

Revised Final Plan Attachment 8.11

Response to Draft Decision: Capital Expenditure

August 2017

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1. Response to Draft Decision on Capital Expenditure

1.1 Introduction

This attachment sets out Australian Gas Networks Limited's (AGN's) response to the Australian Energy Regulator's (AER's) Draft Decision on capital expenditure (capex) for our Victorian and Albury networks over the next (2018 to 2022) Access Arrangement (AA) period.

The AER approved our capex forecast after reflecting some minor updates to our Final Plan.¹ We have accepted the AER's Draft Decision and, as required by the AER, we have incorporated some minor amendments into our Revised Final Plan capex forecast.²

Our Revised Final Plan capex forecast is \$556 million (\$2017), which is \$2 million (or 0.4%) higher than the AER Draft Decision and \$1 million (or 0.1%) higher than our Final Plan capex forecast of \$555 million.

1.2 Stakeholder Engagement

In preparing this Revised Final Plan we have continued to engage with stakeholders, including our Reference Groups and through the submissions to the AER on our Final Plan.

There were three stakeholder submissions in relation to our proposed capex forecast, which focused primarily on our proposed unit rates and information technology (IT) expenditure. A summary of the key feedback provided in relation to our capex proposal is provided in Table 1.1.

Table 1.1: Consideration of Stakeholder Feedback on our Capex Proposal

Stakeholder Feedback on the Final Plan	Our Response to Feedback on the Final Plan
Stakeholders commented that the AER should review our proposed unit rates for mains replacement activities. ³	In response to questioning from the AER, we have adjusted some of our forecast unit rates to reflect updated tender information, which have been reflected in the AER's Draft Decision.
Stakeholders were supportive of our plans to complete our mains replacement program, particularly given the support we received for this program from Energy Safe Victoria. ⁴	We are continuing to forecast the completion of our mains replacement program by the end of the next AA period.
Stakeholders supported our proposed increase in IT expenditure over the next AA period, so long as our costs remain in line with industry benchmarks. ⁵	We are forecasting an increase in IT capex over the next AA period, however despite this our IT expenditure will remain below or in line with the industry mean. For further information please refer to Attachment 8.7 of our Final Plan.

Note: In this 'traffic light' table, green shading represents no change from the Final Plan, orange represents a modification of the position outlined in the Final Plan and red shading represents a change from the Final Plan.

¹ AER, *Attachment 6 – Capital Expenditure | Draft decision - AGN Victoria and Albury gas access arrangement 2018–22*, July 2017, page 6-6.

² *Ibid*, page 6-17.

³ Consumer Challenge Panel, *Advice to the Australian Energy Regulator | Consumer Challenge Panel Sub-Panel 11 | Response to proposals from AGN, AusNet and Multinet for a revenue reset/access arrangement for the period 218 to 2022*, March 2017, page 48.

⁴ Red Energy and Lumo Energy, *Re: Australian Gas Networks Access Arrangement*, March 2017, page 2.

⁵ *Ibid*, page 2.

1.3 AER Draft Decision

The AER largely accepted our Final Plan capex proposal after implementing some minor amendments to our capex forecast. We have provided a summary of the AER's Draft Decision by capex driver category in Table 1.2 below.

Table 1.2: Summary of AER's Draft Decision on Capex

	AER Draft Decision	AER Comment
Mains Replacement	Accept	Accepted our proposal to undertake 297 kilometres of mains replacement over the next AA period, but amended some of our proposed unit rates to reflect updated tender information. ⁶
Growth Capex	Accept	Accepted our growth capex forecast, subject to updating connection volumes to reflect the rejection of the marketing step change. ⁷
IT	Accept	Accepted our proposed IT capex over the next AA period, consistent with the nationalisation of our IT systems approved by the AER for our South Australian network. ⁸
Meter Replacement	Accept	Accepted our proposed meter replacement program, commenting that our forecasting methodology was based on good industry practice and our estimates were well developed. ⁹
Augmentation	Accept	Accepted our proposed augmentation projects over the next AA period on the basis that our business cases were comprehensive and cost estimation techniques used ensured our project cost estimates represented efficient costs. ¹⁰
Telemetry	Accept	Accepted capex relating to our ongoing telemetry program focused on end of life replacement and extending our telemetry network to fringe points. ¹¹
Other Assets	Accept	Accepted a range of other projects to be delivered over the next AA period, which includes the ongoing upgrades to plant and equipment. ¹²
Escalation	Accept	Accepted our approach to forecasting real cost escalation, consistent with their decision in relation to our opex forecast.
Overheads	Accept	Accepted our approach to forecasting overhead costs given it is consistent with the AER's decision in relation to our recent South Australian AA review. ¹³
Contributions	Accept	Accepted our forecast of customer contributions given our approach is based on calculating a three-year historic average of actual contributions, consistent with the approach approved by the AER for our South Australian network. ¹⁴

Note: In this 'traffic light' table, green shading represents the AER's acceptance of AGN's Final Plan, orange represents the AER's modification of AGN's Final Plan and red shading represents the AER's rejection of AGN's Final Plan.

⁶ AER, *Attachment 6 – Capital Expenditure / Draft decision - AGN Victoria and Albury gas access arrangement 2018–22*, July 2017, page 6-17.

⁷ *Ibid*, page 6-18.

⁸ *Ibid*, page 6-22.

⁹ *Ibid*, page 6-29.

¹⁰ *Ibid*, page 6-27.

¹¹ *Ibid*, page 6-29.

¹² *Ibid*, page 6-30.

¹³ *Ibid*, page 6-31.

¹⁴ *Ibid*, page 6-22.

1.4 AGN Response to the Draft Decision

We have accepted the AER's Draft Decision on the basis that it is consistent with our capex proposal in our Final Plan (see Table 1.3).

Table 1.3: Summary of AGN's Response to the AER's Draft Decision on Capex

	AER Draft Decision	AGN Response	AGN Comment
Mains Replacement	Accept	Accept	We have accepted the AER's Draft Decision and note that there has been no new tender information to reflect in the mains replacement unit rates in our Revised Final Plan.
Growth Assets	Accept	Accept	We have accepted the AER's Draft Decision and have updated the customer numbers underpinning our growth capex forecast to reflect the rejection of the marketing step change and the updated connections forecast underpinning our Revised Final Plan.
IT	Accept	Accept	No change to AER's Draft Decision.
Meter Replacement	Accept	Accept	No change to AER's Draft Decision.
Augmentation	Accept	Accept	No change to AER's Draft Decision.
Telemetry	Accept	Accept	No change to AER's Draft Decision.
Other Assets	Accept	Accept	No change to AER's Draft Decision.
Escalation	Accept	Accept	We have applied minor changes to our real cost escalation forecast as a result of the other changes outlined in this table.
Overheads	Accept	Accept	We have applied minor changes to our overheads forecast as a result of the other changes outlined in this table.
Contributions	Accept	Accept	No change to AER's Draft Decision.

Note: In this 'traffic light' table, green shading represents the acceptance, orange represents a modification and red shading represents a rejection.

1.5 Summary

A breakdown of our Revised Final Plan capex forecast (updated for the items listed in Table 1.3), is provided in Table 1.4. Our Revised Final Plan capex forecast is \$556 million over the next AA period, which is \$2 million (or 0.4%) more than the AER's Draft Decision and reflects updated customer number forecasts.

Table 1.4: Breakdown of Capex Forecast (\$2017, million)

	2018	2019	2020	2021	2022	Total
Mains Replacement	33.8	35.8	35.8	33.4	8.6	147.3
Growth Assets	36.2	34.6	34.6	35.3	35.8	176.5
IT	11.5	24.2	16.5	5.2	6.1	63.5
Meter Replacement	7.5	7.5	7.5	5.0	5.0	32.6
Augmentation	9.3	12.0	7.4	3.5	2.1	34.2
Telemetry	0.3	0.3	0.3	0.3	0.1	1.2
Other Assets	4.7	6.5	11.5	8.1	4.0	34.8
Escalation	0.6	1.4	2.0	2.6	2.4	9.0
Overheads	11.6	11.9	11.8	11.3	10.8	57.4
Total Gross Capex	115.5	134.1	127.3	104.7	75.0	556.5
Contributions	1.4	1.4	1.4	1.4	1.4	6.9
Total Net Capex	114.1	132.7	125.9	103.3	73.6	549.6