Proposed Revisions to the Mid-West and South-West Gas Distribution System Access Arrangement for 2020 to 2024

Issues Paper

Alinta Energy Submission

[redacted]

14 November 2018

Introduction

Alinta Sales Pty Ltd (**Alinta Energy**) is pleased to provide comment on the *Proposed Revisions to the Mid-West and South-West Gas Distribution System Access Arrangement for 2020 to 2024 – Issues Paper* (**Issues Paper**) released by the Economic Regulation Authority (**ERA**) in response to the proposed Access Arrangement submitted by ATCO Gas Australia (**ATCO**) for the five-year period from 1 January 2020 to 31 December 2024 (**AA5**).

Alinta Energy has over 500,000 natural gas customers supplied directly from ATCO's Mid-West and South-West Gas Distribution Systems (**MWSWGDS**). Earlier this year, Alinta Energy provided comment to ATCO regarding its *2020-24 Draft Plan*[1] (**Draft Plan**), which outlined ATCO's future investments, proposed prices and planned customer services over the AA5 period. Whilst Alinta Energy commended ATCO on the release of its Draft Plan, which went some way in providing stakeholders with an understanding of ATCO's rationale behind its proposal, Alinta Energy raised some concerns with ATCO, including regarding the forecast gas demand and the reference tariff price path proposed for B3 tariff (residential) customers. ATCO hosted a workshop in July to further inform retailers about these two matters in particular.

Whilst ATCO has made some amendments subsequent to the release of its Draft Plan and the retailer workshop, Alinta Energy still has concerns with certain aspects of the AA5 proposal outlined in ATCO's *2020-24 Plan*[2] (**Proposed Plan**). These concerns are discussed further in the sections below.

[1] *2020-24 Draft Plan: ATCO Mid-West and South-West Gas Distribution System*, ATCO Gas Australia, 1 May 2018

[2] *2020-24 Plan: Access Arrangement Information for ATCO's Mid-West and South-West Gas Distribution System*, ATCO Gas Australia, 31 August 2018

Comments

Issue 1: Demand forecast

Submissions are invited from interested parties on ATCO's proposed demand forecasts over AA5.

From the figures available in Table 9.6 of ATCO's Proposed Plan we have calculated the average demand anticipated by ATCO for a B3 tariff (residential) customer over the AA5 period and compared this demand with the Alinta Energy forecast[redacted] for the same period – refer to Table 1.

Table 1: Comparison of average demand for a residential customer

Average Demand (GJ/customer)	2020	2021	2022	2023	2024
ATCO B3 tariff	13.23	12.85	12.48	12.14	11.82
Alinta Energy base (B3 tariff + residential B2 tariff)	15.69	15.66	15.66	15.66	15.69
[redacted]					

Table 1 indicates ATCO's forecast demand per residential customer is significantly less than Alinta Energy's forecast. We note Alinta Energy's forecast is based on 'active' consuming customers and, as such, we would expect it to be higher than ATCO's forecast, however we note ATCO has considered the disconnection of 5,500 zero-volume connection points[4].

The Alinta Energy base forecast demand is derived from our active customer base of residential customers. This includes [redacted] residential customers on the B2 tariff, which tend to be higher consuming than those on the B3 tariff. This weather-based demand forecast indicates a relatively stable forecast outlook over the AA5 period.

[redacted]

New residential connections are forecast to consume slightly less than the current average, although we do expect the impact of more higher density housing to offset the decrease in per household consumption.

Over the past 12 months, some 13% of gas delivery points in Western Australia have been transferred from one retailer to another[5]. Many of these will have been residential customers seeking to obtain discounted offers. Many other customers will have remained with their current retailer but will have switched from the regulated gas tariff to a discounted offer. We note that lower prices tend to lead to higher demand i.e. the greater the discount, the more a customer is likely to consume as they become less concerned about the amount they will

[redacted]

[4] *Connections* p. 58, *2020-24 Plan*

[5] *Gas Retail Markets Monthly Statistics*, October 2018, AEMO, p.1

be billed. As there are now five gas retailers actively competing for residential customers by offering considerable discounts, we would not anticipate the significant decline in average demand per customer suggested by ATCO.

Item 23 of the Issues Paper notes ATCO's total B3 tariff demand is declining at 1.2% per annum over the AA5 period. From Table 1 we calculate ATCO's decline in demand per customer to be closer to 3% per annum. The ERA will need to be satisfied that, as forecast demand is the basis for the price determination, the demand forecasts provided by ATCO are reasonable and are consistently applied across all calculations.

We agree with ATCO's normalisation of the effect of weather on demand (Item 20 of the Issues Paper) and would expect that doing so would result in a stable load forecast into the future. We note the Effective Degree Day calculations being applied exclude the impact of solar.

Issue 2: Tariff Variations

Submissions are invited from interested parties on ATCO's proposed:

- *Price path, including its effect on small use customers;*
- *Change to include B2 and B3 customers into the existing weighted average price cap for A1, A2 and B1 customers.*

Price path

Alinta Energy supports ATCO's proposal to retain the existing tariff classes (A1, A2, B1, B2 and B3) and tariff structures (comprising a fixed charge and a usage charge) for AA5. However, we have concerns regarding the magnitude of the proposed step increase in the network reference tariff for an average customer in each tariff class at the commencement of AA5, as indicated in Table 2:

Table 2: Change[6] in network reference tariffs between 2019 and 2020

Network Reference Tariff Changes	A1	A2	B1	B2	B3
Increase from 2019 to 2020 (%)	25.8	21.0	17.3	20.6	22.9

For B3 tariff (residential) customers, this is a $38 increase[7] in 2020. Whilst this figure has been revised down from the original $40 increase proposed by ATCO in its Draft Plan, Alinta Energy still considers this a steep and unnecessary increase between AA4[8] and AA5.

Whilst we acknowledge the preference indicated by end-use customers participating in ATCO's Voice of Customer program for *an initial price jump, then price stability*[9] we believe many residential customers would consider the magnitude of this increase to be unreasonable, particularly if retailers were permitted to pass this price change directly through to the consumer. Whilst retailers would, for the most part[10], be able to pass the steep tariff

[6] Calculated from Figures 19.1 – 19.5, p. 164-166, *2020-24 Plan*

[7] Figure 19.5, p. 166, *2020-24 Plan*

[8] 1 July 2014 – 31 December 2019 access arrangement period

[9] Table 4.1, p. 13, *2020-24 Draft Plan*

[10] The ability to pass through any changes in network tariffs would depend on the structure of the contract between a retailer and their customer, however most retailers would structure contracts to enable any movements in network tariffs to be passed directly through to large use customers.

increases proposed by ATCO directly through to commercial and industrial and to larger business customers, the regulated gas tariff for small use customers[11] is set by the Western Australian Government as provided in the *Energy Coordination (Gas Tariffs) Regulations 2000* (**Tariff Regulations**).

Under the Tariff Regulations, a gas retailer is only entitled to increase its regulated gas tariff by a CPI-based formula each financial year. This means that any increases to the network tariff above CPI will be borne by retailers, predominantly by Alinta Energy as the incumbent gas retailer with a significant number of small use customers remaining on the regulated gas tariff.

If Alinta Energy wants to increase the tariff above this amount it must request that the Government amend the Tariff Regulations. However, there is currently no process for how this should occur and any such request comprises a risk that the application won't be approved, even if the change was supported by all market participants, including the ERA.

As there is no alignment between ATCO's proposed network tariffs and the Tariff Regulations, Alinta Energy will be the predominant party impacted by the change in network tariffs as new entrant retailers can offer discounted retail tariffs to high value customers, leaving Alinta Energy to supply, at below cost, low use consumers on regulated retail tariffs. The proposed steep increase in network tariffs on 1 January 2020 further exacerbates the impact on Alinta Energy in that year.

Alinta Energy supports long-term price stability, however we believe this can be achieved without the initial steep price increase in 2020. Recognising it may not be feasible to retain ATCO's existing AA4 price path trajectory through to 2024, we would recommend a smaller initial price increase in 2020 for B3 tariff customers, followed by a smooth increase over the remainder of AA5. A more modest price increase in 2020 would leave retailers less exposed in the transition between AA4 and AA5. Significant network price increases will ultimately impact residential customers when retailers seek to moderate their discounted retail offers to accommodate the increases.

<u>Weighted average price cap</u>

Alinta Energy notes the change to include B2 and B3 customers into the existing weighted average price cap for A1, A2 and B1 customers, as was applied in access arrangements prior to AA4. We support this approach, recognising a price cap will provide an incentive for ATCO to increase customer connections and usage to generate additional revenue. The alternative approach of a revenue yield provides no such incentive for ATCO. The proposed price cap approach means retailers and the network operator are equally incentivised to work hard to obtain new customers and increase demand.

Issue 3: Taxation

Submissions are invited from interested parties on ATCO's proposal to:

- *Introduce a new 'telemetry' asset category with a tax asset life of 10 years;*
- *Retain a straight-line method of depreciation to calculate its tax depreciation.*

Submissions are also invited on whether any of the AER's findings from its review of the regulatory tax approach should be adopted in reviewing ATCO's proposal.

Alinta Energy supports the introduction of the new 'telemetry' asset category with a tax asset life of 10 years, recognising the increasing demand for enhanced flow measurement technologies.

[11] Customers consuming less than 1 terajoule of gas per annum.

Issue 4: Incentive mechanisms

Submissions are invited from interested parties on the following:

- *ATCO's proposal to introduce a new incentive mechanism (the "Network Innovation Scheme") into the access arrangement;*
- *The benefits of the incentive mechanism proposed by ATCO for natural gas consumers, including how the benefits of such a mechanism might be shared between ATCO and consumers.*

Alinta Energy supports innovative and cost-effective energy solutions that benefit end-use customers.

It is important the costs of any individual project under the Network Innovation Scheme (**NIS**)are recovered only from those who will benefit. For example, if a project benefits end-use customers on a particular network tariff, then we would anticipate the costs related to that project are recovered from those customers only and not from the entire customer base.

Additionally, should ATCO work exclusively with an end-use customer or an individual retailer on a project, then that project should not be included in the scheme.

We note it is proposed the NIS be administered by the ERA, which we would support. However, we would encourage the ERA to carefully scrutinise the details and anticipated costs of each proposal and to seek submissions from key stakeholders prior to approving any project under the NIS. The costs to the ERA of administering the NIS should be recovered under the scheme and not from licensed entities via licence fees or charges.

We would also encourage ATCO to continue to pursue external funding from other sources such as the Australian Renewable Energy Agency (ARENA), which is funded by the Australian Government specifically to support the development of renewable energy technologies.

Issue 5: Reliability and security of supply capital expenditure

Submissions are invited from interested parties on whether the aggregate level of proposed reliability and security of supply expenditure is reasonable in the context of current and forecast service performance.

Alinta Energy notes the increase in proposed network sustaining capital expenditure (**capex**) to 54% ($276.1m) of total forecast capex, up from 49% ($221.7m) over the last 5 years of AA4. We urge the ERA to consider whether the network reliability targets proposed for AA5 are commensurate with this increase, noting that some performance targets have been set at more easily achievable levels than those attained over AA4.

Issue 6: Pipeline services

Submissions are invited from interested parties on ATCO's proposal to:

- *Retain the current AA4 haulage reference services for AA5;*
- *Introduce a new 'special meter reading' ancillary reference service.*

Submissions are also invited from interested parties on whether other pipeline services should be classified as reference services.

Alinta Energy agrees with ATCO's proposal to retain the current AA4 haulage reference services in AA5.

The inclusion of a new 'special meter reading' reference service as an ancillary reference service is supported. There has been a significant increase in special meter reading requests over the past few years related to customer transfers and this trend is expected to continue.

Issue 7: Reference tariffs

Submissions are invited from interested parties on ATCO's proposal to:

- *Maintain the current tariff charging parameters for haulage reference services;*
- *Charge users an amount of $12.82 ($ real as at 31 December 2019) for undertaking special meter reading. Previously this charge was a non-reference service.*

Haulage reference services

Alinta Energy supports maintaining the current tariff charging parameters for haulage reference services in AA5, however we would urge the ERA to carefully assess the components that determine the ultimate price of each haulage reference service, including the following:

Operating expenditure

Rule 91 of the National Gas Rules (**NGR**)[12] requires that operating expenditure (**opex**) must be such as would be incurred by a prudent service provider acting efficiently and in accordance with good industry practice to achieve the lowest sustainable cost of delivering pipeline services.

Alinta Energy supports ATCO's proposed base-step-trend approach for calculating the opex for AA5, whereby step changes in operational costs anticipated over the access arrangement period are applied to the base opex. However, the intended expenditure will require ERA evaluation to determine whether it meets the criteria in Rule 91.

We also note that, as customer connection growth forecasts may have a substantial impact on opex, these should be carefully reviewed by the ERA.

Capital expenditure

Alinta Energy notes ATCO has revised the proposed capital expenditure (**capex**) for AA5 down from the 9% or $44m increase proposed in its Draft Plan to a 2% or $12.2m increase in its Proposed Plan. It is important ATCO is in a position to actually undertake the level of work proposed and we would encourage the ERA to review ATCO's proposed initiatives.

We support the proposed Automated Meter Reading project, which will enable meters to be read wirelessly from the street where physical access to the meter is restricted. We would encourage ATCO to work together with retailers to ensure the best outcomes for customers.

[12] National Gas Rules version 37, 10 April 2018

Return on working capital expenditure

We note there have been adjustments to some of the parameters applied to the components of working capital in AA5, principally based on payment terms of creditors and with retailers. We question the considerable increase in receivables from 18 days to 62 days, noting the 10 business day payment terms for reference services in the proposed revised Template Service Agreement[13].

We also note the significant step increase[14] from the closing AA4/opening AA5 working capital of $1.5m in 2020 to $23.8m in the following year and query whether the proposed working capital value represents efficient business operations.

Special meter reading charges

We would support the proposed amount of $12.82 (ex GST) for undertaking a special meter reading reference service and note this is less than the current non-reference service charge of $18.33 (ex GST).

Issue 8: Terms and conditions

Submissions are invited from interested parties on:

- *ATCO's proposal to make amendments to the template service agreement;*
- *Whether any other amendments to the template service agreement should be made.*

The Template Service Agreement sets out the terms and conditions upon which ATCO will provide reference services and, as such, it should ensure that customers are provided with acceptable standards of service and retailers are treated equitably, ensuring fair and robust competition in the retail gas market.

Alinta Energy has a few comments on the Template Service Agreement as follows:

Clause 17 Liability of Parties: We consider this clause is too broad and does not allocate liability where the risk is best controlled. All liability is placed on the User, whereas Alinta Energy considers the Service Provider is the party best able to control the risk.

Schedules 3, 4 and 5 Special Meter Reading: Whilst the Service Provider is required to use reasonable endeavours to undertake a Special Meter Reading within 2 business days of receive a request from a User, it is not clear whether, if the Service Provider does not comply with the request, a Reference Tariff is payable. We consider that payment should not be made until the Special Meter Reading has been conducted, attempted to be conducted or cancelled by the user. That is, if the request is not complied with through the fault of the Service Provider, then payment should not be required by the User.

[13] *Template Service Agreement*, cl 10.2 p. 30, 31 August 2018

[14] Table 16.5, p. 146, *2020-24 Plan*

Issue 9: Application procedures

Submissions are invited from interested parties on:

- *ATCO's proposal to make amendments to the application procedures for requesting access to a pipeline service;*
- *Whether any other amendments to the application procedures should be made.*

Alinta Energy agrees with ATCO's proposal to standardise the process for access to the regulated "covered" MWSWGDS and the non-scheme gas distribution systems in Albany and Kalgoorlie. Stream-lining access requirements will benefit users seeking access across multiple networks.

Issue 11: Extension and expansion requirements

Submissions are invited from interested parties on:

- *ATCO's proposal to introduce a new development rebate scheme to form part of the extension and expansion requirements;*
- *ATCO's proposal to make other amendments to amend the:*
  - *Reporting timeframes for extension and expansions*
  - *Definition of the pressure threshold for high pressure pipelines.*

Alinta Energy supports the proposed development rebate scheme whereby developers who have provided capital funding in excess of $50,000 to reticulate gas in commercial subdivisions will be eligible for a rebate from ATCO.

We support the amount of rebate reflecting the amount ATCO determines meets the new capex criteria under NGR 79.

This scheme will act to encourage the reticulation of gas in commercial subdivisions, providing end-use customers with more choice in energy options and driving the cost of gas down as uptake increases.