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Mr Geoff Houen
Gas Market Development
National Energy Market Branch
Department of Resources, Energy and Tourism
GPO Box 1564
CANBERRA ACT 2601

By email: MCEMarketReform@ret.gov.au

Dear Mr Houen

Response to SCO Draft Policy Position: National Framework for Connection of Retail Customers to Gas Distribution Networks

Thank you for the opportunity to comment on the Draft Policy Position for the *National Framework for Connection of Retail Customers to Gas Distribution Networks* released by the Ministerial Council on Energy Standing Committee of Officials (SCO) on 2 September 2009.

ActewAGL Distribution's response to the Draft Policy Position is provided in the attached submission. We are keen to participate in ongoing consultation on the framework and to respond to the second exposure draft of the National Energy Customer Framework when it is released later this year.

Please contact Alexandra Curran, Senior Regulatory Advisor, on (02) 6248 3190 if you would like to discuss any aspect of our submission.

Yours sincerely

David Graham
Director Regulatory Affairs and Pricing

National Framework for Connection of Retail Customers to Gas Distribution Networks

ActewAGL Distribution response to MCE
Standing Committee of Officials
Draft Policy Position

September 2009

1. Introduction

ActewAGL Distribution welcomes the opportunity to respond to the Ministerial Council on Energy Standing Committee of Officials (SCO) Draft Policy Position on the National Framework for the Connection of Retail Customers to Natural Gas Distribution Networks.

ActewAGL Distribution is Australia's first multi-utility to offer electricity, natural gas, water and wastewater services. ActewAGL Distribution's gas network connects to around 107,000 customers in the ACT and the surrounding region. The electricity network connects to approximately 156,000 customers in the ACT.

SCO's proposed gas connections framework would be a stand alone regulatory arrangement that applies to covered and uncovered gas distribution networks. The framework would apply alongside the national gas access regime, and is intended to complement the access regime.

ActewAGL Distribution has several concerns with the framework set out by SCO in the draft policy paper. The proposed framework increases the scope and complexity of gas network regulation. For example, it involves regulation of networks that are uncovered under the access regime and it involves an additional layer of regulatory approval for covered networks, with the proposed requirement for AER approval of connection charges. ActewAGL Distribution believes that SCO should carefully assess the costs and benefits of the proposed framework, address the potential for overlap and inconsistency with the existing access regime, and consider more light-handed options. These matters and other elements of the proposed framework are discussed in the following sections.

2. Application of the framework

SCO's draft policy position is to apply the national gas connections framework to both covered and uncovered pipelines. SCO says that this is necessary to complement the obligation to supply placed on all retailers by the National Energy Retail Law (p. 6).

ActewAGL Distribution notes that the determination of a pipeline as covered or uncovered is a central element of the access regime. A detailed coverage test is applied to ensure that regulatory intervention occurs only in those circumstances in which it is likely the benefits of regulation outweigh its costs.¹ In 2006 the MCE raised the threshold for coverage by adding a further requirement to the coverage test. The MCE noted that "the adoption of this change should ensure that only pipelines with substantial market power will meet the test for coverage, thus lessening the chances that formal price control is imposed where it is not absolutely necessary".²

¹ Productivity Commission 2004, *Review of the Gas Access Regime*, p. 198.

² MCE 2006, *Review of the National Gas Pipelines Access Regime - Decision*, May, p. 10.

ActewAGL Distribution believes that SCO's proposal to regulate uncovered pipelines under the connections framework should be subject to a more detailed examination of costs and benefits. SCO's justification for applying the framework to uncovered pipelines is that it is necessary to support the obligations of retailers. However, ActewAGL Distribution believes that SCO should examine whether within the connections framework more light-handed requirements may be warranted for uncovered pipelines, for example in relation to approval of connection charges. This should help to ensure that regulation is only applied where and as necessary, consistent with the MCE's intention in relation to access regulation.

3. Connection definitions and approvals

SCO proposes three connection types: basic, additional standardised and negotiated. The framework would require the distributor to provide the basic connection service, which is intended to cover most small customer connections, and would be defined by the distributor and approved by the AER. The basic connection service is intended to involve a simple application and connection procedure. Additional standardised connections could also be defined by the distributor and approved by the AER for other types of standard connection not covered by the basic connection. Negotiated connections would be determined using the negotiating framework set out in the draft position paper.

ActewAGL Distribution is concerned that the proposed arrangements involve some areas of overlap, and potential for inconsistency, with the requirements under the access regime. The key area for concern is the proposal for the AER to approve the connection schedule, including prices (discussed below). A further concern is the proposed treatment of negotiated connections. SCO proposes to include a new negotiating framework in the connections framework. SCO does not address whether and how the new framework will complement the negotiating framework provisions in the National Gas Rules (NGR). ActewAGL Distribution believes that any new negotiating framework needs to be consistent with the existing requirements. Negotiated connections are discussed further in section 6 below.

3.1 AER approval of connection schedule and prices

SCO proposes that for basic and additional standardised connections, distributors must develop a schedule that specifies what is to be provided to the customer, timeframes for various stages to complete the connection and any charges to be paid by the customer. The AER would approve this schedule on the basis that it provides a reasonable level of service, having regard to the National Gas Objective, the distributor's historical practices and the geographical nature of the network.

The schedule would then become part of the standard distribution contract that is deemed under the National Energy Customer Framework (NECF) when the customer makes a connection application. Minor variations to the basic and additional service could be made with an itemised quote provided to the customer.

SCO says in relation to the approval process that it “considers it important the customers know the details and nature of the connection services that are being offered by a distributor” (p. 8).

ActewAGL Distribution agrees that providing information for customers is important. However, we are concerned that the proposal to have the AER connection approval process operate in addition to the AER approval of the access arrangement for covered pipelines creates unreasonable uncertainty for distributors and customers, as well as additional costs. As noted in the Energy Networks Association (ENA) response to the draft policy position, SCO indicated at the workshop on the proposed framework that it expects that if the AER has already approved the access arrangement then approving the proposed basic connection service should be relatively straightforward.

However, ActewAGL Distribution considers that there are some important differences between the access arrangement approval process and the proposed approval process in the connections framework, and the practical implications of these should be addressed. For example, the criteria for assessing connections proposals (that they provide “reasonable levels of service”) are different from the criteria for approval of access arrangement proposals, as set out in the NGR and National Gas Law (NGL). In addition, under access arrangements connection charges are not specifically levied. Most connection costs are recovered through reference tariffs for reference services. The only charges for connections are capital contributions for connections that are non-economic. These are determined in accordance with the NGR and are specific to the customer and connection characteristics.

SCO’s proposal to require AER approval of prices for the basic and additional standardised services provided by *uncovered* pipelines is also inconsistent with the NGL, particularly the National Gas Objective and the coverage criteria.³ As noted in section 2 of this submission, the purpose of the coverage test is to help ensure that regulation is only applied where absolutely necessary. SCO has not established that there is a case for requiring approval of connection charges for uncovered pipelines.

ActewAGL Distribution agrees with the ENA’s comment that it may be more appropriate for the AER to have a monitoring and compliance role rather than an approval role. The case for monitoring, rather than approval, is particularly strong for uncovered pipelines.

If some AER approval role is determined to be necessary, the option of the AER approving a schedule of services and timelines, but not approving associated charges should be considered. Charges would be either calculated in line with the access arrangement (for covered pipelines) or set in a competitive market (for uncovered pipelines). Therefore, the AER could regulate and standardise the service, without approving charges. This is a second best option to excluding unregulated pipelines from the framework altogether recognising that they have an incentive to provide appropriate services to customers.

Alternatively, for covered pipelines the NGR could be amended to require the service provider to include in its access arrangement a connections policy that sets out the things that the connections framework requires (timeframes etc) and is approved at the same time as the

³ See section 97 of the NGL, as well as sections 15 and 23.

access arrangement. This would integrate the connections framework into the access regime and ensure there is no separation between requirements arising from the AER's approval role for basic and additional standardised connection services, and those envisioned under the approved access arrangement.

3.2 Connection charges and capital contributions

SCO says in the draft policy position paper that where the cost of an individual customer connection is evaluated to be more than the amount provided for in the distributor's standard charges, then the distributor can recover additional costs of the connection from that customer (but not other customers). (p. 9)

ActewAGL Distribution is concerned that this proposed approach is different to the current approach under the access regime where customer connections are evaluated as to whether they are economic, taking account of the required network expansion to connect the customer. In many cases the cost of connection to the customer is zero as they are deemed economic connections.

The draft policy approach appears to expect the distributor to define a standard connection and cost (say a 10 metre service line and standard meter), and any connection longer than that be subject to a contribution. Under this approach it appears likely that more customers would have to pay contributions, even where connections are economic, than currently do, which would adversely impact the competitiveness of gas. The proposed approach also appears inconsistent with the access regime, which has a test for market expansion – the incremental revenue test.⁴

SCO says that its intention is for the gas connection framework to complement the national gas access regime. ActewAGL Distribution supports this intention. However we are concerned that the proposed approach to connection charges, as set out in the draft position paper, does not achieve this. This is discussed further in section 7 below.

4. Applications for connection

SCO's draft policy framework would specifically allow end-use customers to apply directly to the distributor for connection. Third parties, such as retailers or gasfitters, may facilitate connections and apply on behalf of customers, but it would not be mandatory for them to do so, and the customer would be deemed to be making the application.

ActewAGL Distribution notes that allowing end-use customers to apply directly to the distributor will involve additional costs for some distributors, where systems must be set up to handle connection applications from the general public, rather than using business-to-business arrangements with retailers. In practice, most customers are likely to prefer an intermediary to arrange the connection. SCO's proposal to allow applications from

⁴ NGR 79(2)(b)

intermediaries to be deemed as being made by the customer is important in facilitating the role of intermediaries. However, to accommodate those customers that choose to arrange the connection directly, additional costs will be borne by some distributors and these costs of implementing the new framework will need to be recovered from customers.

SCO does not address these additional costs, or other costs associated with the transition to a new gas connections framework, in the draft policy position paper. Depending on the cost pass through provisions in their access arrangements, some distributors may have scope to pass through costs associated with regulatory changes introduced during the current regulatory period. However, to avoid uncertainty about how transitional costs will be handled, ActewAGL Distribution supports the ENA's proposal (as set out in its response to the draft policy position) that the transition to the new connections framework be made at the time of the regulatory reset.

5. Contractual arrangements

The proposed gas connections framework would establish model connection terms and conditions that will be part of the National Energy Customer Framework's (NECF's) standard distribution contract. The NECF will require distributors to adopt a deemed standard distribution contract based on the model terms and conditions. (p. 12)

The approach of having a deemed standard distribution contract, as required under the NECF, is supported by ActewAGL Distribution. However the NECF limits its application to covered pipelines. Uncovered pipelines are only included under the NECF by Ministerial nomination. Section 103 of the National Energy Retail Law, first exposure draft, defines a distributor as:

- (a) a service provider within the meaning of the NGL who owns, operates or controls a distribution pipeline that is a covered pipeline under the Law; or
- (b) a nominated distributor, to the extent provided by section 112.

Section 112 says the Minister of a participating jurisdiction may nominate a distributor.

The legal basis for SCO's proposal for all pipelines, covered and uncovered, to have standard connection services approved, and part of the deemed distribution contract, therefore needs to be clarified by SCO.

6. Negotiation framework

SCO proposes to include in the gas connection framework a streamlined negotiation framework for customers requiring a negotiated connection. Negotiated contracts may be required to meet minimum content requirements specified in the relevant rules.

ActewAGL Distribution notes that SCO is “in the process of developing the negotiating framework” and “will consider specifying minimum content that should be addressed in any negotiated connection contract developed under the proposed framework”. (pp. 14-15)

ActewAGL Distribution will respond when these details are developed and released. Our initial observation is that the relevant provisions of the existing access regime need to be taken into account when any additional negotiating framework or requirements are developed.

The gas access a regime is a negotiate-arbitrate regime. It includes basic provisions for handling requests for access, including information provision. The connections framework need not and should not circumvent these.

In addition, the access regime contains no provisions on the appropriate conduct of negotiations for services other than reference services. It is not appropriate to introduce a negotiating framework for one aspect of pipeline services, and it is arguably inappropriate under the formulation of the gas access regime. Negotiated services are covered by existing access arrangements, albeit in a limited way, reflecting the intent of the regime.

7. Treatment of connection assets for capital contributions

SCO acknowledges that the costs of connection for some customers may be more than the approved charge. In these cases the customer may opt to pay an additional charge for the connection to proceed. For regulated pipelines, the additional charge would be required to be no more than the amount needed to make the connection economic. The same would apply to customers seeking negotiated connections (pp 17-18).

The proposed charging arrangement appears to correspond to a capital contribution. However, it is not clear how this relates to the capital contribution requirements under the NGR. SCO says that the proposed treatment of connection assets does not otherwise change the arrangements for user capital contributions under the NGR (p. 16).

ActewAGL Distribution is concerned that rather than complementing the access regime, as is SCO's intention, the proposed arrangements for connection charges appear to result in a dual charging arrangement, with customers potentially charged under both the access arrangement and the connection framework. The proposal set out in the ENA's response to the draft policy position addresses this problem by recovering capital contributions outside the access arrangement. The standard distribution contract would provide for a charge to be levied where a connection is uneconomic and the customer agrees that the work be undertaken. ActewAGL Distribution supports this proposal.

8. *Dispute resolution*

SCO's draft policy position is that a single dispute resolution process be established for the NECF, which will also cover the gas connections framework (p. 19).

ActewAGL Distribution notes that the NGL and NGR include dispute resolution provisions applying to covered pipelines. While SCO has identified the need for a single process under the NECF for dealing with gas and electricity connection disputes, it is also important to consider whether and how the proposed arrangements should operate in parallel with existing dispute resolution arrangements in the NGR and NGL. It would not be appropriate for covered pipeline service providers to be subject to dual dispute resolution schemes.