

# Draft decision

**Jemena Gas Networks (NSW) access  
arrangement 2025 to 2030  
(1 July 2025 to 30 June 2030)**

**Attachment 9 – Reference tariff setting**

**November 2024**

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AER reference: AER22005460

### **Amendment record**

<b>Version</b>	<b>Date</b>	<b>Pages</b>
1	29 November 2024	27

## List of attachments

This attachment forms part of our draft decision on the access arrangement that will apply to Jemena Gas Networks (NSW) for the 2025–30 access arrangement period. It should be read with all other parts of this draft decision.

The draft decision includes the following documents:

Overview

Attachment 1 – Services covered by the access arrangement (no attachment - covered in the Overview)

Attachment 2 – Capital base

Attachment 3 – Rate of return

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 8 – Efficiency carryover mechanism

Attachment 9 – Reference tariff setting

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## 9 Reference tariff setting

This attachment outlines our assessment of the reference tariffs proposed by Jemena Gas Networks' (JGN) (NSW) against the requirements of the National Gas Law (NGL) and National Gas Rules (NGR). Our assessment focuses on the structure of reference tariffs and takes into account the revenue and pricing principles.<sup>1</sup>

This attachment describes our assessment of JGN's proposed reference tariffs and sets out the revisions required by this draft decision. The AER's assessment focuses on the design and structure of tariffs and the allocation of costs to services.

### 9.1 Draft decision

Our draft decision is to accept most of JGN's proposed amendments to its gas transportation tariffs: Specifically:

- merging coastal and country pricing zones
- splitting volume customers into small (under 200 GJ consumption per annum) and large (over 200 GJ)
- recovering proportionally more revenue from demand customers
- increasing the fixed charge for large volume customers
- reducing volume tariff price blocks from 6 to 4
- flattening the volume tariff structure.

However, our draft decision is that:

- more clarity is required on JGN's proposals to undertake further incremental changes during the 2025–30 period (i.e. revenue recovery from demand customers and flattening the volume customer declining block tariff structure)
- further work is required on JGN's gas transportation tariff reform pathways to achieve flat tariffs, including bill impact modelling, for all tariff classes including demand customers.
- further consideration by JGN with stakeholders is required on whether a 10 % side constraint is too broad and whether it would be appropriate for JGN to amend the side constraint to 2 % to align with other gas distributors.

Our requirements set out above are in order for us to be satisfied that JGN is reflecting the updated National Gas Objective (NGO), which now incorporates an emissions reduction element.<sup>2</sup>

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<sup>1</sup> NGL, ss. 24(2)–(7).

<sup>2</sup> NGL, ss 23.

On JGN's ancillary reference service tariffs, our draft decision is to accept JGN's proposed individual price caps, with the exception of its proposed tariff for the volume customer abolishment service.<sup>3</sup>

Our draft decision is to reduce the level of JGN's proposed volume customer abolishment cost by 25%, bringing it down to \$1,104, and to socialise most of that cost, giving an abolishment tariff of \$250. This reflects the NSW safety regulator's preference to reduce the price gap between temporary and permanent disconnection services.

Our draft decision is to not accept JGN's proposed CPI-X ancillary reference service tariff variation mechanism. We note other regulated gas distributors escalate ancillary reference service tariffs by CPI only. At this stage we do not see a rationale to treat JGN differently (for additional discussion see attachment 10 – tariff variation mechanism).

Our reasons for our draft decision are set out below.

## 9.2 JGN's proposal

### 9.2.1 Gas transportation tariffs

JGN proposed to replace its existing declining block tariff structure for volume customers (residential and small business customers)<sup>4</sup> with a simpler, but still declining, block tariff structure. In doing so, JGN proposed several changes from its current tariff structure:<sup>5</sup>

- merge the volume customer (residential and small business) tariff classes of 'coastal' (Sydney, Wollongong, Newcastle, Central Coast) and 'country' (central Tablelands, Central West, Southern Tablelands, Riverina)
- differentiate between small volume customers (under 200 GJ per annum) and large volume customers (over 200 GJ) to establish a higher daily/fixed charge for large volume customers, equivalent to ~20% of the total bill
- reduce the number of volume customer tariff blocks from 6 to 4 and slightly flatten the declining block tariff structure for year one of the 2025–30 access arrangement period
- incrementally further flatten the volume tariff structure over the 2025–30 access arrangement period, although details of what the tariff structure would look like by 2030 have not been submitted.

JGN proposed to make no changes to its existing 6 block declining block tariff structure for demand customers (large commercial and industrial customers).<sup>6</sup> Though JGN indicated it would incrementally increase total cost recovery from demand customers, in the process removing some of the cost recovery burden from smaller customers.

JGN's proposed reference tariffs for the 2025–30 period are set out in Table 9.1.

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<sup>3</sup> NGL, ss. 24(2)–(7).

<sup>4</sup> For 2024–25 JGN expected to earn 92% of its regulated revenue from volume customer tariffs.

<sup>5</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. 14-18.

<sup>6</sup> For 2024–25 JGN expected to earn 8% of its regulated revenue from demand customer tariffs.

**Table 9.1 JGN's proposed transportation reference tariffs**

Tariff category	Tariff classes	Charging structures
<b>Volume market</b>		
Volume individual metered	VI-small VI-large	Fixed charge Declining block volume charges (\$/GJ/qtr.)
Volume boundary metered	VB	Fixed charge Declining block volume charges (\$/GJ/qtr.)
Residential distributed generation technology	VRT-03, VRT-04, VRT-06, VRT-10	Fixed charge Declining block chargeable demand (\$/GJ CD)
<b>Demand market</b>		
Capacity country	DC Country	Fixed charge Declining block chargeable demand (\$/GJ CD)
Capacity coastal	DC1 to DC11	Fixed charge Declining block chargeable demand (\$/GJ CD)
First response	DCFR-01, DCFR-06 & DMTFR-03	Declining block chargeable demand (\$/GJ of CD pa)
Major end-user (throughput)	DMT1 to DMT5	Fixed charge Declining block demand throughput (\$/GJ)
Throughput	DT	Fixed charge Declining block demand throughput (\$/GJ)

Source: AER analysis of JGN, 2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing, June 2024 p. 14-18.

Notes: CD – Chargeable Demand.

Additionally, JGN is proposing to continue providing prudent discounts to two customers who, without the discount, may elect to bypass JGN's network, meaning that tariffs may be higher for all other customers on JGN's network.

## 9.2.2 Ancillary reference services

JGN is proposed a continuation of its existing ancillary reference services. Table 9.2 outlines JGN's ancillary reference service tariff structure.

**Table 9.2 JGN's ancillary reference service tariff structure**

Service	Charge
Hourly charge—non-standard retailer-initiated requests and queries	<ul style="list-style-type: none"> <li>Hourly charge (min charge of 1 hour)</li> </ul>
Disconnection & Reconnection—Volume Customer Delivery Points	<ul style="list-style-type: none"> <li>Completed activity charge</li> <li>Wasted visit charge</li> </ul>
Disconnection & Reconnection—Demand Customer Delivery Points	<ul style="list-style-type: none"> <li>Completed activity charge</li> </ul>
Expedited reconnection	<ul style="list-style-type: none"> <li>Completed activity charge</li> </ul>
Abolishment	<ul style="list-style-type: none"> <li>Completed activity charge for meters with a capacity of less than or equal to 25m<sup>3</sup>/hr</li> <li>Meters above 25m<sup>3</sup>/hr will be individually priced</li> </ul>
Special meter read	<ul style="list-style-type: none"> <li>Completed activity charge</li> <li>Wasted visit charge</li> </ul>

Source: AER analysis of JGN, 2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing, June 2024 p. 19.

JGN proposed to retain a cost reflective abolishment tariff. In doing so, JGN referenced its stakeholder feedback during pre-lodgement consultation that a user-pays approach to abolishment costs is preferred. JGN's proposed abolishment tariff for small customers ("volume customers") is \$1,472 in 2025-26. For large customers ("demand customers") the abolishment service is a negotiated service and the charge is determined dependent on the complexity of the abolishment.<sup>7</sup>

JGN is forecasting ~3,000 abolishments in 2025–26 (consistent with previous years) rising to 12,000 in 2029–30 (a significant variation from previous years).

### 9.3 Assessment approach

In an access arrangement, a service provider is required to specify for each reference service, the reference tariff and proposed approach to setting the reference tariff.<sup>8</sup> This is done by:

- explaining how revenues and costs are allocated, including the relationship between costs and tariffs<sup>9</sup>

<sup>7</sup> JGN, 2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing, June 2024 p. 20.

<sup>8</sup> NGR, rr. 48(1)(d)(i), 72(1)(j).

<sup>9</sup> NGR, rr. 72(1)(j)(i), 93(1)–(2).



- comparing the revenue to be raised by each reference tariff with the cost of providing each individual reference service<sup>10</sup>
- explaining and describing any pricing principles it employed.<sup>11</sup>

We also had regard to submissions received in the course of our consultation on JGN's proposed access arrangement.<sup>12</sup>

### 9.3.1 Identifying the reference service

The NGR require service providers to specify a reference tariff for each reference service.<sup>13</sup> When undertaking our review, we first consider what is (or are) the reference service(s) for the purpose of the NGR. Our initial decision on what constitutes reference services was published in November 2023 and is referenced in the reference services section of the Overview for this decision.<sup>14</sup>

### 9.3.2 Assessing the tariff setting method for the reference service

The reference tariffs for an access arrangement must be designed to meet the requirements of the NGR.

We consider how the service provider, JGN, intends to charge for reference services by:

1. Assessing how JGN intends to allocate costs and revenues between reference services and other services. It must demonstrate that total revenue is allocated between reference and other services in the ratio in which costs are allocated between reference services and other services. Costs must also be allocated to the reference service and other services to which the cost is directly attributable.<sup>15</sup>
2. Assessing how JGN grouped its customers into tariff classes. JGN is required to group together customers for reference services on an economically efficient basis and to avoid unnecessary transaction costs.<sup>16</sup> We consider whether the nature of the reference service (e.g. volume and demand tariff classes) is consistent with the need to group customers together on an economically efficient basis and avoid unnecessary transaction costs.
3. Assessing how:
  - (a) the expected average revenue of a tariff class compares with the standalone cost and avoidable cost of providing the reference service to that tariff class
  - (b) whether the tariff takes into account transaction costs associated with developing and applying the tariff

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<sup>10</sup> NGR, r. 94(3).

<sup>11</sup> NGR, r. 72(1)(j)(ii).

<sup>12</sup> NGR, r. 59.

<sup>13</sup> NGR, r. 48(1)(d)(i).

<sup>14</sup> AER, *Final decision – Jemena Gas Networks (NSW) Ltd – Gas distribution determination 2025 to 2030 – Reference services*, November 2023.

<sup>15</sup> NGR, r. 93(2).

<sup>16</sup> NGR, r. 94(2).

- (c) whether the tariffs take into account the long run marginal costs of providing reference services
- (d) whether customers belonging to the relevant tariff class are able, or likely, to respond to price signals.<sup>17</sup>

We have assessed the proposed reference tariffs for consistency with the NGO and have had regard to the revenue and pricing principles.<sup>18</sup> The NGO was updated late last year to include an emissions reduction objective:<sup>19</sup>

The objective of this Law is to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to—

- (a) price, quality, safety, reliability and security of supply of natural gas; and
- (b) the achievement of targets set by a participating jurisdiction—
  - (i) for reducing Australia's greenhouse gas emissions; or
  - (ii) that are likely to contribute to reducing Australia's greenhouse gas emissions.

For existing fixed principles that were approved before the commencement of the NGR, these are binding on the AER and JGN for the period for which the principle is fixed and these may only be varied or revoked with JGN's consent.<sup>20</sup>

### 9.3.3 Interrelationships

The reference tariffs have interrelationships across other key parts of our draft decision. For example, it interrelates with the total revenue that can be earned by JGN, the services it provides to its customers to recover those revenues, the tariffs it charges for the use of those services, and the demand forecast volumes used to calculate tariffs.

Our draft decision on:

- the total revenue requirement is set out in the Overview of this draft decision
- the services JGN will offer to customers over the 2025–30 period are set out in the reference services section of the Overview for this decision.
- the annual tariff variation mechanisms are set out in Attachment 10 – Reference tariff variation mechanism
- the demand forecast volumes are set out in Attachment 12 – Demand.

## 9.4 Reasons for draft decision

We do not accept JGN's proposed reference service tariffs, because of the lack of detail on several aspects of JGN's transportation tariff proposal and the absence of bill impact modelling of tariff structure options, and with an underlying concern that JGN may not be

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<sup>17</sup> NGR, rr. 94(3)–(4).

<sup>18</sup> NGL, s. 28(2); NGR, r. 100(1).

<sup>19</sup> National Gas (South Australia) Act 2008, s. 23. This includes the latest amendment to the NGO which came into effect on 21 November 2023.

<sup>20</sup> NGR, r. 99.

sufficiently reflecting the updated NGO.<sup>21</sup> We also do not accept JGN's proposed tariff for its abolishment ancillary reference service for volume customers.

The remainder of this section sets out the reasons for our draft decision under the following headings:

- allocation of revenues and costs to reference tariffs
- establishment of tariff classes
- tariff classes and revenue limits
- standalone and avoidable costs
- tariff setting and pricing strategy objectives
- abolishment
- other ancillary reference services
- issues to be considered in revised proposal

#### **9.4.1 Allocation of revenues and costs to reference tariffs**

JGN's proposal included information outlining its standalone costs, long run marginal costs and incremental costs. On reviewing this, we are satisfied JGN's approach to allocating revenue and costs between reference services and non-reference services complies with the NGR for the following reasons:

- We are satisfied JGN's proposed costs relating to its reference services do not include costs incurred (and recovered) from the provision of its non-reference services.
- JGN has not allocated non-reference service revenue to a reference service because the underlying costs have not been included in JGNs building block revenues.

#### **9.4.2 Establishment of tariff classes**

JGN groups customers into tariff classes according to throughput, location and metering type. Smaller customers — those consuming 10 terajoules or under per year (volume customers) — pay tariff structures comprising a fixed charge and declining block volumetric charges. Larger customers — those consuming more than 10 terajoules per year (demand customers) — pay more complicated tariffs, which include demand charges and capacity charges; both of which have declining block structures.<sup>22</sup>

We consider these characteristics are likely to link costs within JGN's gas distribution network to the revenue it receives for services giving rise to costs. Therefore, using them to group customers into tariff classes is appropriate. We are satisfied the proposed tariff classes are consistent with the requirements of the NGR.<sup>23</sup>

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<sup>21</sup> NGL, ss 23.

<sup>22</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. 18.

<sup>23</sup> NGR, r. 94(4).

### 9.4.3 Tariff classes and revenue limits

We have assessed JGN's tariff classes and revenue limits against the requirements in the NGR:<sup>24</sup> Specifically:

- (a) how the expected average revenue of a tariff class compares with the stand-alone cost and avoidable cost of providing the reference service to that tariff class
- (b) whether the tariff takes into account transaction costs associated with developing and applying the tariff
- (c) whether the tariffs take into account the long run marginal costs of reference services
- (d) whether customers belonging to the relevant tariff class are able, or likely, to respond to price signals.

### 9.4.4 Standalone and avoidable costs

We are satisfied that JGN's proposed reference tariffs are consistent with the NGR requirement that the expected revenue to be recovered lie on or between:

- an upper bound representing the standalone cost of providing the reference service to customers who belong to that tariff class
- a lower bound representing the avoidable cost of not providing the reference service to those customers.<sup>25</sup>

JGN's proposal includes detailed appendices discussing how it estimates standalone and avoidable costs. We reviewed JGN's definitions of avoidable and standalone costs for the volume and demand tariff classes, and consider these definitions comply with the NGR.

We have also reviewed the methodology applied by JGN to demonstrate that, for each tariff, the expected tariff revenue lies on or between the avoidable and standalone costs.<sup>26</sup> In doing so, we had regard to the underlying calculations of avoidable and standalone costs JGN provided.<sup>27</sup>

#### 9.4.4.1 Transaction costs

We are satisfied JGN's proposed reference tariffs take into account transaction costs associated with the tariff and the need to avoid them where possible.<sup>28</sup> We consider the proposed changes to tariff classes and to tariff structures will minimise any additional transaction costs across the 2020–25 and 2025–30 access arrangement periods. As we discuss below, we are also satisfied that JGN's approach to estimating long run marginal costs appropriately accounts for transaction costs.

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<sup>24</sup> NGR r. 94.

<sup>25</sup> NGR r. 94(3).

<sup>26</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. 23-24.

<sup>27</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. 23-24.

<sup>28</sup> NGR, 94(2) and 94(4).

#### 9.4.4.2 Long run marginal cost

The NGR requires that JGN must take into account the long run marginal cost (LRMC) when determining its tariffs.<sup>29</sup>

LRMC is equivalent to forward looking variable costs—more specifically, as measured over a period of time sufficient for all factors of production to be varied. When tariffs accurately reflect the marginal, or forward-looking, cost of increasing (or decreasing) demand, consumers can make informed choices about their gas usage. Under such tariffs, customers would increase their use of the network only when they value it more than the costs. This, in turn, signals to distributors to invest in additional capacity to the extent that customers value it.<sup>30</sup>

JGN's LRMC estimation involves the following steps:<sup>31</sup>

- choice of the 'average incremental cost' (AIC) approach to calculating LRMC
- identifying growth-related capex and opex as 'marginal' costs to include in the AIC calculation
- adopting a 13 year forecast period as the 'long run' timescale.

We are satisfied JGN's reference tariffs take LRMC into account after having regard to the transaction costs and whether customers are likely to be able to respond to these price signals.<sup>32</sup> We consider JGN's approach is generally consistent with that applied by other gas distribution networks.

#### Estimation method balances accuracy with implementation costs

JGN considered both the AIC and Turvey<sup>33</sup> approaches to estimating LRMC, ultimately adopting the AIC approach because it is more readily applied.<sup>34</sup>

The AIC approach is broadly considered to be a less costly estimation method compared to other more sophisticated approaches, such as the Turvey approach. While Turvey is perceived to produce more accurate estimates than AIC, it is a higher cost method.<sup>35</sup> In

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<sup>29</sup> NGR, r. 94(4)(a).

<sup>30</sup> Alternatively, customers may reduce their use of the network if the benefit they derive is less than the costs. This in turn signals to distributors the potential to reduce capacity in the network.

<sup>31</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. A3-A4.

<sup>32</sup> NGR, r. 94(4).

<sup>33</sup> The "Turvey approach" to estimating LRMC is an approach that considers the change in forecast future system costs arising from a permanent increment or decrement in the forecast pattern of future demand. For a description of these approaches and their relative merits, see NERA, *Economic Concepts for Pricing Electricity Network Services: A Report for the Australian Energy Market Commission*, 21 July 2014, pp. 14–16.

<sup>34</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. A3.

<sup>35</sup> For a discussion on the relative merits of these approaches, see NERA, *Economic Concepts for Pricing Electricity Network Services: A Report for the Australian Energy Market Commission*, 21 July 2014, pp. 14–16.

recent electricity decisions, we have accepted the use of the AIC approach by electricity distributors.<sup>36</sup>

We consider it is important to balance the benefits and costs of more accurate estimates of LRMC, and this will depend on the circumstance of each business. In JGN's case, a gas distributor is required to have regard to LRMC when setting its tariffs, as distinct from electricity distributors which must base tariffs on LRMC. With this in mind, we are satisfied with JGN's proposal to rely on the AIC approach.

In terms of how JGN applies this method, the estimation is undertaken for each tariff class by dividing the present value of the expected costs of the optimal network by the present value of additional demand supplied.<sup>37</sup> We are satisfied with JGN's proposal to rely on an AIC method to estimate LRMC.

***Definition of marginal costs satisfactory with future enhancement available***

Given growth in customer consumption drives expenditure on shared network assets, JGN included forecast capex and opex relating to forecast growth of the shared network in the LRMC estimate. JGN also included replacement capital expenditure and associated operating expenditure where this is needed to maintain network capacity in the long run at a level that consumers value. We are satisfied with JGN's approach.

***Long run timescale appropriate***

We consider there is no ideal, or correct, timescale on which to base LRMC estimates and we accept a range of timeframes may be compliant with the NGR. However, the timescale must be sufficient to allow a significant number of factors of production to change—and a key factor of production is the level of capacity in the network.

Ultimately, the level of capacity in a distribution network is variable meaning the 'long run' would match the life of the assets. Some distribution network assets have very long lives (in excess of 60 years). However, it would be impractical to produce accurate forecasts over such a long horizon. The longer the estimation period, the more difficult it becomes to estimate and forecast long run costs. We consider a minimum forecast horizon of 10 years captures the essence of 'long run'. JGN's proposal for a 13 year forecast period exceeds this. As a result, we are satisfied with this approach.

**9.4.4.3 Prudent discounts**

We consider that the prudent discounts JGN proposed to offer are necessary to respond to competition from other providers of pipeline services or alternative energy sources and to ensure the ongoing efficient use of its pipeline.<sup>38</sup> Further, JGN has demonstrated that the negotiated revenue from prudent discount services exceeds the estimate of the avoidable costs. Without a prudent discount, a customer may elect to bypass the network, with the

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<sup>36</sup> For example, see *AER, Final decision, Endeavour Energy Distribution Determination 2019 to 2024, Attachment 18 Tariff structure statement*, April 2019.

<sup>37</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024, p. A3.

<sup>38</sup> Service providers offer prudent discount to users in order to respond to competition from other providers of pipeline services or other services of energy. Alternatively, the service provider may offer prudent discounts in order to maintain the efficient use of the pipeline. These applications are made on a confidential basis to the AER.

consequence that tariffs may be higher for all remaining users on the network. Therefore, we are satisfied that JGN's proposed prudent discounts are consistent with the NGR.<sup>39</sup>

We note that with respect to prudent discounts, our role is limited to assessing whether JGN's proposal is compliant with the NGR. Service providers (in this case, JGN) initially determine whether a prudent discount should apply to a particular user.

### **9.4.5 Tariff setting and pricing strategy objectives**

JGN has a broader pricing strategy as part of its approach to the future of gas.<sup>40</sup> As part of this, JGN has established a series of objectives to promote cost reflectivity, pricing stability, simplicity, revenue adequacy and fairness.<sup>41</sup>

JGN has taken practical steps to achieving these pricing objectives as part of setting its reference tariffs. As we discuss in the sections below, we consider the pricing objectives and tariff setting measures JGN is proposing are consistent with promoting the long term interests of consumers.

#### **9.4.5.1 Efficiency objectives**

We are satisfied JGN's pricing strategy promotes efficient network use and cost recovery by having regard to LRMC when setting tariff levels and also maintaining the current tariff variation side constraints. We consider these aspects of JGN's 2025–30 proposal will promote the long-term interests of consumers.

With respect to LRMC, JGN's approach is consistent with the requirements in the NGR, as we discussed above in section 9.4.3. In regard to maintaining tariff variation side constraints, we are questioning whether a 10% side constraint is too broad. The concern with a 10% side constraint is that some customer classes may see large annual price changes due to rebalancing. Further consideration by JGN with stakeholders is required on whether a 10% side constraint is too broad and whether it would be appropriate for JGN to amend the side constraint to 2% to align with other gas distributors.

#### **9.4.5.2 Changes to Tariff Classes and Structures**

We support JGN's proposals to merge the coastal and country tariff classes, differentiate between large and small volume customers, and increase the fixed charge for large volume customers. In principle, we also support incrementally increasing cost recovery from demand customers, though JGN did not submit details of the scale of its intended changes. We consider these changes simplify JGN's transportation tariffs and more appropriately recover revenues from larger volume customers and demand customers, with the effect of removing some of the cost recovery burden from smaller customers.

However, we require more information on JGN's transportation tariff proposal, including the intended extent of changes to be made during the 2025–30 period. We also require more

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<sup>39</sup> NGR, r. 96.

<sup>40</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. v.

<sup>41</sup> JGN, *2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing*, June 2024 p. v.

details of options for alternative approaches to the proposed declining block tariffs, including bill impact modelling of more aggressive changes to the declining block structure.

Overall, we are not satisfied JGN's declining block tariffs sufficiently reflect the updated NGO, which now incorporates an emissions reduction element.

JGN submitted that its pre-lodgement stakeholder engagement process provided support for its proposal to retain the declining block structure and for its intended changes to the structure. The Justice and Equity Centre submitted:<sup>42</sup>

“We remain concerned that in the long-term a declining block structure inappropriately incentivises higher gas use and disproportionately benefits customers with large loads. We question whether this structure remains appropriate in light of the amended NGO...”

However, the Justice and Equity Centre went on to indicate that, despite the above concerns, it supports JGN's transportation tariff proposal:

“...but accept that under current circumstances retail practices mean that a change in structure would be unlikely to have the intended effect. Consequently, we support Jemena's proposal to maintain a declining block structure, while making efforts to address this issue through reducing the number of tariff blocks from six to four. Tariff forum participants overwhelmingly supported this change on grounds that it reduces the incentive to increase gas use.”

Our draft decision requires JGN to submit with its revised proposal a range of options for more fundamental changes to its tariff structures. This will provide stakeholders, in addition to the AER, with the additional information required to form a view on how to best reflect the updated NGO.

#### **9.4.5.3 Declining block tariffs**

We are not satisfied that JGN's flattening of its declining block tariff structure for its transportation tariffs is sufficiently reflective of the updated NGO. We consider JGN needs to provide more tariff options in its revised proposal, supported by bill impact modelling. Those options could include moving incrementally to flat tariffs, for both volume and demand customers, over two regulatory control periods (10 years in total). A range of options between JGN's initial proposal and completely flattening tariffs could also be reflected in JGN's revised proposal. This will allow stakeholders to engage with this issue to inform the AER's final decision.

#### **9.4.6 Abolishment**

In its reference service proposal, JGN proposed that volume customer abolishment continue to be regulated as an ancillary reference service for the 2025–30 period.

As more customers choose to move from gas to other sources of energy, the costs of removing connection assets for individual premises—abolishing the connection permanently—have come under close scrutiny. In reviewing this proposal, we have

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<sup>42</sup> Justice and Equity Centre, *Jemena Gas Networks access arrangement 2025-30: Issues paper*, September 2024, p. 29.



considered the costs of abolishing connections and the broader question of how they are recovered from consumers over time.

As set out in the Overview, our draft decision is to accept JGN's proposed abolishment service as an ancillary reference service.

However, consistent with our considerations set out above, our draft decision is to not accept JGN's proposed ancillary reference service tariff for customer connection abolishments. We consider JGN and stakeholders need further time to consider the relative strengths and weaknesses of the two connection abolishment cost recovery approaches we describe below.<sup>43</sup> JGN and stakeholders are encouraged to respond to these in JGN's revised proposal and in submissions on our draft decision and the revised proposal.

Abolishment is a cessation of service option which involves the removal of connecting infrastructure, including the meter and the connecting pipeline to the mains T intersection. Abolishment is one of 2 types of gas small customer cessation of service options for JGN customers:

- disconnection: temporary disconnection where the service is capped at the meter and the meter remains in place.
- abolishment: permanent disconnection where the service is permanently cut at the mains T intersection.

Charges proposed by JGN for small customer cessation of service options are set out in table 9.3.

**Table 9.3 Proposed small customer cessation of service charges for 2025–26**

Service type	Charge (\$2025–26)
Abolishment	\$1,472
Disconnection	\$84

Source: JGN, 2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing, June 2024 p. 19.

Small customer connection abolishment involves the removal of gas from the pipe connecting a customer's premises to the mains pipeline, sealing the mains and making the site safe. Small customer connection abolishment is priced by JGN at a proposed \$1,472 in 2025-26. The alternative cessation of service option is to cap supply at the meter (a disconnection). This alternative is considerably cheaper than abolishment.

Therefore, a disconnection is a lower cost option for customers. However, it raises issues such as the safety aspect of live gas pipelines remaining underground and the costs to maintain this unused service.

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<sup>43</sup> NGR r. 47A(15).

#### **9.4.6.1 Safety issues in NSW are the jurisdiction of the NSW Safety Regulator**

The Pipeline and Gas Networks (PGN) team (the NSW safety regulator) within the NSW Department of Climate Change, Energy the Environment and Water (NSW DCCEEW) provided the AER with a letter in relation to abolishments supporting reducing the gap between the disconnection and abolishment fees:<sup>44</sup>

“It is the PGN team’s understanding that there is a potential for properties that no longer intend to use gas to “disconnect” from the network purely from a retail perspective without requiring the property to be physically disconnected (or abolished) from the gas network. ...

... The large gap (eg approximately \$1000) between the cost of abolishment compared to disconnection is acting as a perverse incentive to customers completely removing their live gas connection, thereby exacerbating the potential for safety related gas incidents.

To ensure the safety risks of live gas services remaining after a property stops using gas are minimised, the PGN team supports any initiatives to incentivise a customer to proceed with a full abolishment of their gas service. We would support any consideration of closing the gap between the retail “disconnection” fee and network “abolishment” fee.”

#### **9.4.6.2 Proposed charges for small customer connection abolishments**

We have assessed the proposed small customer connection abolishment charges proposed by JGN. Based on both our benchmarking analysis and cost build up assessment, the proposed charges are not reasonable with respect to abolishing small customer connections. They are inconsistent with small customer connection abolishment charges levied by other gas distributors.

The components of the proposed JGN abolishment service charge are almost entirely opex and do not include additional cost recovery. That is, JGN’s proposed abolishment charges reflect the labour cost of staff attending the customer’s premises to perform the task. They do not incorporate any contribution to shared network cost recovery – they are not exit fees. Rather, JGN’s small customer connection abolishment charges have been proposed by JGN on a cost recovery basis.

Several submissions commented on the level of the JGN’s proposed small customer connection abolishment charges and submitted that the associated fee (\$1,472) may act as a disincentive for customers to disconnect, and that the proposed small customer connection abolishment charges are too high.

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<sup>44</sup> NSW Department of Climate Change, Energy, the Environment and Water (DCCEEW), Letter: Costings for the disconnection and abolishment to the natural gas asset for households in NSW, 2 July 2024, pp 1-2.

Stakeholder submissions from ECA<sup>45</sup>, Ausgrid<sup>46</sup>, Rewiring Australia<sup>47</sup>, IEEFA<sup>48</sup>, Arena Energy Consulting/AERIS Capital<sup>49</sup> and Better Renting<sup>50</sup> have been supportive of reducing the proposed abolishment tariff and socialising as much of the abolishment cost as possible. Stakeholders recommended adopting the AER’s approach taken in Victoria and setting the abolishment tariff at around \$220 and socialising the remainder of the abolishment costs.

As above, we consider that JGN’s proposed customer connection abolishment service charges is not reasonable in the context of small customers. We do not consider that it reflects the efficient cost of distributor staff attending the customer’s property, digging down to the mains T intersection, disconnecting and removing (if possible) the customer’s connection pipeline, sealing the mains and making the site safe.

JGN’s proposed abolishment tariff of \$1,472 is high relative to the equivalent tariff established by other regulated gas distributors. Table 9.4 outlines our benchmarking analysis, indicating that JGN’s proposal is out of step with other regulated distributors.

**Table 9.4 Abolishment tariff benchmarks**

Gas Distributor	Charge (\$2025–26)
JGN	\$1,472
MultiNet*	\$1,044*
AGN Victoria*	\$1,044*
AusNet*	\$910*
EvoEnergy	\$884

Notes: \* Abolishment tariff amount excluding the partial socialisation of the abolishment tariff.

We sent three information requests to JGN to gather more information about its cost build-up of their abolishment service. The information JGN provided in response to these requests has not satisfied us that JGN’s cost build up reflects efficient costs. We have compared JGN’s cost build up with the cost build up we have for AusNet’s Abolishment service. This comparison has raised a number of concerns.<sup>51</sup>

In particular, the contract and materials cost components of JGN’s abolishment service charge are significantly higher than AusNet’s. JGN’s corporate and network overheads also account for a large part of the proposed cost, with nearly half of JGN’s proposed \$1,472

<sup>45</sup> ECA, Submission on Jemena Gas Networks 2025-30 AA, September 2024, p. 8.

<sup>46</sup> Ausgrid, Submission on Jemena Gas Networks 2025-30 AA, September 2024, p. 2.

<sup>47</sup> Rewiring Australia, Submission on Jemena Gas Networks 2025-30 AA, September 2024, pp. 3-4.

<sup>48</sup> IEEFA, Submission on Jemena Gas Networks 2025-30 AA, September 2024, p. 4.

<sup>49</sup> Arena Energy Consulting/AERIS Capital, Submission on Jemena Gas Networks 2025-30 AA, September 2024, p.7.

<sup>50</sup> Better Renting, Submission on Jemena Gas Networks 2025-30 AA, September 2024, p. 1.

<sup>51</sup> AER, JGN Information Request #001, July 2024. AER, JGN Information Request #002, July 2024. AER, JGN Information Request #017, October 2024.

abolishment cost being accounted for by the non-contract costs of undertaking the abolishment. By way of comparison, AusNet’s \$910 abolishment tariff comprises lower contract and materials costs and includes more modest overheads and other on-costs.

To bring the abolishment cost back towards the top end of the range of the other gas distributors, our draft decision is to apply a 25% reduction to JGN’s proposed abolishment tariff. A 25% reduction on the proposed tariff of \$1,472 reduces the abolishment tariff to \$1,104. This brings JGN’s abolishment tariff back into the top end of the benchmark of the other distributors and into line with a comparable network like AGN Victoria’s abolishment tariff of \$1,044.

While we consider a small customer connection abolishment charge of \$1,104 is reasonable, levying those charges on individual customers is not the only cost recovery option available.

#### 9.4.6.3 Socialising small customer connection abolishment costs via transportation tariffs

There is potential to recover small customer connection abolishment costs from all customers remaining connected to JGN’s network rather than from individual customers who choose to cease their gas supply.

Table 9.5 sets out our draft decision, which is to partially socialise the abolishment cost via setting a \$250 abolishment tariff and recover the balance of abolishment service costs (\$854 = \$1,104 – \$250) via gas transportation tariffs. The \$250 is set in line with the 2022–23 tariff of \$220 in Victoria which escalates to \$242 by 2025–26.

**Table 9.5 Abolishment tariff - AER Draft Decision for 2025–26**

Service type	Charge (\$2025–26)
Abolishment	\$250 <sup>52</sup>

Source: AER Analysis.

Our draft decision is premised on the safety concern that a relatively high abolishment tariff disincentivises customers from requesting the abolishment service. This would leave an unacceptably large number of unused gas connections in situ for indefinite periods and also involve continuing costs of maintaining an unused service. We further consider that high abolishment tariffs appear to customers as exit fees, to the extent customers are willing to pay them at all, with the effect of inhibiting achievement of jurisdictional emissions reduction targets.

Setting a \$250 abolishment tariff brings the abolishment tariff closer to the \$84 temporary disconnection tariff, which is the alternative cessation of service option.

The safety and regulatory obligations on JGN in relation to abolishing dormant connections are general rather than specific. That is, JGN is required to operate and maintain its network safely. JGN’s approved Safety Case sets out how a customer connection should be

<sup>52</sup> Note this is ex-GST and retailers may, when passing this cost through to customers, add their own mark-up to reflect their administrative costs.

abolished. However, the Safety Case does not set out an explicit obligation in relation to abolishing dormant connections.

We set out below our further consideration of the two options for small customer connection abolishment cost recovery:

- as an ancillary reference service (as proposed by JGN)
- bundled with transportation tariffs (socialised).

#### **9.4.6.4 Abolishment as an ancillary reference service**

A number of gas distributors across Australia currently provide abolishments as ancillary network services. A growing number of distributors provide abolishments as price regulated reference services, consistent with JGN's proposal. The trend towards abolishments becoming reference services reflects expectations of the growing number of customers permanently disconnecting from gas networks.

The nature of the abolishment service, provided in respect of an individual customer's connection, leads to the service being more appropriately categorised as an ancillary network service. It is not a transportation service provided using shared network assets. Consistent with this view, JGN has proposed that small customer connection abolishment be an ancillary reference service. As an ancillary service, abolishment charges are targeted directly to customers who choose to cease their gas supply. This approach benefits customers who choose to remain connected to the reticulated gas network as they are not required to finance other customers' abolishment activities.

We agree with JGN that connection abolishment is a service provided in respect of an individual customer's connection assets. However, we consider the traditional approach of levying a material charge on customers may not be sustainable in the context of large numbers of customers ceasing gas supply. This is because we accept in principle the view expressed by stakeholders that proposed abolishment charges may act as a disincentive for customers to engage the abolishment service.

Faced with the choice of a \$1,472 abolishment service and a \$84 temporary disconnection service, customers are likely to choose the temporary disconnection service. They may state there is potential to reconnect gas in the future to avoid incurring an abolishment charge. Such a disincentive may lead to a material number of customer connections remaining in situ with gas in them, raising safety issues.

Another possible scenario is that if an abolishment is undertaken, then the distributor may compel the retailer to pay the abolishment charge but leave it to recover costs from the customer. This would seem to entail significant financial risk to the retailer. The customer would no longer have a reticulated gas service so the threat of disconnection in case of non-payment would no longer be applicable. To the extent that retailers are able, or inclined, to pursue a customer who considers they no longer have a gas sector relationship, the transaction costs are potentially large relative to the unrecovered revenue.

#### **9.4.6.5 Socialising a portion of abolishment costs**

The alternative cost recovery mechanism would be to bundle a portion of small customer connection abolishments with transportation tariffs. This is sometimes referred to as 'socialising' abolishment costs. As socialised costs, a portion of small customer connection

abolishment costs would be funded by transportation tariffs paid by customers using gas network services at the time. That is, customers choosing to permanently disconnect from the gas network would not be required to pay the full abolishment charge.

When considering whether to socialise a portion of small customer connection abolishment costs, we must first consider the NGR. We consider there is no statutory barrier to bundling of small customer connection abolishment costs with transportation tariffs. Under rule 47A of the NGR no distinction is made between transportation services and ancillary services. The statutory emphasis rather is on ‘pipeline services’ and reference versus non-reference services. Both transportation and ancillary services fall within the scope of ‘pipeline services’. We consider it is open for the AER to bundle, or socialise, these costs should we consider that is the most appropriate approach.

In terms of the implications of socialising a portion of small customer connection abolishment costs, we consider equity issues arise. A cross subsidy would be created, benefiting customers who switch earliest. We consider it likely that customers choosing to electrify their gas load in the short to medium term are likely to have greater resources than customers who continue to use the gas network for longer.

As larger numbers of customers permanently disconnect from the JGN network over time, the financial burden of small customer connection abolishment costs would fall on a diminishing customer base, exacerbating the equity issue. That is, the socialised cost of small customer connection abolishments would be financed by a smaller number of customers, meaning each customer’s contribution would need to be greater. Customers who remain connected to JGN’s network the longest, who may be expected to be amongst the most disadvantaged, would carry the heaviest financial burden under a socialised approach.

In other respects, bundling a portion of small customer connection abolishment costs with transportation services may be beneficial. It would reduce the financial barrier to individual customers switching from natural gas to electricity, consistent with the NGR objective to reduce emissions. As such it may facilitate realisation of the environmental benefits described by the NGR. Any customer choosing to switch from natural gas to electricity, including disadvantaged customers, would receive a benefit financed by those customers who continue to receive gas network supply services.

Perhaps most importantly, socialising a portion of small customer connection abolishment costs may best align with the NSW safety regulator’s determination on safety. This is because socialising a portion of cost recovery would remove the financial barrier to abolishments being undertaken where safety considerations deem it to be appropriate. In the absence of a clear pathway for distributors and retailers to be confident that abolishment costs may be recovered from individual customers who choose to cease their supply, socialising a portion of those costs may be the most pragmatic way forward.

Bundling a portion of small customer abolishment costs across transportation tariffs for all customers means large customers would make a contribution to small customer costs until large customers cease their own gas supply.

Small customers would carry the financial burden of socialised small customer connection abolishment costs, but would benefit should they themselves choose to cease their gas supply in that they would not pay a stand-alone abolishment charge.

#### **9.4.6.6 Temporary and Permanent Disconnection (Abolishment) Services Option**

JGN submitted that around two thirds of its current abolishments are for renovations and knock down rebuilds that are only temporary, with these customers subsequently reconnecting to the gas network once the works are complete.<sup>53</sup>

We therefore raise for consultation the option of splitting the abolishment service into two services. One service would be a cost reflective temporary abolishment service with the fee of \$1,104 for sites where renovations or knock down rebuilds take place. These sites do not have the option of the disconnection service, as JGN's policy is that a gas connection must be abolished before significant works are undertaken at the premises. Levying a cost reflective abolishment tariff on these customers would reduce the price burden created for remaining gas customers via socialisation. Once the rebuild is completed a request for a new connection to the gas network will be required, which manages the moral hazard issue (namely, that customers will be incentivised to claim they will not re-connect).

The other service would be the permanent abolishment service with the fee of \$250, partially socialised for customers permanently disconnecting from the gas network. These households do have the option of the disconnection service (subject to being upfront about permanently defecting from the gas network), which means that partial socialisation would incentivise permanent abolishment over the disconnection service.

We also suggest there would appear to be benefit from aligning the relevant terminology across gas distributors. We suggest JGN consider the following change to the terminology for its current abolishment service:

- Permanent disconnection (abolishment) – permanent decommissioning of a delivery point by sealing the main at the T intersection, removing gas from the connecting pipe, removing the meter and removing the service line/pipe where possible to prevent the withdrawal of gas at the delivery point from the pipeline at the street.

#### **9.4.7 Other Ancillary reference services**

We are satisfied that JGN's proposed charges for its remaining ancillary reference services (that is, with the exception of the small customer abolishment charge) are reasonable. These approved prices are set out in table 9.6.

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<sup>53</sup> JGN, Response to AER Information Request #017, 4 October 2024, p. 5.

**Table 9.6 JGN’s approved ancillary reference services prices**

Ancillary reference service (individual price caps)	2025–26
Hourly charge	\$206.00 plus \$206.00 per hour after the first hour
Disconnections – Volume Customer Delivery Points	Completed activity charge: \$84.00 Wasted Visit: \$46
Reconnections – Volume Customer Delivery Points	Completed activity charge: \$118.00 Wasted Visit: \$118.00
Disconnection and Reconnection – Demand Customer Delivery Points	Completed activity charge: individually priced
Expedited reconnection	Completed activity charge: \$196.00 Wasted visit charge: \$196.00
Abolishment	Completed activity charge: <ul style="list-style-type: none"> <li>Above 25m<sup>3</sup>/hr: individually priced</li> </ul>
Special meter read	Completed activity charge: \$17.00 Wasted visit charge: \$17.00

Source: AER analysis of JGN, 2025–30 Access Arrangement Proposal, Attachment 10.1 Pricing, June 2024 p. 19.

#### 9.4.8 Issues to be considered for revised proposal

We ask JGN to (in its revised access arrangement revisions proposal):

- comment on revenue recovery from demand customers and flattening the volume customer declining block tariff structure.
- comment JGN’s gas transportation tariff reform pathways to achieve flat tariffs, including bill impact modelling, for all tariff classes including demand customers.
- comment on the option of setting the gas transportation tariff side constraint to 2% rather than the current 10%, to align with other gas distributors.
- comment on the option of partially socialising small customer abolishment costs.
- provide updated forecasts of small customer abolishment numbers per year.
- provide estimated bill impacts of partially socialising small customer abolishment costs through transportation tariffs.
- comment on the option of two abolishment services, a temporary abolishment service and a permanent abolishment service.



- comment on the option of aligning terminology for abolishments across gas distributors.

More broadly, we encourage stakeholders to provide us with written submissions on:

- the option of revenue recovery from demand customers and flattening the volume customer declining block tariff structure.
- the option of gas transportation tariff reform pathways to achieve flat tariffs, including bill impact modelling, for all tariff classes including demand customers.
- the option of setting the gas transportation tariff side constraint to 2% rather than the current 10%, to align with other gas distributors.
- the option of two abolishment services, a temporary abolishment service and a permanent abolishment service.
- associated equity and safety issues around abolishment.
- comment on the option of aligning terminology for abolishments across gas distributors.

## 9.5 Revisions

**Table 9.7 Reference tariff setting revisions**

Revisions	Column heading
Revision 9.1	Please set out the changes proposed to be made to the declining block tariff structure during the 2025–30 regulatory period, taking into account the issues identified and discussed in this attachment.
Revision 9.2	Amend the ancillary reference tariff to be \$250 in the 2025–26 year. <sup>54</sup>

Source: AER's analysis

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<sup>54</sup> As an ancillary reference tariff it will be escalated annually by the ancillary reference tariff variation mechanism which is addressed in Attachment 10 of this draft decision.

# **A Confidential appendix to Attachment 9 – Reference tariff setting**

# Glossary

Term	Definition
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
Ancillary RS	Ancillary Reference Service
CAB	Consumer Advisory Board
CCP31	Consumer Challenge Panel, sub-panel 31
JGN	Jemena Gas Networks
NGL	National Gas Laws
NEM	National Electricity Market
NSW	New South Wales
NSW DCCEEW	NSW Department of Climate Change, Energy the Environment and Water
NGO	National Gas Objectives
NGR	National Gas Rules
(PGN) team	Pipeline and Gas Networks team (NSW safety regulator)
Transportation RS	Transportation Reference Service