii)E—The need to ensure the Service Provider only recovers any actual or likely increment in costs to the extent that such increment is solely as a consequence of a Cost Pass Through Event	The methodology JGN has used to calculate its CPT costs in its 2014-15 annual TVN is being unwound by this within year TVN, thereby ensuring the cost-savings relate directly to the CPRS event	Section 4.2.3
3.4(f)(iii)F—Whether the costs of the Cost Pass Through Event have already been factored into the calculation of the Service Provider's annual revenue requirement	The cost-savings of this CPRS pass-through event have not already been factored into JGN's annual revenue requirement.	

4.2.3 DETAILS OF THE CPRS PASS-THROUGH EVENT

4.2.3.1 The CPRS event

Clause 3.5C(b) defines CPRS Event to mean:

> *… the occurrence of an event whereby the Service Provider incurs costs as a result of the introduction and operation of a CPRS or similar legislated scheme which places a cost on carbon or carbon-containing emissions.*

The CPRS Event that is the subject of this application is the Australian Government's repeal of the Clean Energy Act on 17 July 2014. This was effected via the *Clean Energy Legislation (Carbon Tax Repeal) Act 2014* (Cth) (**Repeal Act**), which repealed the Clean Energy Act effective from 1 July 2014.

The AER had previously approved the commencement of the Clean Energy Act as a CPRS Event for JGN as part of JGN's 2012-13, 2013-14 and 2014-15 annual TVNs. Given the back-dating of the Clean Energy Act repeal so that it was effective from the commencement of the 2014-15 financial year, this within-year TVN seeks to unwind the majority of the 2014-15 CPRS pass-through, with a residual amount to be removed via an adjustment to 2015-16 revenues (refer section 4.3).

4.2.3.2 JGN has ceased to be a liable entity

The Repeal Act means various obligations in the Clean Energy Act and the Clean Energy Legislative Package cease to apply to JGN effective from 1 July 2014. In particular, JGN ceased to be a liable entity under those laws from 1 July 2014, and therefore no longer incurs costs of the nature described previously in the annual TVNs from 2012-13 to 2014-15.

Consequently, JGN has determined the amount in respect of its costs savings relating to the CPRS event for the 2014-15 year, which it proposes to pass-through in revised haulage reference tariffs, as outlined in this TVN. For the avoidance of doubt, this amount constitutes the voluntary reduction already in place—which JGN has applied to demand customers from 1 July 2014, and volume customers from 1 August 2014—as applicable from those effective dates until the end of the 2014-15 financial year.

4.2.4 ESTIMATED FINANCIAL EFFECT

JGN's 2014-15 annual TVN outlines our approach to the CPRS event when this was a pass-through of additional JGN costs. JGN estimated the financial impact to be $9,493,101[9]. This is made up of three elements including gas distribution fugitive emissions, gas transmission fugitive emissions and operating costs.

The actual cost to JGN of gas distribution fugitive emissions was set up to be recovered as a throughput charge of $0.110/GJ ($2015) to ensure JGN's carbon price liability for gas distribution fugitive emissions is directly proportional to the costs charged to JGN's gas distribution customers. The calculation is included in the 2014-15 TVN. This shows that the gas distribution fugitive emissions estimate of $9,370,405 was to be recovered by the $0.110/GJ ($2015) throughput charge.[10]

This within-year TVN relates only to stopping this charge from the effective dates in section 2.1. This means that the pass through will provide a refund to customers of approximately $8.793M in 2014-15. JGN considers that this event meets the administrative threshold in clause 3.4(f)(iv) of the AA.

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9 This is an estimate only as it is based on forecast sales in 2014-15.

10 This charge was not applied to transportation services to delivery points that are connected to a section of the network that is designed to operate at more than 1050kPa.

4.3 PASSING BACK THE RESIDUAL COST SAVINGS

The effect of this within-year TVN means that the following have been, or will still be, recovered by JGN during 2014-15:

- an estimated $577,000 (to be adjusted for the time value of money), representing the 1 July 2014 to 31 July 2014 revenue collected from our volume customers from the throughput charge for gas distribution fugitive emissions[11]
- gas transmission fugitive emissions and operating costs (totalling $122,696).[12]

We will return this revenue to customers (including an allowance for time value of money) in 2015-16 reference tariffs. We will do this by including in our revised AA proposal for the 2015-20 regulatory period, which JGN will submit to the AER on or prior to 27 February 2015):

1. a calculation of our actual revenue recovered from volume customers distribution fugitive emissions throughput charge between 1 July 2014 to 31 July 2014—and then adding this to the transmission fugitive emissions and operating costs (currently estimated at $0.7M in total)
2. a 'Clean Energy Act repeal settlement' tariff component for the Volume Individual customer type, with a tariff component level derived for 2015-16 to return the carbon cost over-recoveries in 1 above, less the amount of a retailer of last resort pass through of $14,586[13], to these customers
3. a 'Clean Energy Act repeal settlement' tariff component level for the Volume Individual customer type from 2016-17, to be set at '$0.00'. JGN proposes to remove this tariff component entirely from published network tariff schedules from 2016-17 onwards.

4.3.1 VOLUNTARY REDUCTIONS

JGN's AA provides the legal framework by which we can adjust our tariffs. This includes specific timeframes and processes. However, to give timely effect to returning cost-savings back to customers, JGN voluntarily ceased collecting the $0.110/GJ ($2015) throughput charge from our:

- customers on demand tariffs from 1 July 2014
- customers on volume tariffs from 1 August 2014.

JGN's tariffs, prior to the voluntary reductions that were approved by the AER on 26 May 2014, can be viewed in the network tariff schedule here: http://www.aer.gov.au/node/24821. This within year TVN only impacts the volume throughput rate in section (h) and Clean Energy Act (distribution component) Charge for Demand customers in section (k) of that tariff schedule. Both have the $0.110/GJ charge removed. The updated tariff schedule is at **Attachment 1**.

Attachment 2 provides a copy of JGN's notification to retailers of the voluntary reductions on 25 July 2014.

This within-year TVN would give formal effect to these voluntary reductions and would not result in a change to tariffs customers have faced since the effective dates noted above.

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11 This will not form part of this TVN due to the timing of the Repeal Act being within July 2014 and to allow a simple and accurate refund to customers.

12 This will not form part of this TVN as the gas transmission fugitive emissions charge and operating costs were applied to all of JGN's haulage reference tariffs and the accuracy of returning the relatively small amount would be impacted by tariff rounding.

13 The ROLR event relates to a cost recovery application by AGL for which the AER made a determination on 22 August 2014. The amount paid by JGN is taken to be an approved cost pass through under section 167 of the NERL.

Supporting this approach, we acknowledge and welcome the AER advice[14] that it would consider any voluntary reductions in assessing pass through applications. In particular that the AER has determined that:

> *Gas network operators may immediately remove the carbon cost component from reference tariffs (prices). This would mean the operators would choose to recover prices less than the reference tariffs approved by the AER. Moreover, the AER will take into account any voluntary under recovery by pipeline operators in respect of carbon costs when assessing negative pass through application.*

4.3.2 RATIONALE FOR OUR APPROACH.

JGN took this approach, consistent with consultation with stakeholders and the AER, because it:

- returned the majority of cost savings to customers as quickly as possible
- uses a methodology that does not require estimates
- provided transparency to customers and stakeholders
- supports price stability by only having one additional change to our reference tariffs in 2014-15
- meets stakeholder needs.

Our approach returns the majority ($8.793M out of $9.493M) of cost savings immediately. As outlined in section 4.3 above, the remaining $0.7M relates to volume market gas distribution fugitive emissions in July 2014 as well as operating costs and transmission fugitive emissions. Returning these cost savings within 2014-15 would have meant either:

- two changes to our reference tariffs; and/or
- the use of demand estimates to calculate the July recovery from volume customers (with a subsequent need for a wash-up).

This would not have been in customers' or stakeholders' interests.

We consider this is consistent with finding an administratively simple outcome that meets our requirements to comply with the Repeal Act and, most importantly, pass on the savings to customers as soon as practicable.[15]

[14] Email from Craig Madden dated 24 July 2014.

[15] As supported by the AER—see email from Craig Madden to Robert McMillan dated 24 July 2014.