27 November 2023

Mr Tyson Self
Economic Regulation Authority
PO Box 8469
Perth BC WA 6849

Lodged electronically: https://www.erawa.com.au/consultation

Dear Mr Self,

RE: Proposed revisions to the access arrangement for the Mid-West and South-West Gas Distribution Systems – Issues paper

Origin Energy (Origin) appreciates the opportunity to provide comment on the Proposed Revisions to the Mid-West and South-West Gas Distribution System Access Arrangement for 2025 to 2029 – Issues Paper (Issues Paper) released by the Economic Regulation Authority (ERA) in response to the proposed Access Arrangement submitted by ATCO Gas Australia (ATCO).

This revised gas access arrangement comes at an uncertain period for the gas supply industry. The move towards decarbonisation and the evolving policy response creates considerable uncertainty for both networks and regulators. In addition, the economic environment remains unstable with cost of living pressures at the forefront. These factors present a significant challenge for both ATCO and the ERA to balance the interests of ATCO and consumers.

ATCO's proposal assumes that recent reforms to the National Gas Law (NGL) and National Gas Rules (NGR) will be implemented in Western Australia. However, we agree with the ERA's proposal to apply the relevant regulatory framework at the time of making its draft and final decisions. Notwithstanding, it is important that the ERA retain the flexibility to incorporate these reforms into the regulatory framework if adopted and given the dynamic nature of gas policy, also allow for other significant policy changes that may occur within the regulatory period.

Origin is concerned with the proposed increase in haulage tariffs for 2025. Although there may be no significant increase in gazetted retail tariffs, there will be a significant impact on the contestable retail gas market and on the actual prices paid by market customers. We consider a lesser step increase followed by smaller annual increases in the remaining years of the period would reduce the impact on retailers and customers while allowing ATCO to recover its approved revenue.

ATCO proposes additional expenditure to support the integration of hydrogen and other renewable gases in the distribution network. Given the supporting legislation has not been enacted in Western Australia and uncertainty over the supply availability and cost effectiveness or renewable alternatives, we do not support the proposed expenditure. Any proposed expenditure should be contingent on the introduction of legislation supporting the use of these alternatives and demonstration of the viability and customer benefits.

Similarly, we do not support ATCO's proposal for accelerated depreciation. On the one hand ATCO is proposing to commit expenditure to grow the network and introduce renewable gas yet on the other hand it is arguing that it will have stranded assets as a result of the introduction of renewable gases. We consider it unreasonable for customers to bear additional costs to mitigate asset stranding while simultaneously paying for network growth that could potential add to any asset stranding risk.

Origin's response to selected issues is provided below.

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Legislative framework

We note that recent reforms to the national gas regulatory framework, including extending the framework to hydrogen blends and renewable gases and incorporating an explicit emissions reduction objective have not been implemented in Western Australia. While ATCO's proposal assumes these reforms will be implemented, we consider the ERA's proposal to adopt current legislative settings is prudent. We agree that the developing policy environment means that forecasts and assumptions may need to be revisited prior to the release of the ERA's Draft and Final Decision and potentially into the next access arrangement period to best manage this risk. It is important that the ERA consider how the evolving policy landscape can be effectively incorporated into the access arrangement in a way that promotes efficient outcomes and increased certainty for both customers and ATCO.

Demand forecasts

In the absence of information to the contrary, we consider it reasonable to rely on historic trends to develop forecasts of gas customer consumption and connections for the forthcoming regulatory period. We note the potential for ongoing policy developments, including for example the potential for introducing renewable gases to the network or promoting gas use (as opposed to electrification) to impact both the growth in customer connections and utilisation per connection. It is vital that the ERA and ATCO ensure that demand forecasts are updated progressively as more information comes to hand and the implications for expenditure and prices as the policy environment becomes clearer. Where there are significant within-period variations in demand, the access arrangement may need to be amended to reduce the prospect of price shocks in the following regulatory period.

Disconnection charge

ATCO proposes to introduce a new permanent disconnection ancillary reference service for the forthcoming regulatory period. The proposed 'standard fee' charge for 2025 is $1,184.80 (excluding GST), which is payable at the time of application for the service.

In principle, Origin supports the application of a user-pays approach for directly attributable services. However, it is not clear if a permanent disconnection is required for customers who decide to electrify their properties or if a simple deregistration is sufficient. Where permanent disconnection is required, the proposed charge may act as a de facto exit fee and may discourage customers from exiting the gas market to electrification. Exit fees represent a barrier to switching and customers should be informed of cheaper options to electrify and avoid paying fixed service charges, for example by opting to simply deregister rather than have services permanently removed. The cheapest switching options must be communicated to customers.

To the extent that policy settings change in Western Australia and electrification is incentivised for example, the ERA may need to revisit the proposed permanent disconnection fees to ensure they do not act as a barrier to exit.

Network tariff structure

While we agree that the current tariff structure (declining block) and associated tariff variation mechanism (price cap) may be inconsistent with an emissions reduction objective, there is no clear alternative at this time. Any move from the status quo has potential implications for consumer prices and the potential to transfer risk from networks to consumers. Given the fluid policy environment and uncertainty over the future role for gas and gas distribution networks, we consider it is not appropriate to change these settings at this time.

Investment in renewable gases

ATCO proposes specific expenditure of $26.4 million to support the integration of hydrogen and other renewable gases in the distribution network in the forthcoming period. We appreciate that ATCO is seeking to prepare the network in the event renewable gases prove viable, while also targeting emissions

reductions. However, we consider there are considerable uncertainties associated with the policy framework and we have concerns regarding the supply availability and cost of renewable gases at this time.

Specifically, recent amendments to the NGL and NGR allowing for hydrogen and other renewables and the adoption of emissions targets have not been implemented in Western Australia. It is also not clear if the West Australian Government will promote the use of gas (or renewables) or move towards electrification. Further, the supply availability of alternative gas fuels such as biomethane and hydrogen, and the technical requirements and cost effectiveness remains uncertain.

For these reasons, we consider that expenditure to facilitate hydrogen/renewable gas readiness should only be included in the event that the relevant legislation is passed, and the viability and customer benefits have been demonstrated.

In the absence of legislation coming into effect at the start of the access period, ATCO should seek a cost pass-through.

Accelerated depreciation

ATCO's proposal includes $80 million for accelerated depreciation to address the uncertainty of the future of gas and the use of the gas distribution network. This represents 23 per cent of the increase in proposed revenue.

In principle, Origin supports the use of accelerated depreciation as a means of addressing network asset stranding risk. We note also that the ERA (Dampier to Bunbury Natural Gas Pipeline) and AER (Victorian gas networks) have previously identified the use of accelerated depreciation as an appropriate means of addressing potential asset stranding risk.

However, it is important that any accelerated depreciation proposal is consistent with other aspects of the regulatory proposal. ATCO's proposal to commit expenditure to grow the network and introduce renewable gas appears inconsistent with its proposal to accelerate the end of the useful life of certain elements for its network. While we appreciate that ATCO is seeking to limit its financial exposure and that of its' customers in the face of uncertainty, we consider it unreasonable for customers to bear the additional costs associated with accelerated depreciation while simultaneously paying for network growth.

Current cost of living pressures means that any potential increases in gas tariffs arising from an allowance for accelerated depreciation are likely to be felt especially hard by customers. In addition, excessive price increases in the short-term could exacerbate disconnections from the gas networks, leaving remaining customers to carry a higher cost burden to maintain the networks. It is important therefore that price increases are limited where possible.

Under the circumstances, we do not support ATCO's proposed accelerated depreciation.

As the policy environment and the path to decarbonisation becomes clearer, it may be that the approach to depreciation needs to be revisited or that other measures are required. It is important that the regulatory framework is sufficiently flexible to accommodate the changing policy environment and allows ATCO to respond in an effective and timely manner.

Price path

ATCO proposes a large tariff increase in 2025, followed by annual increases for inflation. For the residential B3 tariff, the average annual distribution charge for an average residential customer will increase by $78 in 2025, representing a 12 per cent increase on an annual retail gas bill at the gazetted retail price.

While we appreciate that the increase is primarily due to circumstances outside of ATCO's control, we have concerns regarding the magnitude of the proposed step increase for an average customer. While gazetted retail tariffs will not increase by the same margin, there will be a significant impact on the contestable retail

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gas market and on the actual prices paid by consumers. Because there is no commensurate increase in gazetted tariffs, the increase in network charges in 2025 will increase market offers to customers, with a reduction in competitive discounts to the most active market customers and less retail competition in general.

We consider that a reduction in the step increase in 2025 followed by smaller annual increases in the remaining years of the period would provide less of a shock to customers and help to maintain retail competition whilst allowing ATCO to achieve full cost recovery over the regulatory period.

If you have any questions regarding this submission, please contact Gary Davies in the first instance at [redacted].

Yours sincerely

Sean Greenup
Group Manager Regulatory Policy