

Ref JC:JC:C19608

6 May 2004

Mr James Cox
Acting Chairman
Independent Pricing and Regulatory Tribunal of NSW
PO Box Q290
QVB Post Office NSW 1230



Dear Mr Cox

MMA Draft Report - Review of Demand Forecasts for the Country Energy Gas Network

Thank you for the opportunity to respond to the McLennan Magasanik Associates (MMA) draft report '*Review of demand forecasts for the Country Energy Gas network*' ("the draft report"). Please accept this letter as Country Energy Gas' written submission to the draft report.

In this submission we have first made some general comments on the overall draft report, and then addressed each of the recommendations raised by MMA throughout the report in more detail.

INTRODUCTORY COMMENTS

Due to mergers and internal restructures, Country Energy Gas has experienced a number of significant system changes in recent years. This has resulted in some difficulty in obtaining detailed Volume market sales data for the current regulatory period. However, Country Energy Gas does not consider this is relevant to the load forecasting process as the Volume market sales information would be based on quarterly meter reading data, which would not provide sufficient detail for regression against daily temperature data.

As agreed with MMA, the process undertaken by Country Energy Gas in calculating the daily Volume load using a subtraction methodology is the correct manner in which to obtain daily Volume load data. This methodology does not rely on systems that generate Volume market sales data, but rather on metered injection and daily Contract market sales data. The quality of this data is extremely high. Country Energy Gas therefore believes that the MMA comments on Volume market sales data should not detract from the Tribunal's findings on the reasonableness of the forecast.

In relation to MMAs' concern regarding the split between residential and non-residential consumption, Country Energy Gas believes that the draft report indicates a high degree of confidence in the Volume market forecast as a whole. Therefore, although there may be some uncertainty in the respective disaggregation, Country Energy Gas considers the relative risk and materiality of this to be small, given the domination of the residential sector within the Volume market. The residential sector accounts for approximately 99% of customer numbers and approximately 85% of total consumption for the Volume market.

MMA RECOMMENDATIONS

Recommendation 1: Country Energy Gas should ensure that systems are in place to accurately collect customer number and sales data for (at a minimum) the residential and non-residential components of the volume market.

Whilst we accept this area could have been improved for the period under review, the recommendation does not impact on the reasonableness of the current forecast. At the time of Country Energy Gas' formation, Country Energy was faced with many merger integration issues. A significant issue was the consolidation of the legacy customer information systems into a single system.

Recommendation 2: Country Energy Gas should check with Wagga Wagga Council its current expectations of population and household growth estimates and compare these with the NIEIR forecasts. An average of the two forecasts may be the most appropriate to use.

Country Energy Gas considered the population and household growth forecasts that were prepared for Wagga Wagga City Council by Kirralie Houghton Planning Consultant in September 1999.

After reviewing both the Wagga Wagga City Council and NIEIR reports, Country Energy Gas decided to rely on the NIEIR report for the following reasons:

- The Wagga Wagga forecast was a projection rather than a forecast. That is, the Wagga Wagga City Council report used a census data starting point and projected forward on the basis of assumed growth rates ranging from 0.5% to 2.0%. There were no cases of negative growth shown in the projected information, despite MMA itself noting that the ABS data for Wagga Wagga showed a decline in 2000 and 2001. The projected growth rates did not vary year by year, and there was no apparent consideration of other factors, such as income or regional GDP; and
- Country Energy Gas relied on the NIEIR data in its electricity price review submission. To rely on a different study for the Wagga Wagga Gas Access Arrangement review process would have raised an inconsistency that would have drawn the reasonableness of the forecast into question.

Recommendation 3: Country Energy Gas should not reduce its forecasts because of disconnections as these are already taken account for in its methodology.

The MMA commentary suggests that disconnections are already reflected in the net household growth. While the NIEIR forecasts for household growth are net of any knockdown and rebuilds, these are not the only cause of disconnections. Country Energy Gas had not provided any specific numbers for disconnection causes, but had discussed with MMA that they arose due to a number of factors. For MMA to suggest that they are solely caused by knockdown and rebuilds is speculative and not based on fact.

MMA have themselves stated that they took materiality into account in its extent of review of the Wagga Wagga forecasts, and we are therefore surprised that this item, which equates to 0.15% of the residential customer base, has been identified in the draft report. Country Energy Gas would argue that without any hard evidence to support their claims, MMA should recognise that 25 disconnections per year well and truly falls within a reasonable, yet immaterial range.

Based on a sample of disconnections processed during the current financial year, only 36% have demolition listed as the reason. Therefore, we question MMAs' assertion that all 25 disconnections assumed in our forecast will be due to knockdown and rebuilds. It would seem inappropriate and unreasonable to assume a sudden decrease to zero in disconnections that are due to factors other than knockdown and rebuild.

Recommendation 4: Country Energy Gas should not assume a sudden cessation of E to G conversions, but that E to G conversion numbers follow a more likely decline rate of, say, 50% per year.

It may be reasonable to include some estimate of E to G conversions, although we believe they will be at a much lower rate than in the past due to the fact that the penetration of existing households is very high, and the marginal cost of trying to convert the remaining electricity only customers to gas would outweigh the benefits in many instances. To suggest a declining rate of 50% per year without any supporting information on how this number was arrived at is completely arbitrary and therefore would not seem to align with the principle of "... best estimates arrived at on a reasonable basis". We believe the rate of conversion going forward requires further analysis, rather than simply relying on an arbitrary judgement.

Recommendation 5: Country Energy Gas should use the June 30th customer numbers in its modelling.

Country Energy Gas does not consider that using the 3 June customer numbers as opposed to the 30 June customer numbers in any way affects the reasonableness of the forecasts. Analysis suggests that this results in only around 25 customers that may have been excluded from the customer count. Sensitivity analysis provided in the load forecast report would indicate that this error would only equate to approximately 1 TJ or approximately 0.13% per year. Again, we question the materiality involved with this issue.

Recommendation 6: Country Energy Gas should carry out a multi-regression analysis of the daily Volume data available, assuming the system-wide UAG as agreed, to determine whether there is any significant change in usage per customer over time. Day of week impact may also be assessed at the same time; and

Recommendation 7: If there is no significant change in average usage over time, and the day of the week has no impact then Country Energy Gas should use the latest analysis as the basis for forecasting.

Country Energy Gas has demonstrated that the greatest driver of consumption in the Volume market is weather, with the correlation coefficient of daily temperature to daily consumption of about 94%. This indicates that any other drivers would have a marginal explanatory value at best. Country Energy Gas considers that the cost of obtaining and analysing this data would exceed its value in improving the reasonableness of the forecasts.

Recommendation 8: Country Energy Gas should confirm that it will retain an "election to be charged contract tariff" clause or similar in its next AA.

Subsequent to the draft report, Country Energy Gas is reviewing its position in relation to this issue, however this cannot be undertaken without fully understanding the impacts on both current and new customers. We will keep MMA and the Tribunal informed on the outcomes from this review.

Recommendation 9: Country Energy Gas should hold discussions with ... and ... to ensure that Country Energy Gas' assumptions for these customers over the coming AA period are realistic.

Country Energy Gas has had further discussions with these two customers and does not consider it necessary to amend its forecasts specifically for MDQ. Both customers have recently reviewed their contracted MDQ and are now satisfied that they have contracted an appropriate level going forward. Recent actual MDQ for both of these customers is consistent with this contracted amount. We are looking at the consumption for the customer that is in its second full year of operations, and may change this forecast, however this will have no bearing on the contracted MDQ upon which our billing is based.

If you have any questions in relation to this submission please contact Terri Benson on (02) 6338 3424 or Lawrence Zulli on (02) 6883 4547.

Yours sincerely



Craig Murray
Managing Director