

AER Gas distribution network tariff review

ENA Initial Perspectives

AER Public Forum

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Form of control: customer engagement and input in future reviews will be crucial

- » Critical issues for consideration in future reviews: need for engagement with gas network customers
- » Gas networks operate across a range of different market contexts that can make different arrangements suitable
- » As AER observes there are differences in the way risks are shared and managed under the different forms of control ('tariff variation mechanisms')
 - weighted average price cap
 - revenue cap
 - hybrid approaches
- » Customers should be thoroughly consulted on risk sharing preferences and consequences → best achieved through individual AA processes, rather than reaching any mandated national approach
- » Clear problem definition also key – are we primarily seeking to solve for:
 - revenue outperformance arising from demand forecasting
 - future amendments to NGO, and implications for the consumption signals from pricing
 - adaptation to jurisdictional policies and interventions



Gas demand: getting more complicated over time

- » Inherent uncertainty in forecasting by its nature → forecasts are independently reviewed & approved by AER as part of each AA
 - for each AA, networks take actual demand into consideration to improve forecasting accuracy
 - not clear that a form of regulation change “solves” a forecasting issue
- » Recent outperformance of forecasts driven by factors such as:
 - colder than average weather
 - impact of COVID-19 on consumption patterns
- » Increase in gas volumes equals lower prices for customers as costs spread over a larger customer base
- » It is not a safe assumption that forecasting risk has always been and will always be one-sided
 - it may be that gas demand (connections + volumes) becomes increasingly difficult to forecast, and this itself is likely to vary on a jurisdictional basis

Flexibility in tariff setting should be retained

- » Any potential changes to block structures should not be considered in isolation
- » To avoid unintended consequences, tariff reform should be reviewed in a broader context that considers the weighting of fixed vs. variable pricing, the split between residential and non-residential prices etc
 - the AA process is designed to facilitate this
- » Review should not unduly restrict the menu of potential tariff approaches that networks engage on with customers
 - diversity of market and operating conditions might give rise to different solutions on a network-by-network basis





Stranded asset risk and gas distribution network tariffs

- » Approaches outlined in AER Information Paper *Regulating Gas Pipelines Under Uncertainty* now being applied
- » Factors beyond form of regulation and pricing structures likely to drive presence and any realisation of stranding risks
 - unclear if a change to revenue caps would have any impact on stranding risks: empirical issue
 - however, it may be that flexible combinations of price and revenue capping arrangements such as ‘caps’ and ‘collars’ could assist manage risk exposures for consumers and networks
- » Different network circumstances (network type and conditions) mean stranding risks best addressed in proposals and decisions shaped by consumer engagement

Summary

- » AER correctly identifies the many balancing issues and trade-offs in play → no obvious 'one size fits all'
- » Review provides for a transparent and central discussion of the issues, but need to engage with different networks customers and circumstances suggests solutions best developed in individual reviews
- » Risk-sharing is also better addressed in interactive and longer-form engagements between networks and their customers, revisited across different AA periods based on developments
- » Likewise, flexibility around tariffs should be retained and not restricted where not required → focus should be on networks and customers being able to reach individual settlements and positions

