REPORT OF PROCEEDINGS BEFORE

STATE AND REGIONAL DEVELOPMENT COMMITTEE

INQUIRY INTO DOWNSTREAM GAS SUPPLY AND AVAILABILITY IN NEW SOUTH WALES

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At Sydney on Monday 18 November 2013

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The Committee met at 9.00 a.m.

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PRESENT

Mr A. Gee (Chair)

Mr A. Marshall
Mr D. Maguire
Mr R. Furolo
Mr G. Piper

CHAIR: Ladies and gentlemen, good morning and thank you for attending the first public hearing of the State and Regional Development's Inquiry into downstream gas supply and availability in New South Wales. We are very grateful that you could join us today.

Before the proceedings commence, could I remind everyone to switch off their mobile phones.

Today the Committee will hear from Ms Danielle Beinart and Mr David Musson from Jemena Gas Networks (NSW), Mr Steve Davies from the Australian Pipeline Industry Association and Mr Craig de Laine and Mr Andrew Staniford from Envestra Limited.

The Committee has resolved to authorise the media to broadcast sound and video excerpts of its public proceedings. Copies of the guidelines governing coverage of proceedings are available from the Committee staff.

I now declare the hearing open.

DANIELLE BEINART, Manager, Gas Network Development, Jemena Gas Networks (NSW) Limited, Level 20, 111 Pacific Highway, North Sydney, and

DAVID MUSSON, General Manager, Gas Networks Commercial, Jemena Gas Networks (NSW) Limited, Level 20, 111 Pacific Highway, North Sydney, affirmed and examined:

CHAIR: Once again Ms Beinart and Mr Musson, welcome. We are very grateful to have you here today. Could you please confirm that you have been issued with the Committee's terms of reference and information about the standing orders that related to the examination of witnesses?

Mr MUSSON: Yes.

Ms BEINART: Yes.

CHAIR: Could you please both state the capacity in which you are appearing today?

Mr MUSSON: I am present on behalf of Jemena Gas Networks as an employee. My title is General Manager, Gas Networks Commercial with Jemena Gas Networks.

Ms BEINART: I am here on behalf of Jemena Gas Networks as well. My position title is Manager, Gas Network Development.

CHAIR: The Committee has received a submission from your organisation and do you wish that submission to form part of your formal evidence?

Mr MUSSON: Sure, thanks.

CHAIR: Do you have questions concerning the procedural information sent to you in relation to witnesses and the hearing process?

Mr MUSSON: No.

CHAIR: Would you like to make an opening statement before the commencement of the questions?

Mr MUSSON: Just very briefly. Jemena Gas Networks is a distributor in New South Wales that supplies about 1.1 million residential and business consumers. I guess the relevance to the Committee is that the network is located within the greater Sydney area but also has pockets along the

Moomba to Sydney pipeline supplied by the Moomba to Sydney pipeline in a number of regional centres, approximately 20 plus. We consider it as a single network but it is actually made up of a number of disparate geographic areas.

CHAIR: As I have said, we have been through your submission and we are grateful for it. What we might do is move around from Committee member to Committee member asking questions and once all of our questions have been exhausted, then you will be free to go.

Perhaps I can commence by asking you what you see as the barriers to expansion of downstream gas supply. What are the barriers to expanding that in New South Wales?

Mr MUSSON: I think the main barrier would be one of economics. Jemena Gas Networks has a natural incentive to grow the network because it is the source of our revenue and that has a certain cost to connect. Ultimately the regulatory regime that we work within requires us to only invest in prudent and efficient expansion of the network.

I think the main barrier for us would be where expansion of the network or availability of the network is hampered by the economics of the expansion not being prudent and efficient.

Ultimately, because of the regulatory regime we work within, if the cost to expand is not net present value positive, that is it does not actually provide greater revenue than the cost over a period of time, including all the associated costs of financing, et cetera, then other consumers end up cross-subsidising the new consumers that are actually connected through that sort of expansion.

Ultimately I think the main barrier would be the economics of individual expansions and extensions.

CHAIR: You have listed in your submission a number of policy settings that would help drive new reticulation and you have mentioned the Energy for Regions program which is operated by the Victorian Government. Could you expand on that program and also give some indication to the Committee as to the extent you think that would work in New South Wales?

Mr MUSSON: As I mentioned in my opening statement, our network consists of a large mass of network in the greater Sydney area plus a number of regional centres. The regional centres that we have extended the network to over the years are microcosms of the sort of expansion that might work more generically should the economics be appropriate and be positive.

The Victorian scheme would seem to address some of those economic barriers where it might not otherwise be net present value positive for a distributor to expand. Where we have found opportunities to do so in a positive way, we have. We are always open to expand the network, given the drivers that I have mentioned previously should the economics of it be appropriate.

What the proposal would be, would be to change the economics that would otherwise be prevalent to make it net present value positive to be able to expand.

CHAIR: What are the main features of the Victorian program?

Mr MUSSON: The main feature that is relevant to us is that it fundamentally changes the economics. The individual detail is not so important to us, because there are quite a few ways you could give effect to the scheme in New South Wales. I think fundamentally some of the important drivers for us would be the long term sustainability of an investment.

If you look at how the network expands, there is an upfront capital cost in terms of getting infrastructure to a particular regional centre and then there is the ongoing maintenance and supply to that region.

I think it is important for it to be economically sustainable by having sufficient base consumption base load within the centre that you get to once you have actually had an economically feasible investment to get the infrastructure there in the first place.

The proposal would be assist with the cost of getting the infrastructure to a region that would otherwise be self-sustaining from a consumption perspective.

CHAIR: Do you have any particular features of the Victorian program which you think could work in New South Wales or you are staying with the broader principle of the issue?

Mr MUSSON: I think it is the broader principle because with the modifications that I have proposed, I think the focus does need to be on the long term sustainability.

Ms BEINART: Looking at the Victorian program, what the Government is assisting with is that upfront capital contribution to extend a pipeline or network to the town, but I am not sure to what extent they look at the ongoing sustainability of that new network in terms of the load that that town would continue to take.

Mr GREG PIPER: Capital infrastructure, is that what you are talking about?

Ms BEINART: The pipeline.

CHAIR: The pipeline.

Mr GREG PIPER: Yes but actual financial assistance with that infrastructure?

Ms BEINART: That is what the Victorian Government is doing. I think they call it a bounty payment.

Mr DARYL MAGUIRE: Can you point to an example?

Ms BEINART: I think I read for Lakes Entrance there was a $20 million bounty payment given to the local network to expand in that town.

Mr DARYL MAGUIRE: For a total investment of how much?

Ms BEINART: I am not sure.

Mr GREG PIPER: Can I just ask a further question on that, is there a State Government dividend for that investment or is this to drive it from the broad economic benefit?

Ms BEINART: My understanding is it is an economic social program for regional areas.

Mr GREG PIPER: Lots of money.

Ms BEINART: Yes.

Mr ROBERT FUROLO: Has Jemena Gas Networks made a submission or a request to the Minister or Government of New South Wales to implement an Energy for Regions type program?

Mr MUSSON: Not that I am aware of. Our submission to this Committee was the main vehicle that we have used to make that point.

Mr ADAM MARSHALL: In your submission you talk about—on the flipside of what we have just been discussing—that there are some costs involved with compliance and other processes. I think you mentioned road opening payment restorations, et cetera and you suggested that they could also be barriers to the extension of the network.

I want to get a sense from your perspective, broadly speaking what are the compliance costs and how could the impact of that on service providers be reduced?

Mr MUSSON: When we connect in an existing area for example, depending on the type of road that the customer is located on, may require us to open certain permits with Roads & Maritime Services or other service providers in order to be able to open the road to lay the infrastructure that we need to in order to actually connect the customer.

In some cases that can be quite inexpensive if the area is a new area that does not have a lot of infrastructure in place already or quieter roads that are not of the certain class that would actually require the level of permit that would otherwise be required.

In contrast to that, a more developed area may require several thousands of dollars of fee paid by Jemena Gas Networks in order to actually get access to the infrastructure that we need to in order to connect the customer.

The cost of compliance takes a number of forms, whether it be the administrative process and the cost of the compliance with the administrative process in order to go through the permitting process through to any sort of fee that is actually payable for the right to do what we need to do.

An opportunity may exist to see a gas distributor on more equal footing with other statutory utilities that may have some assistance provided to not see the transfer of equity occur the way it does.

It is an option available. It would work to lower costs of connection, which would make more connections viable. We are certainly not complaining about the need to comply with the existing process but it does have a cost and that cost does actually impact on the viability of connections.

Mr ADAM MARSHALL: You say in your submission you have networks obviously in other States across Australia, how does the compliance regime in regard to what we have just been talking about compare in this State to other jurisdictions which have networks?

Mr MUSSON: We do not have gas networks in other States, we only have an electricity network in Victoria and so it is a very different case. It is an essential service. Typically it is overhead infrastructure; it is a very different case.

Mr DARYL MAGUIRE: Mr Musson, who are the major shareholders in Jemena Gas Networks?

Mr MUSSON: Singapore Power.

Mr DARYL MAGUIRE: Is it a new entity or is it one that was existing that was purchased by Singapore Power?

Mr MUSSON: Jemena Limited was formerly known as the Australian Gas Light Company.

Mr DARYL MAGUIRE: Does the Australian Gas Light Company or Singapore Power or Jemena Gas Networks have in its policy community service obligations or consideration for specific circumstances where they actually will make some kind of policy abbreviations or policy deviations to allow the connection of a company or of a community to natural gas?

Mr MUSSON: The regulatory regime we operate within is fairly specific in relation to the requirement for connections to be economically viable.

Mr DARYL MAGUIRE: What you are suggesting is if a government similar to Victoria made a contribution—and Mr Chair, we might have to make some inquiries as to what those contributions are, some of the background for the Lakes Entrance that you mentioned. If the Government made a contribution of X amount of dollars, you then raise the issue of your investment, Jemena Gas Networks' investment needing to be sustainable and you are talking about the network ongoing cost of maintenance, et cetera.

If I recall, you actually receive an access charge as well as selling the gas in the network. Is that correct?

Ms BEINART: We receive a network supply charge.

Mr DARYL MAGUIRE: Yes, access fee.

Ms BEINART: But that is only per connection. I guess the risk for us in going to a town that might have a low base load is that a lot of money could be spent taking the network to a particular regional town, but we are not guaranteed of any actual connections.

It might be quite some years until people in the town make that decision to connect to gas. The decision to connect to gas is often driven by the appliance life cycle. People will substitute an electric appliance for a gas appliance; so really you are waiting for breakdowns. Someone generally will not replace their electric hot water system until it breaks down and if gas is available then they might make that decision to switch to gas. It is the same for heating and the same for cooking. But that might only be several years after the network goes to their town, so we are not guaranteed connections immediately.

Mr DARYL MAGUIRE: Does Jemena Gas Networks have a policy on the number of connections needed in any town or village or hamlet before it would extend its network?

Ms BEINART: There is no policy per se, what there is, is a net present value model. We need to model the potential investment. That will include the capital costs of getting to the town, everything from laying mains to laying services to meter costs. That will then be offset by the projected number of connections and the load at each of those connections.

Most households would have a small load or a large load and as David mentioned, in our five yearly access arrangement with the Australian Energy Regulator, we have a requirement to demonstrate that all connections are net present value positive. If we cannot demonstrate that, then there is a real risk that we cannot roll that capital expenditure into our regulatory asset base. So it is like a dead investment for us.

Mr DARYL MAGUIRE: Do you have an example of a community that you have completed that study on and has resulted in the connection of gas and one that you have done the study on that has resulted in no connection?

Mr MUSSON: Two that come to mind—they might not be recent—but Singleton and Blue Mountains.

Mr DARYL MAGUIRE: Is that information that you gather on what you base your commercial decision available to this Committee so that we can see the things that you consider and if your suggestion of a government fund or program is required, then the Committee can get a feel for what we should be recommending?

Mr MUSSON: I would have to take it on notice.

CHAIR: You have mentioned Singleton, what are some of the other 20 regional centres that you supply?

Mr MUSSON: Short of having a map in front of me, Dubbo.

Ms BEINART: Orange.

Mr MUSSON: Parkes, Forbes, Lithgow.

Ms BEINART: Wellington. There is a list of 20 of them.

Mr DARYL MAGUIRE: Can you name a community that applied for gas and was unsuccessful?

Mr MUSSON: I am not aware of communities actually applying in that way. We look for areas where there might be a centre of consumers that might want to get connected to gas.

Mr DARYL MAGUIRE: The reason I ask is because I have been through this exercise with the community of The Rock in Lockhart Shire that went through the process; went through gathering information of all of the town-holders and exactly what you are telling me, concurs. Appliances were an issue, the number of people connecting but ultimately the other driving factor now is the regulation that surrounds wood fires, the pollution that they are creating and government legislation, as well as the cost of liquefied petroleum gas in cylinders skyrocketing.

Those communities are actually older communities, meaning that the population is aged and getting access to energy at a reasonable cost is becoming more difficult, but yet that community still would want to connect to gas. With the absence of base load, which I understand because of an example of Uranquinty Wambo power station creates the base load but you just cannot put a Uranquinty Wambo at every small community.

I note that you have said a policy to encourage that would be good; have you got any suggestions about how we would go about that with policy to attract a business that uses base load in a small community like The Rock?

Mr MUSSON: No. It is certainly a vexing question. It is not really our area of expertise.

Mr DARYL MAGUIRE: Can you think about it for me?

Mr MUSSON: We will certainly take it on notice.

Mr GREG PIPER: Can I just ask a question which was directly to the submission, in relation to some recommendations to grow the customer base or demand which was in relation to the Council of Australian Governments' recommendations on phasing out emission intensive systems. Can you tell me whether or not that proposition to phase out intensive emission appliances is being promoted by the industry actively, by Jemena Gas Networks and other industry players? Are they actually doing that? Are they suggesting an accelerated phase out? There is a natural life, there is attrition and I think you have touched on that earlier about the changeover of appliances, but is there a suggestion in this that we should be accelerating the phasing out?

Ms BEINART: I think it was in 2010 the Council of Australian Governments recommended the phase out of emission intensive hot water systems and then a number of jurisdictions endorsed that, including New South Wales. New South Wales later reversed its policy on that.

For us it was a helpful policy in making more connections economically viable because we could assume a higher connection rate because we understood that when the lifecycle of those emission intensive hot water systems, which are normally electric, came to an end, the most cost effective compliant system for a consumer to move to was a gas connection. So it was likely that we would be getting more gas customers, which would therefore make new connections more viable.

You asked whether we have been agitating on the issue, I think we have certainly made our feelings known without wanting to be aggressive on the point, but we have certainly made submissions on it before.

Mr GREG PIPER: Can I just follow up on that. Using Mr Maguire's example of The Rock as a community that has been seeking gas reticulation, if a community was being looked at from your business model and was on the cusp, would such a program to phase out the emission intensive appliances with the State providing subsidies to the actual consumers to change over their appliances or some other kind of incentive; how does that work?

Mr MUSSON: Anything that would give us greater certainty for a great load per consumer for example would certainly help the economics of the investment.

Mr GREG PIPER: At the same time in your submission you then compare the benefits of gas against heat pump or solar technology and you talk of gas being able to hold its own given some equity in the market. Are you suggesting the subsidies and the assistance that is in that market is disadvantaging gas at this stage and would you see this as equalising it or would that market have an argument that there is an imbalance?

Mr MUSSON: Our focus is really on promoting natural gas, so the sort of program we are talking about would certainly assist consumer uptake of natural gas. In terms of the subjective view about the relativity there, that is not really my place to judge. We are focused on increasing the number of customers and increasing the availability of gas to those customers.

Mr ROBERT FUROLO: You have discussed the prudent and efficient expansion of network test that you do, analysing whether it is worthwhile. How do you determine and where do you apply that test? Which communities would you apply that test to and what is the basis for those communities seeking that test?

Ms BEINART: We apply that test to every single new connection that we make, whether it be a consumer on a street that already has gas; say someone who lives on a street in Leichhardt that already has a gas mains laid down but that particular household does not have a gas connection, we will do it for that household.

We will do it for a whole new street in a different suburb that does not have gas or we will do it if we get a request or a ministerial inquiry as to whether gas could be made available to a regional area.

Mr ROBERT FUROLO: How many requests have you had in the last 12 months—and you can take this on notice—in regional areas? I am not concerned about where gas is already supplied, I am concerned about where gas would need to be provided and supplied.

Ms BEINART: Sure.

Mr ROBERT FUROLO: How many have you had in the last 12 months from regions or towns or villages?

Ms BEINART: We would need to take that on notice once again. Sometimes a request is received from a local member of Parliament. Sometimes it is just a single householder who might call up or send in a letter making an inquiry.

Mr ROBERT FUROLO: Once you have received that request, whether it be from a member of Parliament or a single resident, do you do the full analysis for that town, for that region, for that village? Is that part of your analysis or do you just say one person has inquired, we will not worry about it?

Mr MUSSON: We do request more detailed analyses as required based on the broad viability. For example, if it is going to cost several million dollars to extend to an individual consumer, then we will not do the level of detailed analysis that would bring that price down to a more specific value given the order of magnitude, but certainly a check on the distance to the nearest gas infrastructure is done in order to make that initial assessment.

Mr ROBERT FUROLO: Do you have a method by which you can bring together all the submissions and requests that have been made in a particular region so that you can identify that more than one person is actually seeking a connection?

Mr MUSSON: Yes and that is certainly the process that we have used in order to connect regional areas previously. If I add to the previous comments in terms of the trigger for us to do this sort of assessment, what Danielle mentioned is correct but we also do it proactively. We look for regional centres where something has changed, some driver for the economics of the extension has changed, whether new industry has emerged, whether a population growth has occurred and so proactively we will re-look at areas that we might have looked at previously when those things have changed in order to re-assess.

CHAIR: You mentioned distance to main gas infrastructure as being one of the factors that you consider, is there a critical distance that you have in mind when you are making these assessments with respect to the distance from the main gas infrastructure?

Mr MUSSON: That is all a function of how expensive it is to lay the infrastructure that is required to come from where it is at the moment from where it needs to be.

CHAIR: What is the greatest distance you have ever gone?

Mr MUSSON: I would not be able to speculate.

Mr ROBERT FUROLO: Is there any indicative cost, per metre or per kilometre that you work on?

Mr MUSSON: No, the type of infrastructure that is required actually differs on a case by case basis. For example, you may have gas that is fairly close to a new development but if the new development is of a certain size that is unable to be served by that infrastructure that exists, you may need to lay infrastructure further back into the supply chain in order to get the level of supply and the volume that is required in order to meet that demand. There is no real ready rule of thumb that you can use.

Mr GREG PIPER: In my mind in the discussion we have been having, we have been talking more about residential type connections and the demand there. Obviously there is a range of commercial demands but can I just ask you about the capacity of the industry and yourselves to supply, for example, large scale demand such as power stations. If you could comment on how you see the industry in relation to policy in New South Wales at the moment for example?

Mr MUSSON: The industry has a history of meeting demand in the sense that given the economic equation that we have discussed previously, if a power station were to request supply then supply has always been a function of the cost of expanding the infrastructure in order to meet that demand.

I am not aware of instances where supply has been refused to meet demand for any other reason than the economics of that particular expansion.

Mr GREG PIPER: There has been no problem with capacity to source gas and keep the market satisfied across the board for residential and commercial, if one or two gas fired power stations came on board?

Mr MUSSON: I need to qualify our role is about moving other people's gas from one place to another. I cannot really comment on the actual availability of the commodity. I am only speaking about the availability of the infrastructure to move the commodity from one place to another.

Mr ROBERT FUROLO: The foreshadowed change in federal policy on pricing carbon—in the mind of Jemena Gas Networks or in its business case—have any implications for the prudent and efficient expansion of networks for your organisation? Does it change the calculations in any way?

Mr MUSSON: Carbon is a pass through cost that we pass onto consumers and so it changes the economics in so far as it might make the commodity more or less expensive to that end consumer but from our perspective it is a pass through.

Mr ROBERT FUROLO: If the energy source competing with gas becomes less expensive––which is what is foreshadowed—does that then change the likelihood that the prudent and efficient expansion test would be more difficult to reach?

Mr MUSSON: Gas is not an essential service in New South Wales, it is something that we have always had to promote in order to get uptake. Where an alternative commodity is more attractive to an end consumer, whether it be for price or other reasons, we are competing against that. Of course, where it is less attractive, consumers will move to the other commodity, where it is more attractive consumers will move to gas.

Mr DARYL MAGUIRE: I think what the member is getting at is, is there a differentiation between the carbon tax on energy and the carbon tax on gas? If the carbon tax is removed, is one advantaged over the other is the point he is trying to make.

Mr ROBERT FUROLO: What I was trying to get at—and I think you have answered it in a roundabout way—was if the carbon price is removed and electricity as a result becomes less expensive, does that mean it is more difficult for communities to be able to reach that prudent and efficient expansion of network test because people would be less inclined to take up gas because is it comparatively less attractive? That was my point.

Ms BEINART: I do not think it would have an impact on that. As David mentioned, the carbon tax is currently applied to gas bills as well and that is done as a pass through, so a line item on the bill. If that was removed that line item would just disappear and it does not factor into our economic modelling.

Mr MUSSON: Like any other cost component, should there be disparity between the amount of a particular cost component that appears on the bill, that it is different from one commodity to another, it will have a corresponding impact on consumers' choice, sure.

Mr DARYL MAGUIRE: Who are your competitors in supplying gas in your network?

Mr MUSSON: Because we have a natural monopoly in relation to where we have infrastructure laid, we consider our competitors to be other fuels like electricity, liquefied petroleum gas, other commodities that might be a substitute for natural gas.

Mr DARYL MAGUIRE: But as Mr Furolo pointed out, they are not like for like and depending on how the costs of the carbon tax play out, you really have not got any other energy supplier in natural gas to compete with, correct?

Mr MUSSON: We practically do not. It is not to say from time to time other distributors have chosen to lay in parallel to us.

CHAIR: Who are the other distributors that operate in the same market that you do?

Mr MUSSON: There is the APA Group, Envestra Limited. I am not aware of thers.

CHAIR: I noticed in your submission you did not really deal with the issue of competition in the downstream gas market. What is your view on the state of competition in that market?

Mr MUSSON: I guess we see our role as being to facilitate one retailer transferring a customer to another retailer in collaboration with the Australian Energy Market Operator. So long as a consumer is using natural gas and has chosen natural gas; then we have met our objective. Which retailer actually delivers to that end consumer is really between that retailer and the end consumer.

CHAIR: Do you think there are enough players or operators in your market already?

Mr MUSSON: I do not really have an opinion.

Mr DARYL MAGUIRE: Very wise. Mr Chairman, to other questions: Liquefied natural gas is new technology. America is rolling out liquefied natural gas. Has your organisation considered that the adoption of liquefied natural gas technology and the need for liquefied natural gas service centres will actually bring about a greater draw on the base load for energy that your company can play a major role in?

Mr MUSSON: We have certainly been a supporter of compressed natural gas in the past. Liquefied natural gas is a more difficult technology; I guess a more recent technology which we would see compressed natural gas as being a step towards.

We struggled with compressed natural gas for a number of decades where the relative price of alternative fuels and certainly the relative price of liquefied petroleum gas being the major competitor to compressed natural gas has been fairly influential in terms of the viability of us progressing with compressed natural gas.

Compressed natural gas is still used by a number of different organisations and a number of different vehicles, but certainly the popularity of it waxes and wanes based on the pricing differential.

Mr DARYL MAGUIRE: My last question is what percentage of your gas do you supply to consumers that you source from coal seam?

Mr MUSSON: Well, we do not actually supply the commodity; we move other people's gas from place to place.

Mr DARYL MAGUIRE: Do you know what percentage is actually in the network?

Mr MUSSON: No.

Mr DARYL MAGUIRE: I think it is about five per cent.

CHAIR: Is there anything either of you would like to add to your evidence today?

Mr MUSSON: No, I am certainly comfortable that our submission had covered off the major points that we would like to make.

CHAIR: Can I thank you both for appearing before our Committee today. We have certainly appreciated it and we appreciate the work that you have put into your written submissions as well.

The Committee may wish to send you some additional questions in writing, your replies to which will form part of your evidence and made public. Would you be happy to provide a written reply to any further questions?

Mr MUSSON: Yes, certainly.

(The witnesses withdrew)

STEVEN MICHAEL DAVIES, Policy Advisor, Australian Pipeline Industry Association, 7 National Circuit, Barton ACT, affirmed and examined:

CHAIR: I would like to welcome Mr Steve Davies from the Australian Pipeline Industry Association to Parliament today. Thank you for appearing before the State and Regional Development Committee and for giving evidence today.

Could you please confirm that you have been issued with the Committee's terms of reference and information about the standing orders that relate to the examination of witnesses?

Mr DAVIES: Yes I have.

CHAIR: Could you state the capacity in which you are appearing before the Committee today?

Mr DAVIES: I am here as the Policy Advisor of the Australian Pipeline Industry Association, which is the peak body representing the interests of the gas transmission industry.

CHAIR: We have received the submission of the association. Do you wish for that submission to form part of your formal evidence?

Mr DAVIES: Yes I do.

CHAIR: Before we proceed, do you have any questions concerning the procedural information sent to you in relation to witnesses and the hearing process?

Mr DAVIES: No, I am fine.

CHAIR: Would you like to make an opening statement before the commencement of the questions?

Mr DAVIES: Yes. Thank you very much Mr Chairman and members of the Committee. I would like to make a short opening statement just covering some of the high points of the submission that we have already made and inform you of some of the things that have happened since June when we did make that submission.

The first thing I would like to cover is in regards to the terms of reference and the first point on the terms of reference, the adequacy of transmission pipeline systems and distribution networks, future downstream gas needs and supply challenges.

As we made the point in our submission, currently New South Wales is very adequately served by gas transmission pipelines. The capacity of installed pipelines is currently greater than the typical demand that is experienced in New South Wales, even on a peak day. We have got the Moomba to Sydney pipeline bringing in gas from South Australia and Queensland at the moment and the Eastern Gas pipeline bringing north from Victoria as the two primary sources of gas coming into New South Wales and also the Victorian interconnect coming through Wagga Wagga and the Australian Capital Territory, brings in another regional amount of gas.

The installed capacity of those three systems is more than enough at the moment to meet New South Wales' gas needs. What might change in the future is not that New South Wales' gas demand will outgrow the capacity of those pipelines, but that the Moomba to Sydney pipeline in particular may not have the same quantity of gas coming down it into New South Wales as it currently does.

In that sense whilst the Moomba to Sydney pipeline remains a good resource for the State, if the decision of those who produce and sell gas in South Australia is to allocate that gas somewhere else, then the Moomba to Sydney pipeline may no longer bring in the same amount of gas as it has been bringing into New South Wales.

Things that we have seen reported in the media that because that may occur, this means the adequacy of pipelines coming out of Victoria into New South Wales might be deemed insufficient or that the size of those pipelines could constrain the ability of gas from Victoria and the Bass Strait to come into New South Wales and supply some of New South Wales' needs.

The reality is pipelines are built for what the transport requirements of the day are. They are privately owned. Their capacity is sold under long term contracts and it is very difficult for a company to consider having spare capacity just sitting in a pipeline waiting for the right opportunity to be able to sell it.

Pipelines are designed for what their customers are willing to contract to now and they are readily expandable as those requirements change. You can expand a pipeline through building additional pipes next to the existing pipeline and interconnecting them—that is called looping—or by adding additional compression and increasing the pressure of the pipe. Then that allows you to transport quite a bit more gas.

In the last couple of months as the New South Wales supply situation has been heavily reported in the media and New South Wales gas customers are starting to wonder about where they are going to meet their gas requirements from 2015 on, we have seen several announcements from APA Group and Jemena Gas Networks, two major gas transmission companies, that they are expanding their infrastructure coming out of Victoria.

APA Group owns the Victorian interconnect and they have recently announced a couple of different expansion contracts that will result in its capacity increasing by over 100 per cent and Jemena Gas Networks has also announced that they are in the exploratory stages of a reasonably significant expansion to the Eastern Gas pipeline which brings the majority of gas out of Victoria.

The ability of the gas transmission industry to respond to new requirements is very good. As its customers start to need gas from new sources, we will start to build pipelines from new sources or expand existing pipelines. But we will not be expanding those pipelines in anticipation of the requirement for gas to come from a new source. It is incumbent on the parties who are selling gas and buying gas to reach their arrangements first and then the gas transmission industry will build or supply the infrastructure to enable its transportation.

The second point I would like to cover is just on barriers to expansion of the downstream gas industry. It is not so much a barrier, but the reality is when you are looking at extending gas networks to regions, there needs to be large sources of new gas demand to justify a gas transmission pipeline being extended or being built into a new region.

Residential demand accounts for quite a small amount of gas demand in New South Wales and in all States in Australia. When you are talking 15 to 17 per cent residential demand is your total gas throughput, you really cannot justify transmission pipeline investment on that basis. The majority of transmission pipeline investment is for power stations, for very large gas users such as mineral processing or large manufacturing industries. Once those sort of large foundation demands are met, you can add additional capacity to meet the residential and mass market requirements, but it is very unlikely that household demand can drive a new investment.

As we seek to find ways to extend gas networks and gas pipelines into new regions, we have to be mindful of where are the large sources of gas demand going to be coming from.

The alternative to that is when there are new gas producing regions and they are building pipelines to take gas to the demand that they are servicing, there are opportunities there to service the towns in the vicinity of those new gas production areas or that are along the route of the gas pipeline.

Those are really just highlighting the two main points of our submission and I would be happy to take questions now.

CHAIR: I understand that your main interest is in the transmission sector. What is your view of competition in the downstream gas supply and distribution networks? Is there enough downstream competition? Could there be more?

Mr DAVIES: When it comes to distribution networks, it is very hard to have perfectly competitive environment. Each town or city can only have—cannot only have, but it makes a lot of sense to just have the one distribution network within the town. Jemena Gas Networks is in Sydney and in other parts of the State. I know Envestra Limited and a couple of other companies have smaller regional centres.

You cannot really say that distribution networks are a competitive environment or that they should be a competitive environment. They are overseen by the Australian Energy Regulator to ensure that the tariffs they charge are appropriate.

In the retail space, in terms of the choice customers have in terms of who they can access their gas from, it is reasonably competitive. There are several large retailers that can supply electricity and gas to households. They tend to be the conduit through which gas is sold, so they are not usually producers of gas as well. Gas producers do not typically deal with downstream so much unless it is the very large customers. Most of the gas they would sell onto retailers, who then sell onto households.

I would say it is about as good as it can be in terms of retail competition in New South Wales.

CHAIR: Your fundamental thesis through your submission is that basically if you want to expand downstream gas supply and distribution that you need new large industrial users or gas power stations to basically drive that whole process. Is that fundamentally where you are coming from?

Mr DAVIES: If you want the private sector to pay for that infrastructure, yes. In Victoria you do have a system by which the Victorian Government subsidises the cost of infrastructure to new towns and regions but if you want the private sector to pay for that infrastructure, it is going to have to have those large gas loads which provide the throughput to justify the investment.

CHAIR: What is the Australian Pipeline Industry Association's view of the Victorian experience and what they have done down there?

Mr DAVIES: We think it has been quite successful. It has not directly involved the transmission industry. It has been an extension of distribution networks. The pipelines that are connecting those towns are high pressure pipelines but they are part of the distribution network rather than stand alone transmission pipelines.

We would support those kinds of programs being rolled out where appropriate. It provides gas to new regions, which does provide multiple benefits, not just those additional opportunities to use gas, particularly for residential, space heating and others but it does give industries in those towns opportunities to explore the use of gas for their requirements, which can lower their energy costs as well.

CHAIR: How many members does your association have?

Mr DAVIES: Our association has actually over 400 members but in terms of members that are owners and operators of gas transmission infrastructure, we have about 15.

Mr DARYL MAGUIRE: I am particularly interested in some of the suggestions that base load is the pre-determining factor on whether a community gets gas connected. We have had other information put to us that there are requirements to be met before a distribution company will actually go into a town and put in a network. There has been a suggestion that government should facilitate some kind of funding arrangement. I understand Victoria has a program.

But, there was also a suggestion that you need base load. I gave the example of Uranquinty, which has a four gas turbine generator, 600 megawatts and it was selected because of its location for the main gas line and for its proximity to the electrical distribution network.

Not all towns and communities have that. How, other than throwing money at it, meaning throwing money at the suppliers or the distributors, can government bring about policy that encourages business or investment that base load consumers?

Mr DAVIES: That is a very good question.

Mr DARYL MAGUIRE: It is a tough question.

Mr DAVIES: Yes, it is. It often would take more than one smaller customer to justify it. There needs to be that co-operative element to aggregating as many businesses as possible into a load in a new region. There could be a role in terms of educating businesses as to the opportunities that would be available to them if gas came to their town.

One of the emerging uses of gas that has started to become more and more popular for larger air conditioning loads is gas fired refrigeration; being able to use natural gas to power large abattoir sites, refrigeration units. If you can start informing communities of these kinds of opportunities and lining up as many businesses as possible to make a shift at one time, that could help justify an investment.

Mr DARYL MAGUIRE: What you are suggesting is that technology is similar to the old kerosene fridge, where utilising heat produces coal?

Mr DAVIES: I do not know the technical details of the kerosene refrigeration.

Mr DARYL MAGUIRE: It is the same principle.

Mr DAVIES: It comes down to it is the gases that come out of it as they expand and contract, they absorb heat is in essence what happens with gas refrigeration.

Mr DARYL MAGUIRE: In theory, in Victoria I understand government make a contribution to communities that have identified the need for gas and it might be $10 million or $20 million and walk away. Gas distribution networks receive funds from an access fee that all consumers, as I understand it pay, not whether they are connected to a gas line or not. If the gas line passes past your property, then you are liable for that access fee, whether you are a consumer or connected. Is that correct?

Mr DAVIES: I do not believe so. You have to be connected to the gas network to be charged a connection fee.

Mr DARYL MAGUIRE: But not an access fee?

Mr DAVIES: I am not sure what the difference between an access fee and a connection fee might be, but if you are not using any gas I would not expect that you are paying any sort of fees related to gas.

Mr DARYL MAGUIRE: My understanding is you do, whether you are a gas consumer or not and it is the same with energy and it is the same with water. Can we get some clarification on that?

Mr GREG PIPER: I think it is a fair question. It is similar with reticulated sewerage, where it is an opportunity fee that you pay. It would be very worthy to know if that is actually the case.

Mr DAVIES: I do know, for example, in Queensland some councils run the gas distribution network and so through their rates they may charge a gas access fee similar to a water access fee.

Mr DARYL MAGUIRE: Is that question about access fee one that you can come back to us on, take it on notice?

Mr DAVIES: Absolutely.

Mr DARYL MAGUIRE: And if there are any other examples. The other question I had for you is other than government throwing $10 million or $20 million in and walking away, have you any other ideas, other than attracting major industry, that would encourage consumers to utilise natural gas and obviously that would then precipitate the connection to the main lines or to a reticulation network? Perhaps encouraging or giving bounties for old and dysfunctional type appliances, perhaps giving connection fees or some kinds of consideration so that those communities can access a cheaper form of energy.

As it is now, if you look at Tumbarumba, The Rock, Batlow, Lockhart, to name a few towns in my area, they would all like access to natural gas because of its environmental benefits and because of its cost, yet the gas companies just are not interested because of that base load.

Would a program that encouraged the uptake of new appliances, more efficient appliances encourage the distribution network to connect?

Mr DAVIES: It could help but those kinds of programs would still be aimed at the residential consumers for the most part probably. You would still be having to pay, in some form, through an incentive residential customers some amount of money to switch to gas and even if a household was to switch to gas in all available opportunities in a medium or small town, that is unlikely to be sufficient to justify the investment.

But we would like to see programs that did encourage the swapping of electrical appliances to gas appliances. There are a number of programs throughout the country that encourage the swapping of, for example, water heaters, electrical water heaters to heat pumps or solar hot water heaters but there is nothing to encourage the swap to gas water heaters.

Whereas if you look at how much money you spend versus how much energy you save and how many emissions are produced, for one solar hot water system replacing an old electrical system you would probably put in three gas hot water systems and have greater environmental benefits.

Mr DARYL MAGUIRE: But really what you are saying is for the cost of putting infrastructure in place to support the gas distribution network, government would be far better off to invest in the energy network, which is already existing to every house, village, hamlet and city across Australia, and invest in that network to get the cost down rather than pursue natural gas expansion.

Mr DAVIES: Then you would not have the option of natural gas as well. But that is right, electrical networks are extended throughout the State.

Mr DARYL MAGUIRE: You could invest that money in gas turbine technology.

Mr GREG PIPER: Power stations.

Mr DARYL MAGUIRE: And installations across the State rather than expanding the natural gas network?

Mr DAVIES: And natural gas turbines would have to go where the gas pipelines already are.

Mr DARYL MAGUIRE: Most of them are serviced by an electricity network; that is what I am trying to get to.

Mr DAVIES: Yes.

Mr DARYL MAGUIRE: Those electricity networks are already in place and gas turbine selection is always based at the crossroads of those two.

Mr DAVIES: That is right.

Mr DARYL MAGUIRE: So long as the supply is there.

Mr DAVIES: Yes.

Mr GREG PIPER: Mr Maguire is saying the bottom line is energy, however it is produced, if you take the gas to the end users, the myriad of residential users or if you produce the energy, a significant plant gas turbine in an appropriate location near a gas supply, and then you transport the energy by transmission.

Mr DAVIES: That gets energy to where it needs to go but there are a number of advantages for direct application of natural gas and the primary one is whenever you convert one fuel to electricity, there are massive inefficiencies that occur. Natural gas turbines are the most efficient and they are still about 50 per cent conversion rate of the energy embodied in natural gas, converting that to electricity. Coal power stations seem to be around 30 to 40 per cent depending on the technology.

Mr DARYL MAGUIRE: Has your organisation considered liquefied natural gas? In America liquefied natural gas is being rolled out across the states to power motor vehicles. Has your organisation considered the impact of such technology and also the increase in base loads to the State should that technology be embraced, and would that help in improving the returns to your transmission network and ultimately access for residents to those cleaner forms of gas?

Mr DAVIES: Yes, that would make a very big difference. Obviously the current transport energy demand is very high and substituting some of that from liquid fuels to gaseous fuels could have a big impact on the commerciality of gas networks and gas transmission pipelines.

For the most part it seems the only major level of interest here in Australia has been for liquefied natural gas and compressed natural gas for heavy vehicles, so there are still quite a lot of opportunities there, but it is not something that we have explored a great deal. There is actually another association called Gaseous Fuels of Australia that deals with liquefied petroleum gas, liquefied natural gas and compressed natural gas as a fuel for transportation.

Mr DARYL MAGUIRE: Do you have any information to provide to the Committee about liquefied natural gas and compressed natural gas?

Mr DAVIES: Sure, we can certainly take that on notice.

CHAIR: I might just mention in the public gallery at the moment we have students from the

New England Girls School in Armidale and also their teachers. Can I take this opportunity to welcome you all to the New South Wales Parliament. I know the member Northern Tablelands, who is sitting on my left is absolutely delighted to have you here. We welcome you to the New South Wales Parliament. We are always delighted to have students from regional New South Wales in our Parliament.

This is a public hearing which is being run by the State and Regional Development Committee. We are currently taking evidence from people involved in the gas supply and distribution industries which will assist us in our inquiry into—to put it simply—getting people connected to gas in New South Wales, particularly regional New South Wales. That is what we are doing today.

I think the member for Northern Tablelands has a question for Mr Davies.

Mr GREG PIPER: Could somebody please re-tweet it for him because he cannot do both at once.

CHAIR: Very strong on Twitter is the member for Northern Tablelands.

Mr ADAM MARSHALL: I have not tweeted today. Thank you Mr Chairman and welcome to all the students as well.

Mr Davies, the member for Wagga Wagga asked about the Victorian model and the way government can perhaps play a role in incentivising or trying to ensure the expansion of the downstream supply. On the flipside, looking at the regulatory side, do you see at the moment in New South Wales that there are any regulatory barriers to the expansion of downstream supply or is it simply market forces factor of needing to see more industrial demand drive the expansion?

Mr DAVIES: I really do think it is largely a market forces factor. To expand gas networks you need increased gas usage for the most part. The regulatory system between electricity and gas is a little bit different in terms of how tariffs are determined and revenues are raised for the monopoly infrastructure.

The member for Wagga Wagga did raise the point that electricity networks are near ubiquitous throughout the State and the country, they are connected everywhere and in part that is because electricity costs can be spread across the whole State. It is not a matter of an individual user has to pay their share of their network or their costs. So remote users pay the same as urban users for their electricity connections for the most part, whereas for gas there is very much a user pays approach to tariff determinations. If the network costs however many million dollars and it is only connecting to a thousand customers, those one thousand customers have to bear that full cost.

Mr ADAM MARSHALL: So is it the association's view that there are no real regulatory barriers restricting the expansion of the downstream gas supply and distribution networks? Is that fundamentally your position?

Mr DAVIES: I would only be comfortable commenting on the transmission pipeline side of that, so distribution networks are a separate question again. The transmission pipelines we do not feel there are any regulatory barriers to their expansion.

Mr ADAM MARSHALL: So the association does not have a view on the distribution side of things, is that what you are saying?

Mr DAVIES: Yes, that is right.

Mr ROBERT FUROLO: Through you Mr Chairman, in regard to the Victorian model of the Energy to Regions program, has your association or any members of your association that you are aware of done analysis of the impacts for their business for the industry of that program, what it has meant for transmission companies, if anything and what sort of take up there is in a town that has benefited from that Energy to Regions program?

Mr DAVIES: Unfortunately I am not aware of my members undertaking any work like that but those distribution networks that are active in Victoria I am sure have done so. I would imagine some of those will be here talking to you today. But for transmission pipelines, it really has had a negligible impact. Transmission pipelines have not been built on the back of that program. Distribution programs have been extended. I think there have been over a dozen towns through that program. It has not had a real impact on throughput on the major transmission pipelines.

Mr ROBERT FUROLO: Is that in terms of demand for gas supply?

Mr DAVIES: I cannot comment on within a town what the take up has been like but overall compared to the major industrial loads, even several towns is a really negligible amount. In terms of throughput on a transmission pipeline it has had very little impact.

Mr GREG PIPER: Mr Davies, can I ask about the members of your association. What do they actually do to try and educate and promote take up of gas so as to get that sufficient demand? Obviously it is beneficial to the public sector and to the Government to try and expand the network. That is one of the things we are looking at.

What does the industry do? Obviously it is beneficial to them too to promote that to residential and probably more to commercial customers?

Mr DAVIES: It is an interesting sector. It is quite fragmented. We have the gas explorers and producers on one hand, gas transmission companies, gas distribution companies and then energy retailers who typically sell electricity and gas. There is not a lot of co-operation between the sectors in terms of promoting natural gas to the community.

The transmission pipeline sector has largely been focused on how we see the major growth for transmission pipelines over the next couple of decades coming from increased use of gas for power generation. There are a lot of opportunities there. A few years ago that is where a lot of anticipation that the carbon price and readily available supply of gas would drive a lot of gas fired powered generation investment with the expansion of the liquefied natural gas industry in Queensland and the associated increase in gas prices. With the subsequent removal of the carbon price it is unlikely to see a lot there.

The transmission sector itself has not focused on selling gas to households and in getting a big take up of gas in households. The gas distribution sector has done quite a bit. In New South Wales you would be familiar with the natural gas, the natural choice advertising campaign that has been run here, focused on getting households to switch to gas where appropriate.

I cannot say the transmission sector has done a lot in that regard.

Mr GREG PIPER: You described your association as being fragmented across the industry, from exploration to transmission.

Mr DAVIES: The whole sector is that fragmented and our association is just the transmission side of that.

Mr GREG PIPER: Yet it is all obviously inextricably interlinked. Everybody rides on the participation and the opportunities that others have.

Mr DAVIES: Yes.

Mr GREG PIPER: It seems to me there might be opportunities there for those to work together a bit more closely.

Mr DAVIES: Just to give you an idea of the business of the transmission sector, there is no such thing as a typical transmission pipeline but in New South Wales there are two particularly large transmission pipelines. Both of those pipelines have around 10 customers and of those you have two or three energy retailers and the other seven are large industrial users.

There are not a lot of businesses to deal with and certainly we would like to see as many large industrial customers develop as possible. They will base their investment decisions on quite a number of things; gas supplier will be one of them. Those gas retailers which are expanding that gas in the community usage really do not represent a large portion of our customer base or the throughput to justify that.

I do take your point and we are interested in all opportunities to have natural gas use encouraged but the sector has been focused on that large industrial use.

Mr GREG PIPER: Can I check a figure; I think it came from a question from Mr Maguire previously about the residential usage. Was it about 17 per cent?

Mr DAVIES: Yes.

Mr DARYL MAGUIRE: Are you aware of the percentage of coal seam gas that is transmitted through your network?

Mr DAVIES: Not precisely. In New South Wales currently the amount of gas that is being consumed, about five per cent of that is produced from coal seam gas within New South Wales or existing as production in New South Wales, some of which is coal seam gas. At the moment there would be around 10 per cent of the gas coming through the Moomba to Sydney pipeline is coal seam gas.

Mr DARYL MAGUIRE: The exploration for natural gas, are you aware of any new fields that have been discovered in New South Wales and if so, are they close to transmission lines or does the organisation need to expand that transmission line to those new fields?

Mr DAVIES: As far as I am aware, a lot of the current activity in coal seam gas is focused in—I am sure the Committee know the names of the regions far better than I—the Hunter Valley and further north of there, which is not particularly well serviced by transmission pipelines at the moment. There is one transmission pipeline to Newcastle but there would have to be an extension of the transmission network.

Mr DARYL MAGUIRE: What about traditional natural gas, any new fields?

Mr DAVIES: I am not aware of any new fields of traditional natural gas in New South Wales.

Mr DARYL MAGUIRE: Can you tell the Committee what you know about proposals to pipe coal seam gas from Queensland to New South Wales? Are there any plans in place?

Mr DAVIES: No, not that I am aware of. It was foreseen that quite a bit of coal seam gas would come from Queensland to New South Wales through the QSN Link; that is the pipeline that connects Queensland to Moomba and then on-flowing through the Moomba to Sydney pipeline. That pipeline was finished four years ago with every expectation that it would be the main source of gas in New South Wales into the future.

Since then, in the last 18 months, they have completed a project to enable that pipeline to flow gas from Moomba into Queensland as it seems that that is the direction gas will be flowing. Queensland to Hunter Valley pipeline is a pipeline that has been on the drawing board for many years. It has a large number of its approvals in place and would be able to connect the Surat Basin to the Hunter Valley and then on through the existing transmission pipelines into Sydney but it seems no one is really at this stage anticipating gas flowing out of Queensland anymore.

Mr DARYL MAGUIRE: Are you aware of the proposal to establish a gas turbine generator in Wellington?

Mr DAVIES: No I am not.

Mr DARYL MAGUIRE: If one were established in Wellington, where would it source its gas from?

Mr DAVIES: Sorry, I do not know where Wellington is.

Mr DARYL MAGUIRE: Between Dubbo and Parkes roughly.

Mr DAVIES: I think between Dubbo and Parkes it would be sourced from the Moomba to Sydney pipeline.

Mr ROBERT FUROLO: Does your association have a view on whether investment in transmission pipelines will be affected by changes in the pricing of carbon, whether there will be an increase or a decrease in demand for natural gas?

Mr DAVIES: There will be a relationship between the two. At this stage it seems it is the gas price itself and the impact of the new export industry on gas price that will have a much bigger impact on gas demand in eastern Australia than the carbon price. Even with the removal of the carbon price that is anticipated, that is unlikely to have a big impact on gas demand, but the doubling of wholesale gas prices, if not tripling wholesale gas prices will have a much bigger one, so right now the predictions really are that gas demands will be quite flat for the next 15 years in eastern Australia.

Mr ROBERT FUROLO: That will have an impact on investment decisions for transmission.

Mr DAVIES: That is right. That makes it hard to see major new investments going ahead. In my opening statement I did refer to a couple of investment announcements that happened lately in expanding the transmission network's capacity to bring gas out of Victoria into New South Wales. There would probably be a bit more happening there, bringing gas out of Victoria into New South Wales but apart from that, the transmission network seems fairly adequate at the moment and it is just a matter if the gas keeps flowing in the directions it has traditionally.

CHAIR: With respect to the membership of the association, what does one have to do to be a member of the association? Is it open to anyone to join?

Mr DAVIES: Yes it is.

CHAIR: Or do you have to be in the industry?

Mr DAVIES: No, you do not have to be in the industry. As I said, we have 400 members and there is not nearly that many transmission pipeline owners in Australia, so a lot of it is service industry to the broader gas sector, whether it is equipment suppliers, manufacturers of pipe, also the environmental consultants and legal firms that specialise in resources are our members. We have many individual members but obviously our primary purpose is to serve the interests of the gas transmission industry. Whilst anyone can be a member there would be some decisions and positions that we advocate publicly that you would not have input to, that is something that is reserved for owners of transmission pipelines to help us form our positions.

CHAIR: So there are effectively different classes of member in your association?

Mr DAVIES: Yes.

CHAIR: Is there a cost associated with being in each different class of member, is that how it works?

Mr DAVIES: Yes, that is right. Associate memberships for a business are around a thousand dollars and then outside of pipeline owners, the highest cost that an industry body or a company is asked to pay is around $10,000 and then transmission pipeline owners pay association fees based on the kilometres of pipeline they own.

CHAIR: Mr Davies, thank you for appearing before the Committee today. We are very grateful to you for making the trip from Canberra.

The Committee may wish to send you some additional questions in writing, your replies to which will form part of your evidence and be made public. Would you be happy to provide a written reply to any further questions the Committee may have?

Mr DAVIES: Yes.

(The witness withdrew)

(Short adjournment)

CRAIG ANTHONY DE LAINE, Group Manager - Regulation, Envestra Limited, Level 10, 81 Flinders Street, Adelaide, South Australia, and

ANDREW STANIFORD, Group Manager - Commercial, Envestra Limited, Level 10, 81 Flinders Street, Adelaide, South Australia, sworn and examined:

CHAIR: I would like to welcome Mr Craig de Laine and Mr Andrew Staniford from Envestra Limited. We are delighted that you can join us today. Thank you for being here. Could you please both confirm that you have been issued with the Committee's terms of reference and information about the standing orders that relate to the examination of witnesses?

Mr de LAINE: Yes we have.

Mr STANIFORD: Yes.

CHAIR: I would also be grateful if you could state the capacity in which you are appearing before the Committee today.

Mr de LAINE: My name is Craig de Laine, I am the Group Manager - Regulation at Envestra Limited and that is my capacity from which I am representing our company at today's Committee.

Mr STANIFORD: My name is Andrew Staniford, I am the Group Manager - Commercial at Envestra Limited, involved with the commercial parts of our business which we have addressed in our submission and that is the part that I will be representing today.

CHAIR: We have received a submission from your organisation. Do you want the submission to form part of your formal evidence?

Mr de LAINE: Yes we do. Although I might just state, the main purpose of the presentation is just for today's meeting. We thought it might be a useful way to provide a short overview prior to proceeding if you agree that would be useful.

CHAIR: I think that is a very wise way to proceed. Before we do so, do you have any questions concerning the procedural information sent to you in relation to witnesses and the hearing process?

Mr de LAINE: No.

CHAIR: Would you like to make an opening statement before we commence? I assume we could probably take that as part of your opening statement.

Mr de LAINE: That is our opening statement.

CHAIR: Perhaps we can commence by having a look at this material now and if you could take us through it.

Mr de LAINE: The first slide was simply an introduction to Andrew and me. I think we have gone through that as to what our capacities are and what our responsibilities are with Envestra Limited.

We would like to start by thanking you for providing us with an invitation to appear before the Committee today. We will run through this presentation but at any time please interrupt if you would like to ask a question. We are in your hands.

In terms of an overview today, we thought we would start by just providing an overview of our company, including where we operate, what our key objectives are, the key objectives of our business, what we are trying to achieve. Then we thought we would move onto some of the more substantive things that we covered in our submission in areas where we think a Committee such as this can help our business provide or expand gas distribution networks in New South Wales.

Really the two areas relate to the regulation of our assets and government policy that sits around the provision of natural gas distribution services. What we are trying to get at is really addressing matters that go to the risk to our business in providing those services. That is where we think we can be of assistance in this capacity.

Firstly the overview of Envestra Limited, we are a publicly listed company that was formed in August 1997. Our company was formed at the time and still does, have a mandate of providing natural gas distribution services.

We have a diverse shareholder base. We have two large shareholders or two major shareholders if you like, they are the APA Group, who own 33 per cent of the company and CKI, who own 17 per cent of the company. The remaining 50 per cent is split between retail and institutional investors.

CHAIR: Who is CKI?

Mr de LAINE: CKI is a Hong Kong based infrastructure company. They have various infrastructure assets in Australia. They are a very big global player in the infrastructure market. For example, they own South Australian Power Networks, formerly ETSA Utilities. They own Victorian Power Networks, formerly CitiPower and Powercor and they have an ownership in Spark Infrastructure; so a significant infrastructure player.

We have an enterprise value of around about $4 billion and our distribution network is just over 1.1 million customers spread across south eastern and eastern Australia. Our largest networks are in South Australia and Victoria.

In New South Wales our interests are perhaps a little smaller at this stage. We own two small regulated distribution networks, one in Albury and one in Wagga Wagga. Combined they account for round about five per cent of the company's total revenue.

The next slide is really a diagram of where our networks are and that is really for the interests of Committee members that you might like to look at at some other stage. It just really provides some more detail on exactly where our networks are.

CHAIR: You have got small networks in Albury and Wagga Wagga, can you just elaborate on what you have got in those areas?

Mr de LAINE: Firstly in Wagga Wagga, we acquired that network in October 2010. We acquired the network from Country Energy, so we are a new owner of that network. I have got to get the metrics—we serve around 20,000 customers in the Wagga Wagga region and it has an annual revenue of around about $10 million a year.

We serve the entire city of Wagga Wagga. We also serve surrounding areas of Wagga Wagga through our unregulated distribution networks.

In Albury the network is of similar size in terms of customer base. It has got a lower revenue recovery though, but it is also a regulated network. When I say a regulated network, as you know, we are a gas distribution business, we are a natural monopoly at least at face value and for that reason we come under regulation. We come under the national gas law. We are regulated by the Australian

Energy Regulator.

CHAIR: In Wagga Wagga for example, what infrastructure do you actually own?

Mr de LAINE: The infrastructure that our company owns, we are mainly a distribution company but we do own some transmission network. The transmission networks take the gas at higher pressure and deliver it to the metropolitan urban centres. We own some transmission. We own all the distribution network, or the mains if you like, in the urban areas that supply customers, that supply large industrial, commercial and residential customers and we also own the meter.

Our infrastructure can be broadly thought of from when it reaches an urban area to where it reaches the customer. So beyond the meter, that is not our responsibility.

CHAIR: With respect to Wagga Wagga, what transmission infrastructure is there? Is it just a single pipeline or what do you have there?

Mr de LAINE: Yes it is. It is a single pipeline.

CHAIR: That links the network to the major pipeline, is that how it works?

Mr de LAINE: Exactly. Yes, that is right. So the transmission side of it is really quite small. I would say at a slight guesstimate it accounts for probably around five per cent of our total asset base in Wagga Wagga. The main assets and the core business is about distribution pipes.

In terms of the objectives of our business, the fundamental objective of our business is to increase the volume of gas that flows through our infrastructure. We do this primarily in two ways. We do this by increasing the number of connections to the network and we also aim to increase the average usage per connection. They are the two basic ways that we go about increasing volumes through our network.

The reason why this is so important is because we are an infrastructure business. We are a high fixed cost business. The more volume we get through our network, the lower the average cost to service provision and the lower the average cost to service provision, the lower the average price to consumers of using gas.

That is a particularly key element for our business, being a fuel of choice. Gas is a fuel of choice, which is how we differentiate it from say, electricity, which is more an essential service. If you have gas, you have to make the choice to have gas at your business or residential premise. That is why that is our fundamental objective and that is how we go about achieving it.

As we said at the outset, government policy can be crucial in terms of allowing Envestra Limited to achieve our objective and we think it can be grouped into two areas. One is regulation, so how those networks are regulated, and we will get to that. The other one can be through various government programs.

In our submission, and what we will elaborate on further today, is just some examples of government policy and how that can facilitate providing gas distribution infrastructure, particularly to regional communities.

In terms of Wagga Wagga, what you have before you now is a topical and current example of how the New South Wales Government can assist our business improve the environment for providing gas infrastructure in that particular area.

Just to give you a little bit more background on the Wagga Wagga network—we have covered it already courtesy of the question before—Wagga Wagga accounts for around about two per cent of our total revenue. It is the smallest regulated network that we own. It faces vigorous competition from the electricity sector. The asset or the infrastructure there is significantly under-utilised. It has an average capacity utilisation of around about 20 per cent. So there is an opportunity there to grow the connections and to grow the volume in that particular area without our business incurring significant cost.

It is under-utilised and probably most importantly to where we are at now with the New South Wales Government is there are two retailers in Wagga Wagga, one of which controls 98 per cent of the market and that situation has persisted over a long period of time.

Where we are at with this network, as I mentioned earlier, we acquired the network in October 2010. Due to the facts that I have just outlined to you before, particularly low asset utilisation, lack of retail competition in the area and strong competition from electricity—and that is overlaid by the fact that gas is a fuel of choice—we applied earlier this year to the National Competition Council to have coverage revoked from the network.

What that means essentially is to have regulation of our network removed. The principle reason for that is that the national gas law sets out certain criteria that must be satisfied before a network is covered or regulated. We say—and we have submitted and we have put the evidence forward—that those criteria are not satisfied in the case of Wagga Wagga.

CHAIR: Why not?

Mr ROBERT FUROLO: What would it mean?

Mr de LAINE: I will get to both of those questions. I will get to the why not first and then what it means.

Firstly, the why not; we say two of the four criteria are not satisfied but I will focus on one of those criteria. One of the criteria states that coverage or regulation is required in order to promote competition in a downstream market or upstream for that matter.

As part of that process all parties, and when I say all parties, Envestra Limited and the National Competition Council and all stakeholders to the process agree that the only relevant market whereby our business can influence competition is in the retail market.

Now with the Wagga Wagga market, the New South Wales Government has set up legislation that has allowed retail competition to take place over a 10 year period and at the moment we are in a situation in Wagga Wagga where there is only one active retailer—there are two retailers there but we say there is only one active retailer in Wagga Wagga—who controls 98 per cent of the market.

There is a lack of retail competition in the market. We think it is a no-brainer. We think there are clear reasons as to why there is a lack of retail competition in that market.

CHAIR: What are the reasons?

Mr de LAINE: The reasons essentially come down to the small size of the market and the risks that a retailer and the costs that a retailer must incur to enter that market. The small size of the market means that the risk trade off is not there. It is a cost benefit to the retailers that the retailers weigh up. We say that over the last 10 years they have weighed up the costs versus the benefit of entering that market and they have since decided not to enter the Wagga Wagga market. We think that that situation will more than likely continue over the medium term.

Mr DARYL MAGUIRE: What you are saying is if the market is opened up it will drive down prices for the consumer and it will allow you to expand the network?

Mr de LAINE: I guess our principal argument is that our network should not be regulated because the criteria and the national gas law are not satisfied. We agree with your contention though, it comes without saying, the more competition there is in a retail market, in the competitive market, the lower prices or the better terms and conditions there will be.

The Wagga Wagga market does not have that at the moment and as a result of that the market is regulated currently. Minister Hartcher and the wider New South Wales Government is currently deciding on whether to remove retail price regulation in that market. That is the retail side of things, the more competition the lower prices. It is quite fundamental.

From our side of things, to answer your earlier question, what are the benefits. There are clear benefits to the people of Wagga Wagga and to industry of Wagga Wagga if regulation is removed from our network. What we have put to the Minister as part of our application is that if a decision is made to remove the regulation of our distribution networks in Wagga Wagga, we will reduce price immediately.

Mr DARYL MAGUIRE: By how much?

Mr de LAINE: At the moment it is a regulated network. We have a regulated approved tariff increase, a real tariff increase of 2.5 per cent from 1 July 2014. We have said that we will forego that price increase, we will not apply it and for the remaining five years, price increases will be no higher than the consumer price index, which I guess is particularly counter to where energy prices have been over the recent period.

For example, the Australian Energy Regulator approved a 25 per cent uplift in our tariffs over the most recent five year period. We are saying we are not going to do that. We want to hold prices to be at or below the consumer price index.

Mr DARYL MAGUIRE: Will the abolition of the carbon tax have an effect on pricing as well?

Mr de LAINE: No it will not because the network is not liable to pay carbon tax. It is not big enough.

Mr DARYL MAGUIRE: Not at all?

Mr de LAINE: No.

Mr DARYL MAGUIRE: Not in anything that you do?

Mr de LAINE: No. In our bigger networks we pay the carbon tax, and that is really governed by Commonwealth legislation. They set thresholds or limits as to when your asset or infrastructure is liable to pay the carbon tax. That essentially is based on the size of the network and the Wagga Wagga network is too small. So it does not get over the threshold.

Mr DARYL MAGUIRE: Too small by how much?

Mr de LAINE: I do not know exactly but it is a significant amount. We are dealing with a very small network here. I will give you an example. Say there are 20,000 customers in Wagga Wagga, in our Victorian network we have around about 550,000. From Wagga Wagga we receive around about $10 million in revenue a year. From our Victorian network—to stick with that example––we recover around about $250 million per year.

The issue we have with both of those networks, they are regulated in exactly the same manner. They incur very similar costs as a result of that regulation and that is because with each of those networks the national gas law and the related national gas rules are very prescriptive. They set out a range of requirements that a regulated network must satisfy in order to set a five year price path.

We are saying if we avoid those costs, if we avoid that red tape then we will reduce our costs by quite a significant margin and we will pass that straight back to consumers. That is a starting point for us in terms of Wagga Wagga and we have committed over the five years following, to give price certainty to consumers, to industry to say for the next five year period we will not increase our prices by an amount that is greater than the consumer price index. Our discussions with industry suggest that that would be quite welcome.

Mr DARYL MAGUIRE: In your opening remarks you made a comment about the recovery in Albury is lower than Wagga Wagga. Can you expand a little on that please?

Mr de LAINE: That is essentially driven by the size of the asset base. The asset base in Wagga Wagga is a lot higher than it is in Albury. As I said at the start, we are a fixed cost business. We derive at least 50 per cent of our revenue through the returns we receive on our regulatory asset base. The asset base in Wagga Wagga is twice the size of the asset base in Albury.

That is fundamentally the difference as to why revenue is higher in Wagga Wagga than it is in Albury and that is an historical thing. That relates to a range of factors, including the cost of providing infrastructure in both areas.

Mr DARYL MAGUIRE: Can you enlighten the Committee on infrastructure and access charges for infrastructure that perhaps is not utilised by every householder but exists? Is there a charge?

Mr de LAINE: No there is not.

Mr DARYL MAGUIRE: There is with energy and with water.

Mr de LAINE: There is with water, that is right but in our case how we work is, to use an example, say there is a street in Wagga Wagga. There might be a hundred houses along that street. Unlike electricity where every one of those hundred households will connect, we might pick up say 90 of them. But because of that we might get a house at the front of the street and a house at the end of the street, we are required to run our gas pipes all the way down to get the customer at the end of the street.

So the infrastructure is there. It is in the ground. But we, as a fuel of choice, need to actively compete. We want all of those one hundred households to connect. At the moment we probably get about 85 to 90 of those households connecting. Those who do not connect do not pay any charge. But the infrastructure is there if they do want to connect.

Mr DARYL MAGUIRE: In your submission you make reference to the Victorian Energy for Regions program. You have suggested that there are 12 priority towns. You have already agreed to increasing gas distribution to the Mildura network and you are in advanced negotiations with two more towns. You then name a number of towns that I am particularly interested in, The Rock, Lockhart and Tumbarumba. Batlow would be another one that I would add as a town that has been campaigning for access to natural gas.

Will this kind of program, if adopted, assist you and if the program is not adopted by government or a similar program, what will it take to allow those communities to access natural gas, understanding that not all of them will take up access to natural gas in the first couple of years?

Mr de LAINE: Yes.

Mr DARYL MAGUIRE: What kind of timeframes would be acceptable as appliances deteriorate and change over to gas or the alternative energy take place?

Mr de LAINE: That is on the next slide, those sorts of matters we are dealing with. We will get to that now.

Just to give you a bit of light, to take you back to the first part of your question, how access charges are determined. I mentioned the national gas rules and the prescriptive nature of those national gas rules. What they require is they have an economic test that governs all the expenditure that we incur.

For example, if we incur capital expenditure we have to demonstrate to the regulator, the Australian Energy Regulator, that there is a net positive economic flow through to consumers from expanding that infrastructure.

Mr DARYL MAGUIRE: What about an environmental flow through benefit?

Mr de LAINE: I am not sure. There is no environmental criteria in the rules. There is certainly a safety criteria. There is an economic test and a safety test.

With the Victorian Government Energy for the Regions program, which we highlighted in our submission, what that essentially recognises is that people in regional communities can be at a disadvantage and that is not right. They are at a disadvantage because of where they live. In the case of our business, they live quite often at a distance away from the transmission network and as a result of that they are quite costly to provide the infrastructure to. Because of the cost of providing the infrastructure, the problem we have, and this is why we are so keen to get the Wagga Wagga network unregulated, is if we take the initiative or the innovation to supply those customers now, we run the risk of the regulator, and in these cases it is a no-brainer risk for the regulator, to say Envestra Limited you have spent X million dollars in supplying the infrastructure, but the benefits of that infrastructure provision do not outweigh the cost, so we are not going to allow you to recover that money. So we have no capacity to recover the expenditure that we incur.

What the Government has said is we recognise that particular networks that we own in Wagga Wagga are regulated and we recognise that there is an economic test that sits around the capital expenditure that you incur, so we will provide you a subsidy. The minimum subsidy that is required to provide the infrastructure to those regional communities such that the amount that you spend will be accepted by the regulator and you will be able to recover your proportion of the capital expenditure. That is essentially how the program works.

They are competitive programs. They are competitive tenders for the regions. We are active in all of those regions that make sense for our business, particularly the ones close to our existing networks. We work close with the Government.

So what happens is there is a competitive process. The Government then chooses a successful tenderer, who it will then enter into further negotiations with and those negotiations will be around economic modelling. What you need to do is to do an economic study, which says what infrastructure is required to supply these networks, what transmission lines, what distribution lines, how many customers do you think you will connect, what industry do you think you will attract, essentially how much money do you think you will generate from the region versus what costs you will incur to supply it.

Engineering assessment on the cost, economic feasibility on the cost and the revenue and that works out how much subsidy is required to provide the infrastructure. Then the Victorian Government has a scheme currently where it provides $100 million out of its $1 billion regional development fund which goes towards these 12 priority towns.

That is essentially how the scheme works and without that scheme we would not be in the discussions we are now. Like you said, we are in discussions with three of the 12 priority towns. In one case, a project which is already advanced, we have been approved and the project is commencing in Mildura. It has already attracted a fruit producer to locate within our boundary to take advantage of the lower cost fuel in natural gas. So we are already seeing a benefit in the one project that has kicked off.

Mr DARYL MAGUIRE: Who are the key drivers in the process? Are local government involved to a great degree or is this basically industry driven?

Mr de LAINE: Andrew, I am not quite sure if you can help me out here, in terms of who is primarily involved, clearly I think the local members have been successful in lobbying their peers to get this significant fund in place. I am not privy to those discussions and negotiations obviously.

The interesting thing with Victoria is it is heavily Government driven, it is driven by the Government and it is also driven by the Government because of the benefits that flow through to industry. It is a really pro-economic development initiative of the Government, but it is also pro-choice for the Government. I think there is an environmental initiative there too because obviously natural gas is a low carbon intensive fossil fuel. It is the lowest carbon intensive, so it has got an environmental slant, which is arguably increasingly important now with recent changes at a federal level with climate policy.

Mr STANIFORD: Can I clarify, just on running the program it really is a Victorian Government initiative. Regional Development Victoria are the department who make the money available, who go through the auction process that Craig has talked about and who make decisions about which towns would be eligible for the scheme.

If one of our bids was selected, we go into a process of negotiation with the Government. We actually have a contract with the Government to deliver certain milestones in certain timeframes and in exchange of that we get a contribution to underpin the cost of building the network.

So it very much is a Government thing but behind that there is the Local Governments and the local regional development authorities obviously have close networks into the Government and are involved in, I would imagine, the initial scoping of towns that might be eligible that are eventually chosen by the Government to be part of the scheme.

Mr DARYL MAGUIRE: That is what I was trying to get at, because most of those Local Government areas are very proactive when it comes to trying to attract industry.

Mr STANIFORD: Yes.

Mr DARYL MAGUIRE: In the case for instance of Tumbarumba and Batlow where I once represented, there is also an issue now with the bigger industries using waste product to fire their boilers. It has gotten to the stage where the waste product is actually more valuable than the cost of natural gas. They then become a base load consumer and the councils would be of course very proactive in trying to bring about some resolution to it.

I understand with places like Tumbarumba and Batlow for instance, they have already done the numbers and again the base load consumption was not adequate to drive the case for gas, but now because of the cost of those fuels there actually burning, it has actually become more viable. That is what I understand.

But in places like Lockhart for instance, they are desperate for industry and again the household base load consumption just is not anywhere near enough to drive the case to put gas on. So the Victorian model obviously is producing results.

Mr de LAINE: It is.

Mr STANIFORD: There are two towns where there has been an immediate response from industry and that was Bairnsdale, which is a town we did some time ago where Patties Foods, which is a major pie producing company, basically once gas was there was able to double the size of its production facilities. The other one that Craig mentioned is Lamattina in Mildura who have been out in the Sunraysia area somewhere but using liquefied petroleum gas as a fuel, they have relocated their plant closer to the pipeline but it has given them access to natural gas and will underpin their program going forward.

Mr DARYL MAGUIRE: I actually fear that unless we find a way to get gas to those smaller towns like The Rock, Lockhart, Batlow and Tumbarumba et cetera then cities like Wagga Wagga will continue to be the sponge and really those communities, those councils, want businesses in their region. They have got industrial parks created. They will do anything to get a business there but the odds are still stacked against them; but Bairnsdale is a good example.

Mr STANIFORD: The real problem from our point of view with providing gas to regional towns is if you look at the town itself, often there is enough local demand there to underpin the investment. There might be some industry or there might be some commercial premises or there is some residential consumption, but the problem that we have is when you start applying the tests that Craig was talking about in the code, you need to build a transmission line from the existing infrastructure to that town, a large supply line and it is often with that supply line that we run into problems with the regulatory framework.

With all of that investment, it just does not satisfy the economic tests that we need to demonstrate.

Mr DARYL MAGUIRE: Once the supply line is installed, let us say it is 50 kilometres, what would the upkeep be on a 50 kilometre gas pipeline? Is there regular maintenance that needs to occur? What needs to be done to maintain that infrastructure and at what cost?

Mr STANIFORD: Generally, as Craig mentioned, most of our costs are fixed costs. It is actually getting the infrastructure in the ground to start with. There are annual operating costs but they generally are more along the lines of looking after regulators and meters, making sure they are not leaking, doing drive passes down the pipeline to make sure there are no leaks.

Generally those costs are quite small compared to the initial cost of the infrastructure. Operating costs as a percentage of total cost is quite small.

Mr de LAINE: We take on that responsibility.

Mr STANIFORD: That is our business. We have got all the infrastructure to do that. Those costs, because they are small, they can be recovered from the revenue that we generate from the network. So there is no issue with that.

Mr DARYL MAGUIRE: You are confident with deregulation in say the Wagga Wagga area, it will drive down prices for consumers?

Mr de LAINE: Yes we are.

Mr DARYL MAGUIRE: As well as attract more industry and allow you to expand the network?

Mr de LAINE: Yes we are.

Mr DARYL MAGUIRE: Absolutely confident?

Mr de LAINE: Absolutely confident.

Mr DARYL MAGUIRE: That is what I wanted to hear.

Mr de LAINE: Just to close off on that one as well, that issue is currently before Minister Hartcher. We are hoping that he will make a decision towards the end of this year. If not, it will be early next year, so it is right before the Minister now as we speak.

Mr DARYL MAGUIRE: Are there any concerns that will be raised by the community that will need addressing, because any time that you move to deregulate anything there are always concerns that are raised? What can you see on the horizon?

Mr de LAINE: We did a public consultation process prior to putting in our submission where we went through Wagga Wagga and spoke to our large industrial customers. We did not meet with residential consumers mind you, but we spoke to the large industrial customers and they expressed general support for what we are doing. They expressed general support for the initial decrease in energy price and the certainty about what those prices will be because it allowed them to more effectively plan.

I guess we are working against a backdrop where right across Australia there have been significant increases in infrastructure costs, so this really turns the table, we think, on what has been happening. Like I said, even in Wagga Wagga prices were approved to go up by 25 per cent over the current five year period. We are saying we are going to lock them down.

Mr ROBERT FUROLO: Your suggestion was that price controls would apply for five years at the consumer price index or below.

Mr de LAINE: Yes.

Mr ROBERT FUROLO: What protections do the consumers, businesses and residential customers have post five years if their area is not regulated?

Mr de LAINE: That is a good question and that probably comes to the question you had as well about what potential concerns might there be. With our business we say that what protection the consumers have comes really down to the fact that gas is a fuel of choice. Like I said with that example before, we go down a street, there are a hundred households there, we do not connect all of them because not everybody needs natural gas.

The Wagga Wagga market, unlike Albury, is in an interesting position in regards to the cost competitiveness of natural gas relative to electricity in that particular region. We are in vigorous competition with electricity to get customers and that is our driver in terms of increasing higher volumes.

It is against our interest to do anything but lower prices to consumers. That is the protection they have.

Mr DARYL MAGUIRE: And the competition factor.

Mr de LAINE: And the competition factor, exactly right. So we have competition with our networks and the retail competition side as well.

Mr ROBERT FUROLO: Who is the electricity provider in Wagga Wagga?

Mr DARYL MAGUIRE: Essential Energy.

Mr de LAINE: Yes, that is right.

Mr ROBERT FUROLO: Liquefied petroleum gas distribution, do they offer that?

Mr DARYL MAGUIRE: No, they had it and then they split it.

Mr de LAINE: They sold it.

Mr STANIFORD: We purchased it from the predecessor of Essential Country Energy.

Mr ROBERT FUROLO: Were you worried that they might re-amalgamate down the track and not regulate it?

Mr DARYL MAGUIRE: Who can predict what happens with business.

Mr de LAINE: I might point something else out in terms of your concern; at any time any member of the community, a householder, can apply to the National Competition Council to have the network recovered. Just as we are applying to have regulation removed, any party, be it a retailer, be it an industrial consumer or be it a householder, can apply to the National Competition Council to have regulation put back on the network.

So that is a fair protection that I think is highly relevant. We do not think it will ever get to that. We will just note as a side point that during our ownership of the network we have not had one dispute with a retailer. We have not had one dispute with an industrial customer or a residential customer.

I might just make one other point in regards to the Energy for the Regions program that we have just discussed. That is the current program that the Victorian Government has. Prior to that, in 2003 they had a program which was called their Natural Gas Extension program. That program was also highly successful. As a result of that program we took our networks to eight further regional centres in Victoria.

There has been a lot of activity on behalf of the regional government and a lot of willingness from businesses such as Envestra Limited to participate in those programs. This is the second program, the current one that we have, the Energy for the Regions program.

So all in all for our own business it has resulted in 13 additional regional centres being connected to the gas distribution business infrastructure that otherwise would not have had access to gas.

Mr ROBERT FUROLO: Just to clarify on Energy for the Regions program, it is a competitive process?

Mr de LAINE: It is a competitive process. Just to go back to the point Andrew made, how it will start is the Victorian Government has selected what it thinks are its priority towns.

Mr ROBERT FUROLO: Do you know on what basis that is determined?

Mr de LAINE: I believe size, interest and potential for economic development.

Mr STANIFORD: I think on that they do have a consultant advising them; so they have done some economic analysis to understand—

Mr ROBERT FUROLO: It is not just pork barrelling.

Mr STANIFORD: That is right; there is some sort of analysis that goes behind it.

Mr ROBERT FUROLO: So there is some metrics around it?

Mr STANIFORD: They are advised by an analyst, they had KPMG I think it was who advised them; so there is some analysis that sits around it. They probably get pork barrelled over a number of towns, but then out of that they ended up with the 12 what they call priority towns which came out of that analysis that they did. They were the ones where they deemed there was the most potential.

They then went out to the competitor tender process for those 12 towns but when they went to that tender process, they also left the option open that companies could provide, if we thought there was another opportunity that had not been identified by the process that the Government had gone through, we were able to make that known at that point and put in a non-conforming bid. Then that would be assessed in the process. But we did not actually do that, we just stuck with the priority towns.

Mr ROBERT FUROLO: The subsidy that is ultimately determined is a combination of negotiation between the proponent and the Government?

Mr de LAINE: It is. It is very much a negotiation.

Mr ROBERT FUROLO: Is there any independent analysis of those figures?

Mr STANIFORD: There is. Again, in Victoria the Government had their advisor. The process starts with us putting forward a bid. We estimate the cost of reticulating the network to the town. We calculate an indicative subsidy that will be required to be able to bring that to fruition. That then is taken by the Government and they go back to their advisor and they do their own analysis. They invariably come up with a different number, a different view and then there is a discussion where basically we get engineers in a room and we work through the issues.

That can come down to things as simple as pipeline route, adjusting pipeline route to minimise cost or other views of demand, potential new customers, that sort of thing. But that is a collaborative process and eventually in the towns that we have gone ahead with, we end up with some agreement about the cost that we think we could do it for and what the Government would be prepared to contribute.

Once we get to that point, we then move into the next stage, which is developing, like I said before, a contract where we commit to do certain things. Basically that is, we commit to provide a certain footprint with access to natural gas and it is usually done in a staged manner which recognises the cost profile of putting the network in. We get part payments, so three payments say. One payment on the end of finishing the supply main, another one when you get the trunk mains in and then a third one when the rest of the reticulation is in or something like that. So it is a staged payment scheme.

Mr ROBERT FUROLO: Is there any analysis on the post delivery benefits, economic activity that is directly attributable to that investment, any environmental outcomes directly attributable to that investment? So the taxpayers would be able to determine what benefit they have derived from that investment?

Mr STANIFORD: As far as I am aware, I do not believe the Victorian Government has done any analysis like that, but certainly from our point of view, we have done an analysis. The one that I have most recently done is the Bairnsdale one where we came up with certain forecasts and the question was asked before about uptake rates. This was done in 2005 or 2006, that period, so it is some years on now. We did this post audit of what had happened.

Generally what we found is the capital costs were basically as expected, apart from one increase, which was due to some heritage issues that we came across when we started digging the pipeline and that involved some additional survey work which we had not contemplated. That was a cost that we bore as a result of that. There was no capacity at that point to re-open that.

Then we found that the uptake rate over the period was lower than what we expected. That reflects the fact that although natural gas can be cheaper, there is actually a cost of converting from the existing appliance, whatever it may be, to natural gas. With liquefied petroleum gas that is relatively easy and what we found is it is important to have some sort of a connection offer to customers to help them fund that conversion.

Mr ROBERT FUROLO: Appliance changeover.

Mr Staniford: Appliance changeover. So in these programs we have a focused program where we try to provide that kind of support and information to assist it. But in the longer term, people still will not want to replace appliances often until they expire and die.

You tend to get a delay when appliances are changed over. That is exactly what happened in Bairnsdale. Our forecast was below what we expected it would be in the early stages but we have now reached the point where basically we are on track as we had forecast; so it is looking pretty good.

CHAIR: Gentlemen, I have just been having a look at the National Competition Council's determination if you like. There were a number of submissions, particularly from retailers, which disagreed with your assertion that coverage would not materially promote competition. What do you say about the position that, for example, the retailers took?

Mr de LAINE: It has been an interesting process. We say the retailers acted in their own interests in putting those submissions forward. It was clear to us by the nature of those submissions and the common content of those submissions that they organised themselves to act in their own interests. They were successful in their applications to the National Competition Council, who accepted those submissions at face value. The National Competition Council did not test those submissions. The National Competition Council in our view did not do the analysis it should have done around those submissions to test whether what the retailers were saying was accurate.

We believe the New South Wales Government is aware of those issues and is aware of those concerns that we have. We are hopeful that the New South Wales Government will do the analysis and the testing that is required and that was put in our submission.

Once that testing is done it will be clear that what we have observed over the last 10 year period, and that is a fact, what we have observed over the last 10 year period is one dominant retailer who still controls 98 per cent of the market. What we have explained in our submission is that the reason for what we have observed in the past is that there are high costs of entering that market and there is a low potential benefit from that market entry.

When I say retailers are acting in their best interest, this whole process that we have put forward has been convoluted with another process that is before the New South Wales Government which concerns the removal of retail price regulation.

The retailers, when we say they were acting in their self interest, were concerned that any decision made on our network might impact the decision the New South Wales Government might make in regard to retail price regulation. That is their capacity that we believe they were acting in when they were putting their submissions forward. That is their main game at the moment. They are purely focused on getting retail price regulation removed.

They saw our submissions and our process, particularly through highlighting the lack of retail competition in regional areas as potentially harming that. They then went into defence mode to protect the bigger game that they have and that is freeing up retail markets in New South Wales.

What is before the Minister now, the Australian Energy Market Commission put in a submission which was very important and the Energy Networks Association also put in a supportive submission. The Australian Energy Market Commission was responsible for the final recommendation on retail price regulation and made it very clear to the National Competition Council that any decision that the National Competition Council makes regarding the regulation of our network will have no bearing on its recommendation regarding whether retail price regulation should be removed.

That is, our network will not impact that decision, although the Australian Energy Market Commission in its final decision said if the New South Wales Government is concerned by the lack of retail competition, then it can continue voluntary pricing arrangements in those regional areas to address those specific areas.

The National Competition Council followed on by saying if that were to occur then our network should not be regulated.

That is probably a longer answer but clearly what I was trying to get at there is that our process was mixed in with another process, that may have impacted where the retailers want to get to with retail price deregulation so they grouped together and they put an argument against; all of which arguments we have proved to be incorrect.

CHAIR: Gentlemen, thank you very much for appearing before us today. We certainly appreciate you taking the time and also for your contribution towards the work of the Committee.

The Committee may wish to send you some additional questions in writing, the replies to which will form part of your evidence and be made public. Would you be happy to provide a written reply to any further questions?

Mr de LAINE: Yes we would. We are happy to participate in whatever capacity we can.

CHAIR: Can I again thank you for your submissions. I think we all found them very helpful and you have certainly assisted the Committee in its work.

(The witnesses withdrew)

(The Committee adjourned at 12.34 p.m.)