MASTER BUILDERS
WESTERN AUSTRALIA

Monday, 12 January 2015

Mr Greg Watkinson
CEO
Economic Regulation Authority
L4, Albert Facie House
469-489 Wellington Street
Perth WA 6000

Via email: records@erawa.com.au

Dear Greg

DRAFT REVISION TO THE ACCESS ARRANGEMENT FOR THE MID-WEST AND SOUTH-WEST GAS DISTRIBUTION SYSTEM

Thank you for the opportunity to comment on the Economic Regulation Authority's (**ERA**) *Draft Decision on Proposed Revision to the Access Arrangement for the Mid-West and South-West Gas Distribution System* ("**Draft Decision"**).

Please note that the timing of the due date for comment has restricted industry comments and feedback from builders, given that many people in the industry take leave over the Christmas-New Year period.

About Master Builders Association of Western Australia

The Master Builders Association of Western Australia ("Master Builders") is the peak construction sector association, representing the building and construction industry since 1898 in this state.

Master Builders' 1800 plus member businesses cover both commercial and residential sectors, and are drawn from a range of trades, professions and backgrounds. These members are active in new home, apartment building and commercial building projects.

The organisation's primary role is to promote the views and interests of the building and construction industry to assist to develop our built environment and promote quality construction. It also provides services to members in a broad range of areas including contracts, training, legal services, industrial relations, building codes and standards, industry economics and safety advice.

The construction sector employs some 140,000 workers in Western Australia, and is currently the second biggest employer in WA. Our members build the vast majority of new homes and apartments in Western Australia each year.

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Feedback on draft decision

Master Builders believes there is cause for alarm if the draft decision of the ERA were to be implemented and result in the outcomes predicted by ATCO Gas.

The draft decision of the ERA will significantly cut capital expenditure for ATCO Gas, reduce the commercial incentive for investment in gas, and substantially alter the current funding model for gas connections.

We understand that no new connections in Greenfield development areas will be offered by ATCO Gas because of the limited commercial incentive for ATCO Gas to provide connections - even with the customer paying upfront – gas availability will not be promoted in new development areas and the costs borne by developers, builders and customers will increase.

Feedback from Master Builders members is that consumers overwhelmingly want the choice of gas supply to their new homes. Consistent with this member feedback, ATCO Gas has forecast that approximately 100,000 customers will seek a natural gas connection over the next 5 years, based on current trends.

Below is advice received from ATCO Gas, together with our comments:

1. *The new model will change the pricing model so that upfront capital costs will no longer be recovered by ATCO Gas over a 25 year period for homebuyers in greenfields developments through increased tariffs. Instead, the cost of connections will need to be paid upfront and may not be offered at all.*

   This will have a major impact on energy supply choices made by consumers at the time of purchase of what is usually the major purchase of their lifetime – namely the family home. Consumers face challenge of funding their largest investment and are commonly not in a position to fund upfront capital costs to recover that investment through lower tariffs during the lifetime of an asset. The reality is that discretionary up-front capital costs are commonly cut by consumers and gas reticulation is likely to suffer given competing financial demands at the time of building. This will distort consumer choices due to short term financial challenges. Further, the costs of retrofitting gas infrastructure are likely to prove a strong deterrent to future investment. It is not simply a case of retrofitting the gas supply piping - consumers would also need to fund any changed stoves, heating or other services (eg hot water units) and replace existing appliances that have long useful lives. This would result in inefficient economic outcomes for our communities.

2. *ATCO will no longer be able to fund connections or to maintain the gas supply infrastructure under the draft decision in greenfields developments and has no commercial incentive to provide services even where the upfront costs are covered by another party. Capital expenditure to fund connections has been reduced down to only support the infrastructure for 10,000 new customer connections over 5 years, which only allows for connecting customers where there is already a gas main in the street. In addition, this decision will not just effect the next five years because the economics of providing gas to future new developments will deteriorate as a result of increased costs associated with reaching new areas adjacent to developments where no gas infrastructure exists.*

   Should developers fund the infrastructure (<u>if they provide it at all</u>), the upfront costs could be recovered through costs of purchasing land and buildings. This would push up the cost of a new home in Western Australia, exacerbating well documented and well known current affordability concerns in our community. See the Bankwest Curtin Economics Centre, *Housing Affordability - The Real Cost of Housing in WA,* Focus on Western Australia Report Series, No 2, April 2014 at page 5:

> More and more Australians are paying a higher proportion of their income both to enter and remain in the housing market. Indeed, many find it difficult to enter into home ownership at all, particularly among the younger generations.
>
> While the resource boom in Western Australia has benefited many, high housing prices can provide one of the greatest barriers to many more accessing these benefits. Housing is a major consideration for families looking to move to the west. House prices that are high relative to the income you can earn from the job opportunities available in WA can create disincentives to skilled workers seeking to make the move to the region and enhance the state's stock of human capital and its productivity potential.

The policy shift could be classified as a new tax on development via the ERA policy change. Further, it is not clear who would maintain the cost of the gas infrastructure once the development is completed. The ERA needs to articulate why this would benefit our community and how maintenance of gas networks would be funded post sale.

3. *The decision would drastically slow the gas infrastructure and connection process due to the increase in volume of work that would need to be processed individually to co-ordinate such a model as well as the increased design work and cost as a result of limited capacity upgrades occurring without a specifically identified load or connection.*

   Construction times in Western Australia are already increasing due to planning approval delays and some shortages of trades. Additional delays in connection times adds to the cost of construction (through building costs, finance costs or additional rental costs), creating more inefficiency in our building sector – again impacting on the affordability of housing in our community.

4. *Segregation between developments pre 2015 and post 2015, resulting in new greenfield developments being potentially less marketable over land developments with natural gas.*

   This would result in short term consumer choices of land and house packages being distorted. But it also raises a long term intergenerational equity issue, where future home buyers will generally be forced to pay an upfront cost for capital works for gas supply – something previous generations have not been required to do. Once again, housing affordability concerns are being created.

Overall, Master Builders believes more detailed investigation of the ERA draft decision is required, alongside further stakeholder consultation. The decision, if implemented, is likely to cause a significant shift in the financing of a popular consumer energy supply choice and will distort current market place behaviour. Given the short and long term significance of the reform, a more detailed investigation is warranted warranted to ensure the benefits of the ERA's approach to householders and industry, the community and the state are identified - and transparent - in both the short and the long term.

If upfront construction costs are going to increase, this cautious approach is advisable. At a macro-economic level, federal and state governments are looking to the building sector to step up and replace the strong mining investment we have seen in the last decade.

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Even if the ERA decides to proceed with its draft decision, a significant transitional period would be required to ensure that consumers and industry are protected from adverse financial impacts of a change in regulatory policy that could deter investment in natural gas.

I look forward to your response.

Yours sincerely
MASTER BUILDERS' ASSOCIATION OF WA

Geoff Cooper
DIRECTOR OF HOUSING; BUSINESS DEVELOPMENT