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## Victorian Transmission System Stakeholder Engagement Group. 2023-27 access arrangement (AA6).

### Roundtable 11 – First Look at regulatory positions – Q&A and discussion

26 October 2021



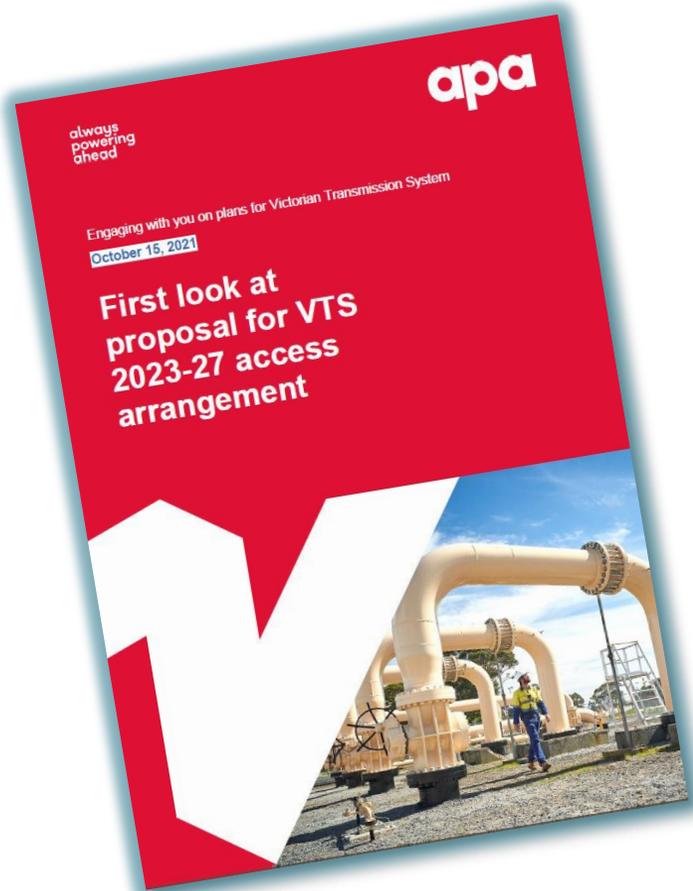
# Today's discussion & format

	Topics	Times
1	Welcome & Acknowledgement of Country	2.30 to 2.35
2	Format for today	2.35 to 2.45
3	Update on our thinking	2.45 to 3.00
4	What we heard from stakeholders and how we have taken them into consideration	3.00 to 3.15
5	Recap of key assumptions & revenue building block components & questions for stakeholders	3.15 to 4.10
6	Recap on revenue & tariff impacts & questions for stakeholders	4.10 to 4.25
7	Next steps	4.25 to 4.30

**Note that the meeting will be recorded to assist updating issues register.  
Video will not be distributed outside of APA.**

**Purpose of today's discussion is to consult & involve.  
We do encourage your views and feedback today**

# We'll be going through the First Look consultation document



- We sent you the First Look document on 15 October
- At the same time, we sent the Oakley Greenwood *Issues Affecting Demand and Supply for Gas on the Victorian Transmission System. Final Report*
- We sought to address further issues raised in Roundtable 10 including cost allocation method
- Today, we are seeking to get your views on the positions proposed in the First Look document.

# Update on our thinking

**We met with AER staff to discuss VTS First Look consultation document**

**We were seeking early guidance and feedback on draft positions to ensure 'no surprises'**

## **Our key take-outs:**

- AER Board attuned to taking prudent measures now to alleviate stress in the future
- Prudent measure may be to propose shortening of asset lives (resulting in accelerating depreciation of the asset base)
- Asset lives can be reviewed at each access arrangement review to consider changes that extend economic lives of assets such as repurposing of pipelines for hydrogen
- It will be difficult to reconcile a larger capital expenditure program with an aggressive depreciation proposal
- Our idea to remove indexation of the regulatory asset base is unlikely to be accepted as compliant
- Price stability is favoured rather than price shocks
- We need explicit and transparent with stakeholders and the AER
- We wish to use R11 to get stakeholder position on preferred principles and positions.

# What we heard from stakeholders and how we have taken them into consideration

# Replay what we heard from stakeholders and how we have taken them into consideration

## What we heard

- Energy affordability and tariffs need to keep in mind the supply chain
- Solving short-term problems with long-term investment solutions
- Inter-generational fairness considered in energy transition and recovery of economic costs
- Seeking assurance that cost allocation between APA regulated and unregulated assets is fair and reasonable
- Seeking assurance that forecast costs are efficient, fair and reasonable
- Range of views about hydrogen with stakeholders considering there was merit in an assessment being undertaken but concerns centred on the cost and who should fund such an assessment.



## Our proposed position

- Investing under policy uncertainty means we need to be more flexible and have a greater focus on minimising expenditure
- Minimise expenditure by incremental approach to investing in South West Pipeline (recognising that demand management option is not available to APA)
- Replacement/ stay-in business expenditure upgrades to equipment components rather than replacement of asset (such as compressor units)
- Start to transition tariffs in line with reduction in demand by shortening lives of assets (new and old assets)
- Following Energy Minister’s September announcement indicates that a hydrogen capability assessment is required on safety and integrity grounds
- If there are policy changes or the VTS is repurposed then the depreciation profiles can be changed at each five-year access arrangement review.
- We will not be proposing a removal of indexation of regulatory asset base – be we are considering shorter asset lives.

No.	Questions for stakeholders
2	Do you have any comments on the summary of what we heard and how were have considered your feedback? In particular, should we give more or less emphasis to key themes that have emerged?

# Benefits to customers and consumers

Draft VTS access arrangement proposal seeks to balance trade-offs between competing factors

## **Affordability and a secure and reliable supply**

Keeping tariffs as low as possible while maintaining safety, security and reliability of the VTS.

## **Orderly transition**

Starting to transition VTS tariffs early to prevent future price shocks as energy sector transitions to lower carbon energy sources.

We are concerned that any future price shocks would have a more concentrated impact on those in vulnerable circumstances and hard to abate customers.

## **Critical infrastructure**

Maintain system security by safeguarding critical infrastructure against threats in line with obligations under Security of Critical Infrastructure framework and do this in an efficient and proportionate way.

# Recap of key assumptions & revenue building block components & questions for stakeholders

# Questions for stakeholders on key assumptions

## Demand and supply forecasts

Oakley Greenwood was engaged to make sense of demand and supply factors likely to impact Victoria and the VTS

We accepted Oakley Greenwood findings but did not include Port Kembla Import Terminal in supply as the project has not yet reached Final Investment Decision.

No.	Questions for stakeholders
5	Do you have any comments on the adjustments APA has made to the AEMO GSOO analysis and graphs?
6	Do you accept that the SWP expansion would be prudent to meet the demand requirements as we know them today? What timing might you suggest for that project?
7	Do you have any views about the long term supply term supply adequacy for Victoria?

## Decarbonisation and depreciation

Key theme throughout this access arrangement consultation process is the Victorian Government’s Net Zero 2050 initiatives and their impact on future gas consumption levels

Propose to start addressing this by transitioning tariffs in tandem with reduction in demand by shortening lives of assets (new and old assets)

We will not be proposing removal of indexation from the asset base.

No.	Questions for stakeholders
8	Do you have any comments on APA’s proposed approach to risks of decarbonisation by using accelerated depreciation and removing indexation of the regulatory asset base?
9	Do you have views about measures to facilitate orderly transition to meet Victorian Government policy?

# Questions for stakeholders on key assumptions

## Security of Critical Infrastructure

We are undertaking bottom-up and top-down modelling to work out the ranges and sensitivity analysis on the category of criticality.

APA is strongly focused on SOCI - APA is an ASX listed company and faces the intense scrutiny by investors. Substantial proportion will be borne by APA security holders.

APA CAM used to calculated VTS share of costs.

No.	Questions for stakeholders
11	Do you have any comments about APA's SOCI requirements?
12	Do you have any suggestions for cost allocation principles related to SOCI?

## APA cost allocation method for regulated assets

APA's approach to cost allocation is set out the Cost Allocation Methodology (CAM) document prepared for APA regulatory reporting purposes.

CAM principles - costs are not allocated more than once; costs cannot be treated as a directly attributed cost and other directly attributable cost; and costs are allocated on a causal basis, in instances where direct attribution is not possible.

Where costs are not directly attributable, they are allocated among the APA businesses on a revenue basis.

No.	Questions for stakeholders
10	Do you wish to know more about APA's Cost Allocation Method?

# Questions for stakeholders on expenditure forecasts

**Draft proposed total capital expenditure for 2023-2027 of \$343.4 million is 21% higher than the total capital expenditure for the current period.**

**Replacement expenditure**

The replacement program and projects are integral to maintaining and improving safety, security and reliability of transmission services. Replacement expenditure is forecast to be \$152.8 million compared to \$73.7 million in the current period. This represents a \$79.1 million (or 107%) increase forecast for the next period. Largely driven by asset integrity and encroachment.

Ent	
13	Do you have any comments about APA's replacement capital expenditure proposal?

**South West Pipeline**

APA is proposing a staged approach to invest in the SWP to balance the need for system security with concerns that the situation on the SWP was a short-term problem.

SWP\_570 is estimated to cost \$71 million (plus overheads).

Questions for stakeholders	
14	Do you have any comments about APA's proposed approach to the investing in the SWP?
15	How will you or your customers be impacted by the proposed SWP?

**Western Outer Ring Main**

The Western Outer Ring Main (WORM) was proposed by APA (and supported by AEMO) for the 2018-22 access arrangement period capital program to address tightening of supply / demand balance forecast.

Total cost forecast to be \$185 million over current and next access arrangement periods.

Questions for stakeholders	
16	Do you have any comments about the WORM project?
17	How will you or your customers be impacted by the WORM?

# Questions for stakeholders on expenditure forecasts

## Hydrogen safety and integrity assessment

In August 2021, Energy Ministers agreed to amend the National Gas Law, National Energy Retail Law so hydrogen blends, and other renewable methane gas blends are within the national energy regulatory framework. APA considers that there is a need to undertake a technical assessment to understand the safety and integrity impacts of hydrogen on the VTS. Estimated cost is \$37.9 million.

### Questions for stakeholders

- 18 Do you have any comments about the proposed assessment for hydrogen?
- 19 Do you have any views about the role of hydrogen in meeting future energy needs?

## Transformation & Technology

APA is undergoing a review of the corporate Transformation and Technology (T&T) program to replace legacy systems that need to be replaced. VTS is allocated a cost of the T&T budget based on a cost allocation method using a revenue allocation. This allocation is 8.21% of total corporate costs.

### Questions for stakeholders

- 20 Do you have any comments about the proposed Transformation and Technology plans?

## Operating expenditure

We have applied the AER's preferred base-step-trend approach to operating expenditure forecasting, using a 2020 base year (the last complete year at time of writing), as reported to the AER in response to the 2020 Annual Reporting Regulatory Information Notice. At this stage we have forecast that ongoing operating expenditure will remain flat in real terms from the 2020 levels

### Questions for stakeholders

- 21 Do you have any comments about the proposed approach to operating expenditure forecasts?

# Recap on revenue & tariff impacts

# Forecast VTS tariff scenario testing

## Some insights from the scenario testing:

- The impact of capping asset lives at 25 years is about 5¢/GJ
- The impact of stopping indexation of the capital base is about 14.5¢/GJ
- The impact of undertaking the SWP\_570 expansion is about 0.4¢/GJ
- The impact of undertaking the VTS hydrogen capability assessment is about 1.8¢/GJ.

Table 3 VTS scenario analysis of tariff impacts

Scenario	Pipeline asset life (years)	Index asset base	SWP570 security expand	Hydrogen assess.	Composite tariff	Change from base case	Change from base case (%)
<b>Base case</b>	55	Yes	Yes	Yes	0.5976		-
<b>Scenario 1 - shorter lives</b>	25	Yes	Yes	Yes	0.6493	0.0517	8.7%
<b>Scenario 2 - no indexation</b>	55	No	Yes	Yes	0.7423	0.1447	24.2%
<b>Scenario 3 - Without SWP570</b>	55	Yes	No	Yes	0.5940	-0.0036	-0.6%
<b>Scenario 4 - Without Hydrogen</b>	55	Yes	Yes	No	0.5791	-0.0185	-3.1%

## No. Questions for stakeholders

3 Do you have any comments about tariff scenario analysis?

## Next steps

- **First Look consultation paper**
  - Send your comments by 8 November
  - Get in touch if you wish to meet to discuss
  
- **Next roundtable proposed**
  - Roundtable 12 How you shaped our thinking on the
  - VTS regulatory proposal
  - Proposed for Wednesday 17 November.

**Thank you for participating today!**



# Timetable

Phase 3 - Putting the plans together			
15-Oct-2021	Consultation	APA release APA VTS early consultation document	Involve
25-Oct-2021	Roundtable 11	Early consultation proposal - Q&A session	Involve
11/10/2021 to 22/10/2021	Consultation	Opportunity for one on one meetings with stakeholders	Involve
TBA	Placeholder	Follow-up on any outstanding issues & updates	Involve
8-Nov-2021	Consultation	Submissions to APA on early consultation document	
17-Nov-2021	Roundtable 12	How you shaped our thinking on the VTS regulatory proposal	Involve
01-Dec-2021	Submission	APA VTS regulatory proposal submitted to AER	
09-Dec-2021	Feedback session	Post lodgement review and feedback on VTS engagement	Involve
TBA	Further roundtables	Proposed during the regulatory process	

**For further information**

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