

28 May 2013

Wagga Wagga Revocation
National Competition Council
Level 21, 200 Queen Street
Melbourne VIC 3000

By email: gas@ncc.gov.au

Dear Sir/Madam,

RE: Application for revocation of coverage – Wagga Wagga natural gas distribution network

The Energy Retailers Association of Australia (ERAA) welcomes the opportunity to comment on the *Application for revocation of coverage – Wagga Wagga natural gas distribution network* (the Application).

The ERAA represents the organisations providing electricity and gas to almost 10 million Australian households and businesses. Our member organisations are mostly privately owned, vary in size and operate in all areas within the national electricity market (NEM) and are the first point of contact for end use customers of both electricity and gas.

The ERAA does not support the Application from Envestra Limited (Envestra) for revocation of the Wagga Wagga natural gas distribution network. Approval of the Application would introduce a risk that network users could face inefficient tariffs, terms and conditions. The ERAA believes that the Wagga Wagga network does indeed satisfy criterion (a) – (d) of section 15 of the National Gas Rules, and thus a revocation of coverage would not serve the National Gas Objective.

Criterion (a)

The ERAA does not agree that Envestra has a strong incentive to increase throughput on the network. Envestra claims that this will lower the unit cost for access to the network, making gas more competitive when compared to alternate fuel sources.¹ Envestra's pricing strategy is instead likely to be driven by a desire to maximise rents. When the prices and conditions of monopoly businesses are not subject to sufficient regulatory oversight, there exists a risk that competition will decrease materially.

The Application does not provide sufficient details outlining how and why customers could substitute their current gas use with alternative sources of energy. The Application states that appliances are easily replaceable with electricity appliances;² however the up-front costs of doing so are not specified. Purchasing electricity appliances can be expensive. Also, it may be difficult to sell second-hand gas appliances in a market where customers are transitioning from gas use to electricity use. In the case of large customers, building new pipeline infrastructure would require significant capital investment.

The Application argues that in many respects Liquid Petroleum Gas (LPG) can be used as a direct substitute for natural gas.³ This is not consistent with the experiences of the ERAA's members. Customers are unlikely to use LPG bottles to fuel the activities currently fuelled by

¹ Envestra (2013), *Wagga Wagga Network Revocation Submission*, p.35

² Ibid, p.17

³ Ibid, p.19



natural gas. Even if they were to be used, the impracticality of LPG would be included in any calculation of substitution costs.

While some customers face investment decisions that make reticulated natural gas substitutable for them, this will not be the case for all customers. Many Wagga Wagga residents live in rental properties. Renters face barriers to installing new appliances as they will not necessarily reap the full benefit from their investment. These split incentives mean that some up-front investments would have to be recovered over the life of the expected rental term. Even where customers own their own property, many will still be unable to afford the up-front costs, meaning those who can least afford to switch will continue to pay higher prices.

Criterion (d)

To satisfy criterion (d), it must be demonstrated that access to services is not contrary to the public interest. Envestra estimates expected coverage costs to be \$2,800,000, and states that these costs are incurred for negligible benefits. As outlined below, the ERAA argues that access provides benefits that are sufficiently significant so that it could not be reasonably argued they do not outweigh costs, and thus are not in the public interest. The ERAA encourages the National Competition Council (NCC) to assess the claims made in the Application that these access arrangement review costs are largely independent of the size of the network.

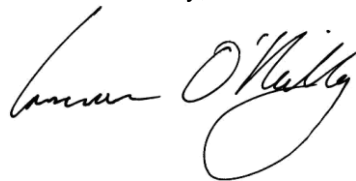
As outlined above in response to criterion (a), the current regulatory arrangements ensure increases to tariffs relate to the revenues needed to cover efficient costs and provide a commercial return on capital, as determined by the Australian Energy Regulator (AER). Any savings from the removal of these arrangements won't necessarily lead to savings in the long term. Given the barriers to fuel substitution, the ERAA considers the potential for prices to rise above efficient levels to be a material risk if revocation of the network is approved.

In additions to costs, conditions of access are equally important. While tariffs may be relatively comparable, terms and conditions may transfer risk to network users who cannot efficiently manage this risk. If the terms and conditions are less clear, they may be accompanied by a reduction in accountability to retailers and customers. The ERAA notes that some previous proposals by Envestra to impose certain terms and conditions on users of its South Australian and Queensland networks were not approved by the AER.

Under the current regulatory arrangements retailers and customers are able to participate in determination processes, ensuring that regulated monopolies and the AER are informed of consumer preferences. The AER's Better Regulation program is currently seeking to strengthen these arrangements so that customers' interests are better incorporated into regulatory pricing decisions. Similarly, the formation of a Consumer Challenge Panel will provide customers with the opportunity to advise the AER on issues that are important to them. While Envestra has indicated it will 'engage with retailers to determine a mutually agreeable set of terms',⁴ this intention is not sufficient to show that criterion (d) is not satisfied. Should the Application be approved, the ERAA would not be confident that retailers, customers and Envestra would be able to achieve an efficient outcome price and service outcome.

Should you wish to discuss the details of this submission, please contact me on (02) 8241 1800 and I will be happy to facilitate such discussions with my member companies.

Yours sincerely,



Cameron O'Reilly
CEO
Energy Retailers Association of Australia

⁴ Ibid, p.34