14 October 2022

Ms Anna Collyer
Chair
Australian Energy Market Commission
GPO Box 2603
SYDNEY 2001
Lodged via submission page

Dear Ms Collyer

Re: Hydrogen blends and renewable gases reforms

Thank you for the opportunity to provide feedback on the draft National Gas Rules (NGR) to accommodate hydrogen blends and renewable gases published on 8 September 2022.

We are pleased to see the Commission progressing with changes to the NGR and consider it to be an important enabler to transition networks to supply lower emission fuels and meet net zero targets.

Our comments on the draft NGR have been based on our understanding of the draft regulatory package of changes to the National Gas Law (NGL) provided in March/April 2022. Given the complementary nature of the NGR to and the NGL, it is difficult to fully assess implications without the final version of the regulatory package.

In particular, the inclusion of blend processing in the NGL as a related business creates complications. Blending infrastructure is physically connected and linked to the existing distribution network of the service provider and will be complex to separate. Complexities include the need for a service provider to maintain some level of control over safety related to the blend mix and the resulting gas quality delivered by ATCO's reticulation network and therefore this integrated infrastructure cannot be simply assigned to an associate to operate.

Our feedback on the draft NGR focuses on:

- Ensuring new reporting requirements for service providers reflect the ability of the pipeline to accept gas types
- Incorporating a grace period for ring fencing
- Shortening the advance notification requirements for associate contracts
- Providing certainty on the circumstances concessional finance will be treated as a capital contribution
- Consistency and clarity in transitional provisions for ATCO's existing hydrogen projects and the ability to provide for their cost recovery as well as other investments made up until the rules commence.

It is noted that the draft rules do not allow pipeline services providers to produce any quantity of covered gas. ATCO considers an exemption from minimum ring fencing requirements should exist to allow pipeline service providers to have the ability to produce small quantities of renewable gases to a threshold level. Small production quantities will allow the continuation of industry development and will not impact competition in the markets for the supply of renewable gases.

New reporting requirement on gas types and changes

ATCO supports measures to provide access to information that will enable the efficient use of pipelines to transport covered gases. We note that draft rule 101B (2) will require service providers to publish a range of information about the type of gas transported. However, some of the information identified (Draft rule 101B (2) (h)) requires service providers to publish information on potential future changes to the gases being transported through the network that are impacted by a range of factors outside service providers control.

Service providers have the ability to ensure the readiness of the network to accept various gas blends, but its ability to determine when this will occur could be impacted by a range of factors outside its control. It is anticipated that likely drivers will be government policy or customer demands. It is unlikely the service provider will have information available to meet these requirements so as to be able to notify future changes in advance. It is suggested that the drafting of this rule, particularly part (h) focus on the service provider's readiness and ability to transport gas types and its potential to accept these in the future.

Ring fencing

In addition to the transitional ring fencing exemptions afforded to service providers for existing hydrogen projects, the increased scope of what would constitute a "related business" requires service providers to be afforded a grace period from compliance with section 140 of at least 12 months. Broadening the scope of what constitutes a related business means that certain activities undertaken by associates may now fall within this definition such that these associates will need to be considered in respect of compliance with section 140.

A grace period would allow ATCO Gas Australia as a service provider time to meet the restrictions relating to marketing staff of these associates that may now take part in a related business. As an example, ATCO Australia's Clean Energy Innovation Park project, https://www.atco.com/en-au/projects/clean-energy-innovation-park.html, will involve the production of hydrogen. Under the new rules, ATCO Australia will therefore be considered an associate of ATCO Gas Australia that takes part in a related business and ATCO Gas Australia will be required to ensure the segregation of marketing staff between these entities. While cost separation is already undertaken, the grace period would allow consideration of the current structure of ATCO Gas Australia and these associates that may now be carrying on a related business, obtaining legal advice and implementing any necessary reorganisation of staff.

It is noted that, when ring-fencing rules were introduced by the Australian Energy Regulator (AER) for electricity distribution businesses, a 'grace period' of around 15 months was allowed for businesses to implement ring-fencing measures for existing activities. The AER published the first version of its ring-fencing guideline in October 2016, but only required compliance by 1 January 2018. The AER noted that immediate implementation of the new ring-fencing obligations would create costs for distribution businesses as they amend their corporate processes and structures to comply with the new arrangements (costs that would ultimately be passed on to customers). To mitigate transitional costs, the AER allowed some flexibility around implementation of compliance measures – with such measures required to be in place no later than 1 January 2018. This was in addition to exemptions and waivers being granted for specific projects and services, in some cases for around 3 years.

Associate contracts

The new advance notice requirement for certain associate contracts (requirement to notify 20 business days prior to execution/variation of an associate contract where the terms of access differ from standing terms issued under NGR 101C) will negatively impact the ability for parties to enter

into or vary these types of commercial arrangements and will effectively build in 20 business days to the timeline for such arrangement.

ATCO would suggest a shorter period of 5 or 10 days. A longer time period will result in an extended period for contracts to be executed or varied.

Concessional finance treatment

ATCO reiterates its position from our prior submission that rule 82 should not include any reference to the treatment of concessional finance. Treating concessional finance different to any other form of debt financing goes against the principles embedded in setting the cost of debt in the Rate of Return Instrument by the regulator and the incentive base regulatory framework.

The proposed wording of the NGR, where the treatment of concessional finance as a capital contribution is to be determined by the regulator, creates uncertainty for investment and does not support incentivising investment where it would not normally occur. The proposed wording will create significant investment uncertainty as it will not be until the next access arrangement process (up to 5 years after the investment decision) that the regulator will make a decision on the treatment of the concessional finance.

Draft rule 82 does not provide any indication of the assessment or situation that will determine if concessional finance will be treated as a capital contribution. In the interests of providing certainty for investment, consideration should be given to the inclusion of factors the regulator should have regard to in determining if the concessional finance is to be treated as a capital contribution. It is noted that, draft rule 82 (9) identifies concessional finance in comparison to a market rate, and the term market rate is not defined in the Rule. It is suggested that rather than “market rate”, a link should be made to the cost of debt under the Rate of Return Instrument.

Transitional provisions

It is noted that transitional provisions for ATCO Gas Australia’s hydrogen projects have been identified in draft NGR Schedule 6, Part 2 (2). Due to differences in the structure of projects by designated entities, there are inconsistencies in the prescribed requirements articulated in Column 3. It is assumed that the intention is that all designated entities should be subject to the same exemption from a prescribed requirement, the drafting should reflect this consistency.

In addition, the transitional provisions create new obligations for ATCO Gas Australia to establish, and provide details of, internal controls that “substantially replicate the controls that would apply to associate contracts” if the exempted hydrogen project was “carried on by an associate”. It is unclear the intention of these requirements, what it is expected to capture and the types of internal controls that would be required. If the intention is, as we expect, for contracts between the service provider and an associate for these hydrogen projects to effectively be treated as an “associate contract” then we do not consider the current drafting achieves this. In any event, it remains unclear what “internal controls” would be required and appears to be contrary to the intent of the transitional exemption. It is noted that subsection c) of the rule covers accounting controls and ATCO Gas Australia is comfortable financial separation requirements can be met with existing controls in place already. Further clarity on the intention of subsections a) and b) would assist ATCO Gas Australia understand its obligations.

Lastly, ATCO has made substantial investments in hydrogen and renewable gases to prepare the network to accept these gases prior to the introduction of these draft rules. Recognition and recovery of this investment has not been provided for in the draft rules and should be incorporated into the economic regulation framework. Transitional provisions to enable the recognition and recovery of this investment could be modelled on the speculative investment provisions in the NGR

subject to the regulator satisfying itself that the investment is prudent and efficient in the usual way. Alternatively, similar provisions made by the AEMC in the National Electricity Rules Schedule 6.2, which prescribed an asset value to establish an opening regulatory asset base may be another option.

If you have any questions or would like to discuss any of the comments made in this submission, please contact Kiran Ranbir, Manager Energy Policy and Government Strategy on 0432 158 656.

Yours sincerely

J.D. Patrick Creaghan
Country Chair
ATCO Australia

It was great to see you in person in Sydney last week. I very much appreciated your contribution to the conference and will never look at a mobile phone the same way again!.