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Multinet Gas

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Dear David

**Re: Review of Unaccounted for benchmarks**

Multinet is pleased to respond to the Essential Services Commission (ESC) draft decision. The ESC will be aware that Multinet has already made a submission, dated 21 April 2017. We note that the ESC has not made that submission available on the website. We would prefer if that submission was made public by the ESC. That submission provides our view on how the benchmarks should be established. The ESC should refer to that submission together with the comments made below:

**1. Multi-year approach to setting the benchmark**

When setting the benchmarks for the 2013 to 2017 period the ESC used an average of 3 years data to establish the base year amount. We concur with this approach and believe the ESC should adopt this approach for when setting the 2018 to 2022 benchmarks. We believe that three years is an appropriate number of years that balances off current performance with historical performance to create a benchmark that is relevant and provides the appropriate incentives.

Our view is that the ESC should use the most recent available data – this being the 2014 to 2016 period. In Multinet's case 2014 data is settled, 2015 data (to be provided to AEMO by 30 June 2017) and is capable of being settled. 2016 data is available at the aggregate level and is subject to minimal changes.

The ESC has proposed only using settled data. We accept that this is simple and administratively the easiest. The ESC's task is not to set benchmarks that are simple it is to set benchmarks that are consistent with the Rules that govern the Industry. Specifically we consider that the benchmarks need to meet the Revenue and Pricing Principles (RPP) set out in section 24(2) of the National Gas Law (NGL), which provides that:

*A service provider should be provided with a reasonable opportunity to recover at least the efficient costs the service provider incurs in –*

- a. providing reference services; and*
- b. complying with a regulatory obligation or requirement or making a regulatory payment.*

In establishing the 2018 to 2022 UAFG benchmarks the Commission must also have regard to its objectives set out in sections 8 and 8A of the Essential Services Commission Act 2001 (ESC Act).

In particular, section 8 provides that the ESC must:

- (1) *In performing its functions and exercising its powers ... promote the long term interests of Victorian consumers.*
- (2) *Without derogating from subsection (1), in performing its functions and exercising its powers in relation to essential services, the Commission must in seeking to achieve the objective specified in subsection (1) have regard to the price, quality and reliability of essential services*

Section 8A of the ESC Act further provides that the ESC must, in making decisions, have regard to the following matters:

- (1) *In seeking to achieve the objective specified in section 8, the Commission must have regard to the following matters to the extent that they are relevant in any particular case—*
  - (a) *efficiency in the industry and incentives for long term investment;*
  - (b) *the financial viability of the industry;*
  - (c) *the degree of, and scope for, competition within the industry, including countervailing market power and information asymmetries;*
  - (d) *the relevant health, safety, environmental and social legislation applying to the industry;*
  - (e) *the benefits and costs of regulation (including externalities and the gains from competition and efficiency) for—*
    - (i) *consumers and users of products or services (including low income and vulnerable consumers);*
    - (ii) *regulated entities;*
  - (f) *consistency in regulation between States and on a national basis;*
  - (g) *any matters specified in the empowering instrument.*

*Without derogating from section 8 or subsection (1), the Commission must also when performing its functions and exercising its powers in relation to a regulated industry do so in a manner that the Commission considers best achieves any objectives specified in the empowering instrument.*

Our experience in settling UAFG is that it can take up to seven months for final settlement and for all parties to agree. For example when settling 2014 actual UAFG results we provided AEMO the necessary data and files in the last week of November 2015. It was finally settled with all parties on 16 June 2016. Importantly the first file we provided to AEMO in late 2015 provided a UAFG calculation of 4.97%. The settlement some seven months later settled for 4.95%. This highlights the accuracy of our data and the slowness of the actual settlement process.

If that occurred for the 2015 settlement under the ESC approach 2015 data would not be included in the benchmark process. We would maintain that the data we provide for 2015 is materially accurate.

The hold up with the settlement process is with the retailers and how much we pay them. Any negotiations with retailers does not change our overall settlement amount – it is merely a redistribution amongst retailers. Multinet should not be penalised for not having settled data.

If the ESC advocates an approach that it only uses settled data; for 2015 data (and forecast 2016 data) it is in the retailers interest to actively pursue a strategy of not settling the data in order for Multinet to have

a lower benchmarks for the 2018 to 2022 period. This “incentive” provided to the retailers by the ESC would penalise Multinet through no fault of our own and also fail the Rules requirements set out above. There are currently no obligations on the retailers to respond in a timely manner.

## **2. Adjustments to the benchmarks including efficiencies**

On one hand the ESC proposes to set aside within period adjustments to benchmarks for the pipe works replacement and pipe condition yet on the other hand proposes to amend the benchmark for so called efficiencies. Our earlier submission proposes that adjustments be made for all of the matter outlined above. Our view is that this is consistent with good regulatory practice and is symmetrical in nature i.e. it considers both improvements and decrements to the benchmarks.

Given the materiality of the adjustments Multinet does not object to setting aside all adjustments to the benchmarks, including efficiencies.

## **3. UAFG price**

Our view is that the Gas Distribution Code (GDC) should include not only a benchmark percentage, it should include the benchmark price for the 2018 to 2022 period. Better still AEMO should be directed by the ESC via a specific change to the GDC to determine the price of the X price factor in accordance with the GDC or for there to be no reconciliation payment obligation on distributors relating to price.

Distributors are not in a position to hedge against the gas market wholesale price. This is clearly best left to retailers who manage this price risk on a daily basis as part of their normal business, this is also consistent with the treatment of losses in electricity which are paid for by retailers. Distributors would incur additional cost that would not be considered prudent or efficient.

The GDC also refers to Schedule 1 Part C for UAFG benchmarks and settlements process. The reconciliation process requires a gas spot price to be calculated, the X term, i.e. the quantity annual price of Gas, using spot and contract prices and quantities, as determined by AEMO for the previous calendar year expressed in dollar per gigajoule. To determine the UAFG reconciliation amounts owing, AEMO must be able to provide the quantities and the cost of contracted gas by the retailers and the quantities and cost of the deviation amounts of gas settled on the market and be in a position to calculate a relatively stable gas price based on retailers gas supply contracts.

The current AEMO procedures in our view are not consistent with the setting of the UAFG benchmark in Victoria which rely solely on within day spot gas spot price which is influenced by retailers forecasting accuracy. The setting of the gas UAFG benchmark is to incentivise a distributor to ensure that gas leakage is minimised and if the benchmark is set correctly the benchmark should have an equal chance of being exceeded or not and a flat gas stable gas price reflects the penalty or reward to the distributor.

The ESC process suggests that UAFG is a benchmark gas percentage, is an incentive and also refers to efficient management of the network and efficient costs etc. The GDC requires a distributor to use reasonable endeavours to ensure that the quantity of unaccounted for gas in its distribution system for any year as a percentage of the aggregate quantity of gas received by the Distributor at transfer points into its distribution system in that year is less than the benchmark. As stated in the ESC paper, the quantity of gas as a volume is the distributor obligation and the various sources of gas, heating value measurement and flow weighted discrepancies, averaging or profiling of basic metered customers etc. all lead to errors over which the distributor has no control. The calculations in Part C refer to a quantity of energy and not a quantity of gas. As gas sources have changed over time and AEMO have amended the price calculation to be market based, the distributor is worse off 70% of the time as AEMO have

deemed the within day loss of gas and within day price to be an accurate setting of UAFG. There is no evidence that this is the case noting that of the 5 factors the ESC describes the distributor has some limited control over emissions and only some control over two other areas, metering and theft. The AEMO approach prescribes an accuracy of gas losses and energy in what the ESC suggest is a very uncertain measurement of volume of gas and energy which is inappropriate and unsubstantiated.

The GDC amendments should require AEMO to determine the X price factor in accordance with the GDC or for there to be no reconciliation payment obligation on distributors relating to price.

#### **4. Other matters**

The GDC clause 2.4 (b) requires the gas distributor to provide written notice to AEMO by 30 April each year of the gas withdrawn. This clause should be deleted as AEMO is not in a position to provide CTM and hourly metered customer data until around June each year for the preceding year. Distributors and retailers then agree data and AEMO is provided with the agreed settled data for invoicing. If this clause were to remain it should refer to settled data to AEMO not for the previous year but to the year prior to that i.e. t-2 by 30 April.

ESC is aware that the timeframe in the GDC is unable to be met and it would be beneficial if the date was removed or amended to a more realistic timeframe such as 30 April for settlement of the two year prior data.

Any queries should be directed to me.

Yours sincerely



Andrew Schille  
**General Manager Regulation, Multinet**