RESPONSE TO AER DRAFT DECISION & APA VICTORIAN TRANSMISSION SYSTEM (VTS) REVISED 2023-27 ACCESS ARRANGEMENT PROPOSAL

Prepared for

Brotherhood of St Laurence
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EXECUTIVE SUMMARY

OVERARCHING OBJECTIVES THAT SHOULD FRAME APA'S AA

In order for APA's Revised AA be able to be seen to be consistent with the National Gas Objective, it needs to at least meet these three key objectives:

- Objective#1 - Keeping gas prices as low as possible for today's household and small business consumers.
- Objective #2: the costs and risks of transitioning to lower emissions energy sources must be efficient and carefully managed
- Objective #3: sufficient supporting information must be provided to enable AER to assess whether proposal is capable of acceptance under NGR.

HOW APA'S REVISED AA PROPOSAL (RAP) ADDRESSES BSL'S KEY FOCUS AREAS (AS OUTLINED IN INITIAL REPORT)

Key Focus Area	Elements of APA's Revised AA Proposal	Does it address BSL's Position?
Consumer affordability	- Adopt demand forecasts based on a *Delayed Step Change* scenario - AEMO *Progressive Change* scenario for the five years (the period of this AA) then shift to a AEMO *Step Change* scenario in subsequent AA period - Restricting asset lives to 30 years, in an accelerated depreciation proposal - Pursue an alternative SWP expansion, commenced in the current period - Forecast replacement capex is still at high levels - $112m - $332m in forecast capex for the AA period - Total revenue still high - $695.98m	No
Security of supply and of VTS, but not at any price	- Continued with the WORM project but even higher costs - SWP expansion project – 2nd compressor at Winchelsea instead - Significant increase in Security of Critical Infrastructure capex and opex	No

HOW APA'S REVISED AA PROPOSAL (RAP) ADDRESSES BSL'S KEY FOCUS AREAS (CONT'D)

Key Focus Area	What is Contained in Revised Access Arrangement Proposal	Does it address BSL's Position?
Accelerated depreciation as a measure to address uncertainty	- APA doesn't appear to have properly addressed the criteria AER outlined in DD for justifying accelerated depreciation - Other factors are already placing stress on consumers' capacity to afford energy - Still high levels of replacement capex being proposed	No
Tariff levels and tariff path stability	- Composite tariff is 13.9% higher than the AER's DD tariff and 12.3% higher than the original AA proposal tariff - Significant increase in total revenue allowance (relative to DD allowance) – even without taking into account the effect of higher inflation and interest rates - High levels of replacement and expansion capex still being proposed - No consideration of changes to tariff structure	No
Investment in hydrogen readiness costs	- Reduced level of expenditure spread over two AA periods and intends to depreciate the capex over the same life as pipeline asset class - Still yet to address concerns about whether the NGR allows it to be included in the capital base - Still has not addressed consumer input, that hydrogen expenditure is not supported	No

HOW APA'S REVISED AA PROPOSAL ADDRESSES BSL'S KEY FOCUS AREAS (CONT'D)

Key Focus Area	What is Contained in Revised AA Proposal	Does it address BSL's Position?
Prudency & Efficiency of opex and capex	- Further information provided on certain expenditure items to substantiate prudency and efficiency which appear capable of acceptance but not on all matters - AER still needs to assess efficiency and prudency of actual capex in 2018-22 - AER will need to review SoCI related capex and opex forecasts given confidentiality	Not yet
Adequacy of supporting information	- Will require AER and its consultants to assess adequacy of supporting information for SoCI forecast capex because of confidentiality issues - Adequacy of evidence for opex step changes are not accepted - Evidence for accelerated depreciation does not address consumer concerns	Not yet
Future of gas	- Continuing with hydrogen study but reducing the total expenditure and spreading it over two AA periods instead of one period. Also, depreciate the cost over the life of pipelines - Introduce accelerated depreciation	No

ARE KEY ELEMENTS OF REVISED AA CAPABLE OF ACCEPTANCE BY AER?

Slides 7-10 summarise how each of the key elements in the Revised AA align with BSL's overarching objectives and whether they are capable of acceptance by AER, based on the information submitted by APA (and refer to the pages in this report where further commentary is provided in each element).

Element of Revised AA	APA's Position	Materiality	Objective Alignment?	Capable of Acceptance?	Pages of Report
Total Revenue	APA is seeking $695.98m over the AA period (although this doesn't use up to date inflation figures).	H			12
Tariff Structure	Reference Tariff Structure remains unaltered from initial AA proposal	M			34-35
Tariff path	Unclear what has been proposed given that APA has not changed its inflation assumption and X factor needs re-setting	M			34-35
Fixed Principles	Removal of Fixed Principle to ensure SWP & WORM capex is not subject to capital redundancy provisions	L			33

ARE KEY FEATURES OF REVISED AA CAPABLE OF ACCEPTANCE BY AER?

Element of Revised AA	APA's Position	Materiality	Objective Alignment?	Capable of Acceptance?	See Pages
Depreciation & Asset Lives	- Continuing to cap maximum asset lives (to 30yrs) to accelerate depreciation of assets	H			29-32
Depreciation & Asset Lives	- Maintained a new asset class for inspections (10 yrs) - Hydrogen study capex is now depreciated over the same life as pipelines (30 yrs) - Unclear if there are separate asset classes for WORM and SWP - Unclear if it has split "other" asset class into "short life" (5yrs) and "long life" (15yrs)	H			33
Opening Capital Base (OCB)	- APA adopts AER endorsed methodology to set OCB although the values used in methodology differ from AER's DD values - Actual capex needs further substantiation	M			14-17
Rule 80 Applications	- No longer pursuing Rule 80 applications for capex to support other gas supply projects not yet at FID but want to maintain a cost pass through tariff variation mechanism	M			35

ARE KEY FEATURES OF REVISED AA CAPABLE OF ACCEPTANCE BY AER?

Element of Revised AA	APA's Position	Materiality	Objective Alignment?	Capable of Acceptance?	See Pages
Hydrogen studies capex	- Spread capex for forecast hydrogen safety & integrity testing over 2 AA periods	M	👎	👎	24-25
Expansion capex	- Reduced capex associated with SWP – 2nd Winchelsea Compressor but yet to be justified - Still significant level of capex being proposed	H	👉	👉	16-20
WORM Capex	- Continue with the WORM project capex but further increase in total capex	H	👉	👉	16-17
Replacement Capex	- Level of forecast Replacement Capex is still high	H	👉	👉	21-22
SoCI Capex	- Significant increase in forecast Security of Critical Infrastructure capex and opex program	M	👉	👉	25
Forecast Opex	- Maintained most of the items disallowed by the AER in the DD	H	👉	👉	26-28

ARE KEY FEATURES OF REVISED AA CAPABLE OF ACCEPTANCE BY AER?

Element of Revised AA	APA's Position	Materiality	Objective Alignment?	Capable of Acceptance?	See Pages
Actual Capex	- Total actual capex will increase even further to $332m because of: a. increases in the level of replacement capex b. cost overruns with the WORM project c. timing of expenditure for the 2nd Winchelsea compressor	H			14-15
Overheads capex	- Maintained prior position but provided more clarity	M			30
Carbon offset opex	- Maintained its position from original AA proposal to include an allowance for carbon offsets	M			28

DETAILED COMMENTS ON KEY ELEMENTS OF APA'S REVISED AA PROPOSAL

TARIFF IMPACTS AS A RESULT OF PROPOSED BUILDING BLOCKS

- The key changes in the RAP relative to the current AA are as follows:

Building Block	Change	Impact
Actual capex for 2018-22 ($332.1m) vs AER approved forecast	+$109.4m	45.10% ↑
Forecast capex for 2023-27 ($279.6m) vs actual capex	+$52.5m	15.81% ↑
Forecast opex for 2023-27 ($186.4m) vs actual & estimted opex	+$45.3m	32.10% ↑
Depreciation (2018-22 vs forecast)	+$93.43m	44.01% ↑
Rate of Return (allowed in 2018-23 vs proposed)*	-0.85%	14.8% ↓
*APA's RAP rate of return has not been updated		

- This results in significant increases to system wide tariff impacts (nominal impact on composite tariff). RAP composite tariff is 13.9% higher than the AER's DD tariff and 12.3% higher than the initial AA proposal tariff (when even based on the initial AA Proposal, the 2027 tariff was already going to be 46.9% higher than 2018 tariff).

COMMENTS ON KEY ELEMENTS OF RAP

The following slides comment on each of the key features of APA's revised AA Proposal (RAP) having regard to:

- Compliance with the requirements of the NGL and NGR
- Consistency with BSL's position on each of BSL's key focus areas
- Consistency with the key objectives

Our comments are based on the information submitted by APA to the AER in support of the RAP and which has been made publicly available.

In each slide, we have adopted the following legend as our comment:

-  - consistent with key objectives
-  - further work or analysis required before we could recommend that BSL could accept that it is consistent with the key objectives
-  - not capable of acceptance based on information provided by APA

Where relevant we have also commented on the AER's reasoning in the Draft Decision

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Actual Capex 2018-22	**AER DD** Even though, at the time of the DD, APA was expected to have incurred $32.6m more in capex in 2018-22 than the $263.6m of capex approved by the AER in the current AA (as forecast capex) and APA had not undertaken a significant number of the projects that were included in that AER approved forecast, the AER's DD focused only on areas where there were significant overspends between the allowance and the expected/actual expenditure - mostly in replacement and non-system categories. The AER did not appear to revisit its assessment of each specific item of expenditure. The AER DD approved $326.4m ($105.5 million ($2022) of total net capex for APA for the 2018–20 period as conforming capex and $220.9m as placeholder capex for 2021-22) subject to the following: - APA providing information regarding the efficiency of its proposed expenditure for the 2nd Winchelsea compressor) – $39.8m - APA providing information regarding corporate shared assets and network overheads applied for 2018–22 **APA's RAP** 1. APA's RAP expects that total actual capex will increase even further to $332m because of: a. increases in the level of replacement capex b. cost overruns with the WORM project c. timing of expenditure for the 2nd Winchelsea compressor 2. APA does not appear to have provided further information beyond the business case submitted earlier in 2022 regarding the efficiency and prudency of the proposed capex for the 2nd Winchelsea Compressor.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Actual Capex 2018-22 	**Comments on AER DD assessment of actual capex** The AER should undertake an assessment of each specific items of actual/estimated expenditure. This is particularly important given: - The NGR (Rule 79) requires that the AER does this; - The impact of rising energy costs on consumers' cost of living and debt levels; and - APA's latest estimate of capex for the period 2018/22 is even more than what it filed in the initial AA proposal ($332m). **Comments on APA' RAP** 1. APA's RAP expects that total actual capex will increase to $332m because of a number of factors: a. Increases in the level of replacement capex b. cost overruns with the WORM project c. timing of expenditure for the 2nd Winchelsea compressor 2. APA has not provided further information to address the areas of concern identified in response to the initial proposal: - The reasons for undertaking the Dandenong office and storage project (when it wasn't included in the forecast approved by the AER for the current AA - Lack of information about risk assessments undertaken for projects that have been deferred or brought forward - Lack of information to explain the drivers for increases in capex for all capex categories 3. It is difficult to assess the efficiency and prudency of the expenditure for the 2nd Winchelsea Compressor as no further information has been provided by APA beyond the business case submitted earlier in 2022.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
WORM Pipeline project	**AER DD** The AER determined that the WORM project will deliver ongoing benefits to consumers in maintaining reliability and security of supply and therefore in the DD, the AER includes both capital and operating expenditure for its completion and ongoing operation ($49.0 million of forecast forecast capex for 2023, $144.8 million of capex in the final two years of the current AA period). **APA's RAP** Revised capital expenditure for the WORM increased a further 17% ($31.7m) to $216.7 million (from $185m). $156.2m of this total incurred in current AA period which is a 15% increase on the amount that was proposed in the original AA proposal. The balance of $60.5m is proposed to be incurred as forecast capex in 2023-27. This amount is a 23% increase in what was proposed in the original AA proposal. APA claim that the increase in costs between the original AA proposal and the RAP has been as a result of increases in construction costs for trenching, mitigating rock risk, welding costs, street works, facilities construction, construction supervision, Department of Transport requirements and diesel costs. The total capex for the WORM is also justified by APA on the following grounds: - It will save $12.4m in forecast capex for replacement projects (BC203, 204, 242, 260 and 267); and - It is now an even more critical investment to manage the risk of pending supply outages particularly with AEMO issuing a threat to system security in direct response to depletion of Iona storage inventory to a level threatening capacity to deliver gas from Iona.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
WORM Pipeline project	**Comments on AER DD** The AER should again re-assess the prudency and efficiency of the capex for this project given: - the significant increases in the level of capex over time (see table below); - the impact of rising energy costs on consumers' cost of living and debt levels; and - the future of gas pipeline infrastructure is being called into question. **Comments on APA's RAP** - Insufficient substantiating information has been given to explain how, in only 8 months since the original AA proposal was submitted, capex for this project has increased a further 17%. It is not sufficient to claim the increase is "due to matters beyond APA's control as they are all market based cost items". - Given the significance of the increase, the change in scope and the above factors, an updated business case should be submitted for consideration by the AER.

WORM capex total as at:	Capex ($2022)	% Change
2017/22 AA approval	$139.7m	N/A
Original AA proposal (Dec 21)	$184.5m	+32.07%
Revised AA Proposal (Aug 21)	$216.0m	+54.62%

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Capex for SWP – 2nd Winchelsea Compressor 	**AER DD and APA's RAP** AER supported AEMO's recommendation and APA's revised proposal in March 2022 that duplication of the Winchelsea compressor on the SWP ($60.1m - $37.2 million to be incurred in 2022 and $22.8 million in 2023) should be supported instead of the $90m forecast SWP expansion project initially proposed by APA given: - It will be a more timely and lower cost solution; - It will be a more appropriate response to the short term risk of supply shortfalls in Winter 2023 and also to the longer term need to ensure the VTS can adapt to changing sources of gas supply to Victoria. AER noted that its assessment of the proposed forecast capex was ongoing at the time of the DD, and that its consultants recommended only $45m be allowed as conforming capex. APA's RAP proposed $60.1 m for the 2nd compressor at Winchelsea, again split across the two AA periods.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Capex for SWP – 2nd Winchelsea Compressor (cont'd) 	**Comments on APA's RAP** - Even if the 2nd compressor at Winchelsea is the most appropriate response to the short term risk of supply shortfalls in Winter 2023 and also to the longer term need to ensure the VTS can adapt to changing sources of gas supply to Victoria it is not clear why the AER has approved an amount of $60m for this project when the AER's consultants recommends only $45m. APA does not appear to address why $45m is not the most prudent and efficient level of conforming capex for this project.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Capex for SWP – 2nd Winchelsea Compressor (cont'd) 	**Comments on APA's RAP (cont'd)** - Consideration should be given to the inclusion of the capex for Winchelsea 2nd compressor as speculative capex until it commences to be used in the provision of pipeline services. This is because there is no certainty that it will be used in the provision of services, even if there is a gas supply shortage in Winter 2023. This is because: • The purpose of the 2nd compressor at Winchelsea is to enable gas from Iona Storage to be used to support the market but there is no certainty that there will be adequate gas in storage at that time to serve the market; • There is no certainty that there will actually be a gas supply shortage from other sources. If other sources can meet demand during Winter 2023 without the need to access Iona storage gas, then the capital expenditure for the compressor would have been unnecessary. - There should therefore be an allowance for inclusion of this in the speculative investment account but also the inclusion of trigger event that allows for the capex associated with the compressor to be rolled into the capital base at the time that the compressor is required to be used to provide services to meet demand. The trigger event should also allow for the forecast opex to be increased by the amount forecast to run the compressor (ie $250k pa) from the point in time that the compressor commences to provide services to meet demand. - This provides certainty to APA that it will earn a return on and of the investment if it is used to provide pipeline services but at the same time, ensures that consumers are not paying for the asset in the event that it does not, in fact, ever get used to provide services. This ensures that prices are kept as low as possible for consumers, particularly in current circumstances of increasing cost pressures.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Forecast Replacement Capex - general 	APA's RAP doesn't appear to address concerns raised in our initial technical report prepared in response to the original AA Proposal – ie that we would expect to see more supporting information to: - explain the replacement program; and - analyse the costs and benefits of different types of replacement programs – eg run to fail v condition monitoring based replacement. This is particularly important in circumstances where accelerated depreciation is being proposed because of expected shortened life of the asset due to reduced demand.
Forecast Replacement Capex – Level of capex 	- While the level of replacement capex in APA's RAP is $20.2m less than what was initially proposed by APA, it is still $6.4m (7%) higher than the level approved by the AER in the Draft Decision. The prudency of this increase should be challenged by the AER given the current circumstances. It also does not appear to be consistent with one of the AER's criteria for the use of accelerated depreciation (see page 29). - APA claims that most of the forecast is as a result of an increased focus on pipeline integrity following an increased focus on managing risks to "as low as is reasonably practicable" because of ageing assets. However, APA has not included any supporting analysis that would be expected such as: • Evidence since the last AA review in 2017 of an increase in frequency of pipeline integrity issues (ie increased frequency of integrity issues) or an increase in consequences as a result of pipeline integrity issues; and • evidence/analysis that the suite of present controls are inadequate to achieve ALARP.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Forecast Replacement Capex – BC203 & 204 	APA's RAP includes forecast capex to develop decommissioning plans for two assets that are presently not used (BC 203 & 204). The AER should investigate this further because: - it is not clear why it will take 5 years to develop the decommissioning plans when they are presently not used - by retaining them in the asset base for the 5 year period, consumers are still paying for them (because APA earns a return of and a return on the original capital expended on these assets) even though the assets are not used in the provision of pipeline services. - the initial capex for these assets should have included an allowance for decommissioning. Accounting standards require decommissioning to be accounted for in the balance sheet of a service provider's accounts. The AER should investigate whether there is no double recovery occurring. - if the assets are not being used, they must, by operation of the provisions of the NGR (Rules 77 and 85), be removed from the opening capital base as a redundant asset. In light of the above, it does not seem to be appropriate to retain the unrecovered amount of these assets in the capital base if, as acknowledged by AEMO, these assets are presently not being used for the provision of services (or will not be once the WORM is commissioned).
Forecast Replacement Capex – number of projects 	Of the 13 replacement capex projects initially proposed by APA in the original AA proposal, APA is only proposing in the RAP to include forecast capex for 7 of the projects and one additional project not previously included. - The proposal for all 7 projects other than for BC203 and 204 (as commented on above) would appear capable of acceptance as confirming capex. - It is not clear whether and to what extent the additional project (BC331 Pipeline Fracture Resistance - $1.4m) relates to the hydrogen study. If it does, it should not be supported as conforming capex

FORECAST CAPEX ISSUES – HYDROGEN ASSESSMENT

Key Element	Comment
Proposed forecast capex for hydrogen safety and integrity assessment 	**AER DD** AER did not accept APA's proposed $37.9 million hydrogen safety and integrity study for a number of reasons: - APA has not provided sufficient evidence of its assessment of risk, how its proposed study would mitigate it, or that its proposed costs of completing this study are efficient. - It is not clear that APA has considered alternative risk mitigation options to its proposed study. - It is not clear that APA has considered whether some or all of this expenditure could be prudently deferred to or spread across future periods. Nor has it identified committed projects to carry hydrogen on either the VTS or Victorian distribution networks **APA's RAP** Hydrogen study expenditure of $18.9m is being proposed, noting that the study is now proposed to be undertaken over 2 AA periods, with capex to be depreciated as if it formed part of the pipeline asset category. This forecast capex has been justified as follows: - APA has obligations under Victorian government legislation to ensure the safety and integrity of the pipelines. It has been supported by the Victorian Safety Regulator (ESV). - It would be prudent to start testing for safety and integrity during 2023-27 in order to keep options open for hydrogen as a future source of energy. APA has provided information to the AER showing the number and location of potential hydrogen producers who have approached APA about injecting into the VTS. - The scope and timing of the study has been revised in response to stakeholder submissions and AER draft decision. APA's analysis of the bill impact is 20 cents per year for residential customers.

FORECAST CAPEX ISSUES – HYDROGEN ASSESSMENT

Key Element	Comment
Proposed forecast capex for hydrogen safety and integrity assessment (cont'd) 	**Comments on AER DD and APA's RAP** - AER DD to not allow the forecast capex is supported - APA should outline more clearly the overall strategy of APA and the pipeline industry towards hydrogen to understand the possible total capital costs which could be incurred for the VTS to enable hydrogen to be commercially injected into the VTS. Without this analysis, this capex may be the "thin end of the wedge" in terms of R&D capex, putting pressure on gas affordability when demand is already declining. - Similarly, what additional costs are likely to be incurred to allow more than 10% hydrogen to be blended into the VTS gas stream. - It makes a lot of sense for the industry to be pooling their resources on this (particularly given that there is no real "first mover advantage" for one pipeline company over another to the use of hydrogen in its network). However, it's not apparent how much of the forecast represents APA's share of industry R&D expenditure. - Consumers have not supported the proposal for hydrogen blending

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
SoCI forecast capex and opex 	Not all of the SOCI related expenditure was approved by the AER in the DD – only $3m of the total $16m (being the cyber security component of the forecast) was approved. The remaining expenditure wasn't approved because APA hadn't provided sufficient evidence to meet the conforming capital expenditure criteria for the other components (being the physical and program components), in particular that APA had not demonstrated that: - the expenditure related to addressing material risks to availability, reliability and integrity of the asset – ie risks that would cause stoppage or major slowdown of the asset's functioning for an unmanageable period; and - The material risks could not be adequately managed by existing controls APA claims that it has provided the information to demonstrate the above matters in its RAP but it has provided very little publicly available information to support its position. We are therefore reliant on the AER making this assessment.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Forecast Opex - general	**AER DD** AER allowed an alternative estimate of total opex forecast of $172.5 million ($2022), which is $7.8 million ($2022) (or 4.3%) lower than APA's proposal. The reduction can be explained as follows: - A $21.6m reduction of step change items, the majority of which are: • Removal of $9.4m in Transformation of Technology expenditure due to lack of substantiating information • A removal of $2.5m in SoCI expenditure • Disallowances of (1) the additional $3.9m to operate the expanded SWP (because project wasn't proceeding), (2) increases in property taxes and (3) the cost of purchasing carbon credits - Offset by increases in the following: • a higher base year opex (increased by $9.8m) • Inclusion of a final year increment of $6.9m, consistent with the AER's guideline • A placeholder amount for the costs of operating the 2nd Winchelsea compressor **APA's RAP** APA has included the following in its revised opex forecast: - A step change amount of $8.1m for Transformation of Technology expenditure - A higher allowance for the running costs of the 2nd Winchelsea compressor than assumed in the AER DD because it is expected to run more frequently and it will be run in series with the first compressor - Carbon offset costs because this meets consumer expectations - SoCI related expenditure for items that address the criteria from the AER's DD on SoCI - A category specific forecast of $1.1m for additional property taxes

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Forecast Opex - general 	**Comments on APA's RAP** *Transformation of Technology expenditure ($8.1m)* - We encourage further scrutiny of this step change, to confirm that spending is unavoidable, and has not been pursued to increase performance or service levels *Running costs of the 2nd Winchelsea compressor* - We question the logic of allowing a higher level of opex because of the compressor being run in series. There was a lack of information provided to substantiate this. While it is acknowledged that running two compressor in series (as opposed to them being run in parallel) may deliver additional capacity, it doesn't follow that additional operating costs will be incurred. *Additional SoCI related expenditure* - We support the reasoning contained in the AER DD as to the type of expenditure for SOCI that would comply with the requirements of the NGR. *Other items* - We support the removal from forecasts opex of amounts for preparation of the AA and working capital costs for linepack and spares and instead, making an allowance for these in the capital base.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Forecast Opex - general 	**Comments on APA's RAP** *Carbon offset costs* APA maintained its proposal from the original AA proposal to include $1.5m as a step change to cover the costs of purchasing Carbon Credit Units to offset emissions from pipelines so as to align with the Vic Government's net zero 2050 transition plan. The supporting information does not appear to address the concerns raised in response to the original AA proposal, being: • There is no legislated obligation to purchase ACCUs • We don't accept the logic that the calculation method for fugitive emissions requires the application of an offset scheme for its resolution. • What incentives are there to reduce emissions from pipelines if the cost of offsets are being passed through to consumers?

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments

Capping maximum asset lives (to 30yrs) to accelerate depreciation of assets 	• AER DD did not agree with APA's proposal to cap the maximum asset life for all asset classes at 30 years and therefore to accelerate depreciation and instead, the AER decided that the current standard asset lives that reflect the technical lives of each asset class (using the weighted average approach) should be adopted. This decision is supported.
	• AER DD outlined the following needs to be provided to enable accelerated depreciation to be considered in the RAP and Final Decision:
	  • a better case needs to be built to demonstrate significant uncertainty of demand for gas – better scenarios showing a spectrum of outlooks and to estimate the likelihood of each scenario
	  • government policy aligning with uncertainty about the future of gas pipelines and networks – while the gas substitution roadmap is providing greater policy certainty, and it is creating incentives to electrify and disincentives for growth in gas pipelines, it also still identifies hydrogen as playing a role.
	  • there is evidence of pricing risk – ie capacity of future users to pay for higher prices as a result of deferring accelerated depreciation. It should also be noted that consideration should be give to the capacity of today's consumers to pay higher prices if accelerated depreciation is introduced now, particularly when it is coupled with the impact of rising inflation and interest rates.
	  • forecast capex / investment profile is limited (ie no growth/expansions and no new connections or significantly reduced replacement and non-network capex)
	  • modelling of future impacts on the VTS
	  • Evidence that maintaining the status quo should not be an appropriate default option – noting the AER's own analysis shows that deferring a decision on accelerated depreciation by 5 years (ie waiting until the next AA review) will only incrementally add approximately 1% to annual revenues in the next AA period.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments

Capping maximum asset lives (to 30yrs) to accelerate depreciation of assets 	• Based on what APA has submitted in support of its RAP, it is not clear that APA has met this criteria:
	  • AER does not appear to have presented scenarios showing a spectrum of outlooks and to estimate the likelihood of each scenario
	  • The recently released Vic Govt gas substitution roadmap is providing greater policy certainty, and it is creating incentives to electrify and disincentives for growth in gas pipelines. But it also still identifies hydrogen as playing a role.
	  • Evidence of pricing risk – there are two components to this:
	  • capacity of future users to pay for higher prices as a result of deferring accelerated depreciation - AER's own analysis shows that deferring a decision on accelerated depreciation by 5 years (ie waiting until the next AA review) will only incrementally add approximately 1% to annual revenues in the next AA period
	  • capacity of today's consumers to pay higher prices if accelerated depreciation is introduced now – even without taking into account the impact of changes in inflation and interest rates, APA has proposed a 14% increase ($85m) in total revenue for the AA period compared with the DD allowance. Even without accelerated depreciation being included, the increase in total revenue being proposed is $79m.
	  • Forecast capex profile – while APA's forecast capex is $73m less than APA's initial AA proposal, it is still $93.4m more (50% higher) than allowed in the DD. Even replacement capex is in excess of $100m and represents 36% of the total of forecast capex. There has also been a step up in the level of forecast capex since the current AA period.
	  • Hard to argue that, in light of the above, maintaining the status quo is not an appropriate default option

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments

Capping maximum asset lives (to 30yrs) to accelerate depreciation of assets 	• Consideration does not appear to have been given to the additional risks consumers will be faced with as a result of adopting accelerated depreciation:
	  • Increased costs for gas consumers could make the switch to electrification even more economic, thereby accelerating the voluntary moving away from the use of gas pipelines.
	  • It will result in higher costs for remaining customers who are less able to switch to electrification because of either the cost involved or they are reliant on gas for their downstream operations
	  • It exacerbates existing stresses of consumers who are already facing increased debt levels for energy usage
	  • Incentivises service providers to continue spending on expansions to the infrastructure and R&D for alternatives to natural gas, which costs are also being proposed to be passed through to consumers
	• When combined with the following other features of the RAP, the risk of asset stranding appears to be unfairly transferred wholly to consumers:
	  • The tariff structures are such that consumers wear demand risk
	  • Debt financiers place a significant importance on demand and asset stranding risk and this should already be factored into the allowed cost of debt
	  • The costs of assessing alternative (renewable) energy to use the asset is being wholly passed on to consumers
	  • Some items of expenditure that have to date been capitalised are now proposed to be expensed
	  • Even the costs of managing reputational risk associated with current use of hydrocarbons (ie purchasing carbon credits) is being sought to be passed on to consumers
	• Proposed use of accelerated depreciation does not appear to be consistent with the NGR and NGL.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Capping maximum asset lives (to 30yrs) to accelerate depreciation of assets (Cont'd) 	Any decision to allow accelerated depreciation in part needs to be part of a total package of measures that should address the above matters, such as: • A cessation of gas network augmentation – and the establishment of policies (eg electrification programs) that allow gas network augmentation to be avoided. Or, if they are required, that they are not funded by the consumers who do not benefit from them or they are funded by government. • Expenditure incurred on research and development into alternative energy sources to natural gas such as hydrogen/biogas research or readiness should not be allowed as part of capital or operating expenditure in any tariff calculation. It could be allowed as speculative investment and not recovered under tariffs until the alternative sources are commercially proven. • Appropriate consideration should be given to transfer of the ownership of any potentially useful assets after full depreciation so as to create incentives for ongoing use of the assets • Support for consumers unable to manage a transition away from the use of gas infrastructure (eg appliance replacement subsidies, financial support for hardship) • Government support for network operators to invest in R&D for alternative, decarbonised energy sources to replace natural gas, rather than seeking to have consumers pay • A strategy to fund assets that become underutilised to avoid spiralling costs – this may include asset write downs and government support

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments

Other depreciation issues 	- Maintained a new asset class for inspections (10 yrs)
	- While a case has not been made for Hydrogen study capex as conforming capex, if it were to be accepted, it should be depreciated over the same life as pipelines (30 yrs)
	- It is not clear from the RAP whether APA has:
	  - Adopted separate asset classes for WORM and SWP related capex – the AER did not allow this in the Draft Decision
	  - Did not split "other" asset class into "short life" (5yrs) and "long life" (15yrs), which was a requirement of the Draft Decision
	- Further information should be sought from APA to clarify what APA has proposed on these two matters

Removal of Fixed Principle associated with SWP and WORM capex 	The RAP has removed the feature of the initial AA proposal that included a Fixed Principle under Rule 100 that the expenditure associated with the SWP and the WORM would not be subject to the capital redundancy provisions included in the access arrangement by virtue of Rule 85. This removal is supported.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Rate of Return & Corporate Tax 	We support APA's proposal to fully adopt the AER's prevailing rate of return instrument and corporate tax methodology. However, we note that APA has not updated its forecast of inflation in the RAP.
Incentive Mechanism 	The retention of only one incentive mechanism (ie the OEIM) is supported, but the calculation of the carryover amounts totalling $3.2m from the current AA period will need to be reviewed as a result of the opex changes being proposed in the RAP. The proposal to not include property taxes (ie a category specific allowance) in the OEIM formula is supported as this is consistent with regulatory precedent with distribution businesses.
Reference tariff variation mechanism 	The following changes to the reference tariff variation mechanisms are supported: - Removal of the mechanism where actual volumes fall either higher or lower than 5.5% of forecasts - The amendments required by the AER to certain definitions in the cost pass through mechanism However, we do not support APA's retention of the pre-approved capex event pass through mechanism, particularly if this is as a result of a Rule 80 determination. If that occurs, the nature of the changes would be likely to warrant a full revision of the AA being submitted for approval as there are likely to be implications for a range of the building blocks.

COMMENTS ON KEY ELEMENTS OF RAP

Key Element	Comments
Tariff setting 	Because the AER DD endorses APA's original proposal relating to the structure and features of the reference tariffs and the proposed prudent discounts, then APA has not proposed any changes in this regard, even though, in stakeholder consultation, APA had considered moving away from the current structure and features (but ran out of time). The following changes should be considered as examples: - more emphasis should be placed on a tariff structure in which the risk of demand forecasts not being met are shared more evenly between consumers and the service provider - Simplicity in structure, particularly in recognition of the high gas market prices and the declining availability of gas
Smoothing of tariffs during AA period 	Leaving aside comments on the individual building blocks that make up the total revenue, the limiting of tariff increases in year one of the access arrangement period to only CPI provides stability of prices for residential consumers from one access arrangement period to the next and is supported While it is noted that the X-factor values to be used to determine the rate of change in tariffs from one year to the next in the AA period will be set as part of the final decision, we would encourage the AER to consider that tariff increases in each subsequent year must fall within a range that is consistent with regulatory precedent, particularly given the significant impact that energy costs are having on cost of living pressures and debt burdens of vulnerable consumers.


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