ENERGY CONSUMERS AUSTRALIA

A Suite 2, Level 14, 1 Castlereagh Street
Sydney NSW 2000
T 02 9220 5500
W energyconsumersaustralia.com.au
@energyvoiceau
in /energyconsumersaustralia
f /energyconsumersaustralia

ABN 96 603 931 326

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Mr Sebastian Roberts
General Manager, Transmission and Gas
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Via email: JGNGAAR2020-25@aer.gov.au

JEMENA GAS NETWORKS REVISED ACCESS ARRANGEMENT PROPOSAL 2020-25

Dear Mr Roberts,

Energy Consumers Australia is the national voice for residential and small business energy consumers. Established by the Council of Australian Governments (COAG) Energy Council in 2015, our objective is to promote the long-term interests of energy consumers with respect to price, quality, reliability, safety and security of supply.

We appreciate the opportunity to respond to the Australian Energy Regulator's (AER) consultation on its Draft Decision for the Jemena Gas Networks (JGN) access arrangement proposal for 2020-25 (the revised proposal).

While there is alignment on most issues, we do not consider that JGN's revised proposal is capable of acceptance by the AER.

We engaged TRAC Partners to undertake a technical review of JGN's initial and revised access arrangement proposals. This analysis informed our submissions on JGN's draft plan (May 2019) and JGN's formal proposal (August 2019). We have attached the technical report provided by TRAC Partners on the revised proposal to help inform your assessment. This assessment has raised the following key issues where further thought and discussion are required: the treatment of uncertainty and accelerated depreciation; consumer engagement; and pricing. This submission further expands on these issues.

When formed by the COAG Energy Council, Energy Consumers Australia was tasked with promoting the long-term interests of consumers through evidence-based consumer advocacy on matters of strategic importance of material consequence for energy consumers.[1] The AER's decisions on the issues raised above are likely to have an impact on broader gas access arrangements, and potentially electricity regulated revenue proposals The issues related to uncertainty and consumer engagement fall squarely with the category of matters of strategic importance with material consequence nationally.

What consumers are telling us

The results of our December 2019 Energy Consumer Sentiment Survey (ECSS) show that NSW consumers' satisfaction with gas services is starting to increase across all measures. With 82 per cent of NSW consumers are satisfied with the reliability of the service and 68 per cent are satisfied with the value for money they get for gas.[2] This still leaves gas ranking behind other utilities in consumers perceptions of value for money across service types.

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[1] Energy Consumers Australia, Constitution of Energy Consumers Australia Limited, section 4.1 (a).
[2] Energy Consumers Australia, ECSS, December 2019, page 61.

Qualitative research we commissioned to explore consumer expectations for better energy services reveals expectations for cheaper, simpler, cleaner, smarter energy services in the future, and a need to know the consumer voice is included in decision making process – with consumers being very realistic about their expertise and ability to commit time to such processes. This research suggests to us greater responsibility on all parties to make sure a careful and comprehensive approach is taken to “consumer voice in the room”.

Uncertainty and accelerated depreciation

Business managers make subjective decisions about the probability distributions to apply to future events all the time, they assign risk levels. The depreciation schedule of a business is management’s assignment of a probability distribution to how much the asset will be used in each of a series of future years. In cases of assigned risk it is then possible to place a value on the cost of absorbing that risk; this is fundamentally what the Capital Asset Pricing Model used to determine the allowed rate of return is purporting to do, it is assessing how the financial market prices that assigned risk.

To change a depreciation schedule, to accelerate depreciation, is management saying it has changed its subjective assessment of future uses of the network. It is now assigning a different risk profile. This change has consequences for the cost of capital, which consumers fund.

It is a fundamental principle that risk should be borne by the party best able to manage it, though this is sometimes described as best “able to wear” the risk. In reality, all risk is ultimately borne by consumers, usually through the cost of operations and the cost of capital. In our submission to JGN’s initial proposal, we included a graph illustrating the significant imbalance between increasing gas and electricity indices and total consumer price index (CPI). Where consumers wages may be tied to CPI we may infer that wage growth is slower than gas and electricity price growth.

Consumers are continuing to tell us – through quantitative experience research and qualitative expectations research that affordability is their prime concern.

In our view, any subjective judgment that increases the cost to consumers needs to be tested very thoroughly by the AER as the decision maker.

Such testing will be taking place against a backdrop of significant infrastructure works foreshadowed for the energy market generally. Additional cost to consumers must be carefully considered, and considered in a way that reflects the reality for consumers that discrete costs along the supply chain end up bundled into consumers’ bills. For the last 10 years, the outcome of that process compared to ability to pay, funded by wages growth, has left consumers saying, “Unaffordable”. There is some way to go for the sector to be regarded by consumers as delivering affordable energy services.

Rafael Ramirez of the Oxford Saïd Business School Scenario Planning Programme tells us that:

> *It is in memory that we store the heuristics (or rule of thumb) that have served us well and which we routinely depend upon to reach decisions in situations that conform to some pattern we have experienced before. Such heuristics feature as pre-judgements and pre-conceptions, as well as biases in decision making…Yet, in a study of eighty failed strategies, Finkelstein et al (2013) found that 82 percent of the failures were related to “misleading pre-judgements.”*[3]

Right now, gas and electricity infrastructure owners have not seen as much change since the creation of the East Coast Gas Market and National Electricity Market. It is difficult to separate the transformation of energy provision in Australia as a whole, from its component parts (that is, gas and

[3] Rafael Ramirez and Angela Wilkinson, *Strategic Reframing: The Oxford Scenario Planning Approach*, 2018, page 60.

electricity). This is because changes in one are likely to see changes in the other. For example, the role of gas in the electricity market transformation as a transitional fuel as mentioned by the Prime Minister recently.[4]

In Australia's Chief Scientist's National Press Club Address: *The orderly transition to the electric planet*, Dr Alan Finkel supported the Prime Minister's reference to gas as a fuel of transition and referred to hydrogen as the "hero". Dr Finkel said that this transition would take decades and that "It will also require respectful planning and re-training to ensure affected individuals and communities, who have fueled our energy progress for generations, are supported throughout the transition".[5] From our perspective, this respectful planning approach to transition must include consideration of the consumers who have, and continue to pay for, the investment in the physical infrastructure.

We note that since the lodgment of the revised proposal, the NSW Government has made a commitment to inject 70 petajoules of gas into the market.[6] We see this as a good example of why there needs to be broader discussion and cooperation to address uncertainty that does not see consumers bearing the cost risk.

In terms of the treatment of the risk in the revised proposal (that is, through accelerated depreciation of the asset base, starting in this period with new assets), our view is that there is insufficient compelling evidence to support this approach and indeed positive opportunities emerging in the recent discussions referred to above.

The longer-term question is whether the current economic regulatory framework for gas is equipped to address any issues of uncertainty which may lead to considerations of the costs of accelerated depreciation? This question provides the AER with the opportunity to elevate the discussion outside of the regulatory framework, considering both gas and electricity equally. This is a conversation that the AER is well-placed to lead and should start soon, heeding Dr Finkel's comments above.

Without careful consideration and consultation on how the sector handles "orderly transition" and discussion about where the costs of this should fall, a single network response by the AER on a proposal in regard to accelerated depreciation may result in consumers being unwilling to pay for stranded assets, rather seeing such costs as a "fee for no service".

Consumer engagement

In Attachment 8.4 of JGN's revised proposal – *Professor Cosmo UK – Regulatory decision making and consumer voices – January 2020*, the discussion around uncertainty and accelerated depreciation appears to be conflated with what good engagement looks like. This report assesses consumer views on accelerated depreciation in isolation of the broader consumer engagement program. Given the good work that secured JGN a joint win (with Jemena Electricity Networks) of the ENA ECA Network Community Engagement Award 2019, we are disappointed by the approach taken in this report. We were not consulted as part of the report's development.

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[4] Prime Minister of Australia and Premier of New South Wales media release: *NSW energy deal to reduce power prices and emissions*, 31 January 2020. Accessed from https://www.pm.gov.au/media/nsw-energy-deal-reduce-power-prices-and-emissions

[5] Australia's Chief Scientist, National Press Club Address, *The orderly transition to the electric planet*, accessed from https://www.chiefscientist.gov.au/news-and-media/national-press-club-address-orderly-transition-electric-planet.

[6] Prime Minister of Australia and Premier of New South Wales media release: *NSW energy deal to reduce power prices and emissions*, 31 January 2020. Accessed from https://www.pm.gov.au/media/nsw-energy-deal-reduce-power-prices-and-emissions

Pricing

The rationale behind JGN's approach to pricing is to be commended and reflects its commitment to improving affordability outcomes for consumers, as a signatory of the Energy Charter.

Generally, we support price paths that provide the greatest stability for consumers, as price stability helps to rebuild consumer trust and confidence in the sector.

We do however, recognise the tension between a network wanting to protect its consumers from changing wholesale prices; a regulator bound by the regulatory framework; and a retail sector that has lost the trust of consumers that it will pass through the savings opportunities made available by a network in its pricing structure. This tension is heightened when considering the volatility in wholesale market prices. Recent AEMC work indicates reduction in wholesale gas prices in East Coast markets.

In the attached report, TRAC Partners suggests testing the approach against a number of scenarios and we support this suggestion. Also, in its submission to the AER's consultation on Energy Queensland's electricity pricing determination 2020-25, the Queensland Council of Social Service companion report by Etrog Consulting suggests that the AER establish a transition working group to, among other things, manage the implementation of tariff reform. We suggest that the principle behind this suggestion (that is, coordinated and considered approach to tariff reform/development) could be appropriate across both electricity and gas.

Concluding comments

The AER is in a unique position to have a deeper understanding of decisions made by network businesses and the impacts of these decisions on consumers given its access to information; ability to identify and analyse trends and emerging issues in the energy sector; and analysis of the impact of these issues on consumers. This position suggests that the AER is best placed to help further the sector's discussion about the ongoing reform of the economic regulatory framework.

We have raised several issues in this submission that we believe the AER can elevate above the framework and we would happily participate in these discussions. If you would like to discuss any of the issues raised in this submission, please contact Shelley Ashe, Associate Director, on 02 9220 5514 or via email at shelley.ashe@energyconsumersaustralia.com.au.

Yours sincerely,

Rosemary Sinclair AM
Chief Executive Officer

Att: TRAC Partners *Technical Report: Response to JGN Revised Access Arrangement Proposal – 2020-25*