Draft decision

AusNet Gas Services (Victoria) 2023−28 access arrangement variation proposal

January 2025

AUSTRALIAN ENERGY REGULATOR

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Invitation for submissions

This document sets out the AER's draft decision on the access arrangement variation proposal submitted by AusNet Gas Services (AusNet) on 30 September 2024.

In response to our draft decision, AusNet has the opportunity to submit a revised proposal by **14 March 2025**.

Interested stakeholders are invited to make submissions on both our draft decision and AusNet's revised proposal (once submitted) by **11 April 2025**.

Submissions should be sent to: VicGAAR2023@aer.gov.au.

Alternatively, submissions can be sent to:

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Submissions should be in Microsoft Word or another text readable document format.

We prefer that all submissions be publicly available to facilitate an informed and transparent consultative process. Submissions will be treated as public documents unless otherwise requested.

Parties wishing to submit confidential information should:

1. Clearly identify the information that is the subject of the confidentiality claim.
2. Provide a non-confidential version of the submission in a form suitable for publication.

All non-confidential submissions will be placed on our website. [1]

[1] For further information regarding our use and disclosure of information provided to us, see the *ACCC/AER Information Policy* (June 2014), which is available on our website: www.aer.gov.au/publications/corporatedocuments/accc-and-aer-information-policy-collection-and-disclosure-of-information.

Executive summary

The Australian Energy Regulator (AER) exists to ensure energy consumers are better off, now and in the future. Consumers are at the heart of our work, and we focus on ensuring a secure, reliable, and affordable energy future for Australia. The regulatory framework governing gas transmission and distribution networks is the National Gas Law and Rules (NGL and NGR). Our work is guided by the National Gas Objective (NGO).

A regulated gas network business must periodically apply to us for a ruling on network charges, in the form of an access arrangement specifying the services it will provide, the tariffs for those services, and the other terms and conditions on which they will be provided.

AusNet Gas Services (AusNet) provides reticulated gas distribution services in Victoria.

On 2 June 2023, we released our final decision on the access arrangement proposal submitted to us by AusNet for the 2023−28 access arrangement period (2023 final decision). Among other things, our 2023 final decision permitted AusNet to recover from customers $105 million ($2022−23) in accelerated depreciation.

On 30 September 2024, AusNet submitted a proposal to vary its approved 2023−28 access arrangement by increasing its accelerated depreciation to $175 million ($2022−23) (the proposal). With associated adjustments to its capital expenditure and operating expenditure forecasts (capex and opex), AusNet proposed to recover an additional $98.1 million ($nominal, smoothed) from customers over the remaining 3 years of AusNet's current access arrangement period: 2025−26, 2026−27 and 2027−28. This would result in real price increases of 8.87% per annum in those years instead of the 2.41% per annum real increases determined in our 2023 final decision.

AusNet submitted that its proposal is in response to recent initiatives by the Victorian Government and the Essential Services Commission of Victoria (ESCV). These include a partial ban on new gas connections, cost reflective connection charges for the connections that do occur, and announced intentions to undertake regulatory impact statement (RIS) assessments for electrification of commercial buildings and gas appliance bans.

Having received AusNet's proposal, the AER was required to decide whether or not we considered the variation non-material.[2] On 25 October 2024, we decided that AusNet's proposal is material. In coming to this conclusion, we considered:[3]

- the monetary value of the proposal
- the fact that the proposal raises significant issues relating to:
  - the potential revenues and tariffs for AusNet
  - the likely impact on AusNet's customers (including the likely impact on customer gas bills)
  - the precedent that could be set for other network service providers.

[2] NGR, rule 66(1).

[3] https://www.aer.gov.au/industry/registers/access-arrangements/ausnet-services-access-arrangement-2023-28-variation-proposal/initiation

Accordingly, we referred the proposal to be dealt with as an access arrangement proposal under Division 8, Part 8 of the NGR.[4]

AusNet's proposal is novel in that it is the first time that a gas network service provider has submitted for the AER's approval a proposal for a variation of an access arrangement in accordance with rule 65 of the NGR.

The subject matter of the proposal is relevant not only to AusNet but to all regulated gas networks, their customers and stakeholders. Accelerated depreciation is a regulatory tool we use to reduce asset stranding risk arising from demand uncertainty in the gas sector. While accelerated depreciation leads to higher revenues over the access arrangement period, it can help reduce asset stranding risk to some extent by reducing the residual capital base to be recovered from a smaller customer base in the long term.

AusNet's proposal coincides with cost-of-living pressures that continue to impact energy customers, with a disproportionate impact on customers experiencing vulnerability. Any proposal that would increase utility bills must be viewed in the context of both the energy transition and the economic circumstances experienced by existing customers of gas networks such as AusNet's.

We published AusNet's proposal on the AER website and called for submissions.[5] Thirteen submissions were received from a range of customer and environmental advocacy groups, energy retailers, individual large and small customers, and the Victorian Minister for Energy and Resources.

Most stakeholder submissions opposed AusNet's proposal. They expressed concern about the price impacts and the perceived transfer of risk from AusNet to customers. Stakeholders also argued that accelerated depreciation is predominantly about protecting gas network investors from the risk of economic stranding of their investments, rather than about mitigating future price shocks. A small customer submission noted their reluctance to pay higher bills for gas networks when they face significant barriers to electrifying their apartment building.[6]

In contrast, the Energy Users Association of Australia (EUAA), the Energy Networks Association (ENA) and Brickworks (a large AusNet gas customer) supported AusNet's proposal.[7] In their submissions, these stakeholders focused on the policy and regulatory changes referenced by AusNet's proposal and the opportunity to bring forward investment cost recovery before total customer numbers begin to fall.

We have carefully assessed AusNet's proposal, its supporting information and stakeholder submissions. Our draft decision is to not approve AusNet's proposal. We consider AusNet has not justified the various elements of its proposal. In our view, the impact of Victorian policy and regulatory changes will likely accrue more slowly than AusNet has proposed. We also note that how gas customers respond to those changes is uncertain. In addition, some

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4 NGR, rule 66(3).

5 See *AusNet Services – Access Arrangement 2023–28 – Variation proposal*.

6 Jan Lacy, *Submission re. AusNet Services Access Arrangement 2023−28 variation proposal*, November 2024.

7 EUAA, *Submission on AusNet Services' variation proposal*, November 2023; Brickworks, *Submission on AusNet Services' variation proposal*, November 2023; ENA, *Submission on AusNet's variation proposal*, November 2024.

elements of AusNet's proposal are already catered for by existing flexibility mechanisms within its approved 2023−28 access arrangement. We therefore consider that intervention is not required. Our draft decision on each element of AusNet's proposal is summarised below:

- Demand forecasts – we consider the actual decline in customer numbers over the remaining years of the 2023−28 access arrangement period, is likely to be smaller than AusNet has proposed and any difference to the existing forecast will be immaterial.
- Capex – we consider that because the actual decline in customer numbers is likely to be smaller than AusNet proposed, changes to AusNet's approved capex forecast are not required.
- Opex – the cost of Energy Safe Victoria (ESV) levies is already appropriately accounted for in AusNet's approved opex forecast; AusNet will be fully compensated for any increase in abolishments compared to forecasts by the true-up mechanism in its approved access arrangement; and we consider output growth will not change materially, so AusNet's opex forecast does not require adjustment.
- Accelerated depreciation – we consider that the risk of asset stranding faced by AusNet has not materially changed since our 2023 final decision. This is because our 2023 final decision on accelerated depreciation took into account the Victorian Government's Gas Substitution Roadmap. We note too that further increasing accelerated depreciation in an environment of declining demand could exacerbate upward pressure on prices, and potentially trigger an unintended disconnection spiral.

We note that AusNet will begin its own stakeholder consultation on its 2028−33 access arrangement proposal relatively soon, for submission to us by July 2027. Rather than amending AusNet's approved 2023−28 access arrangement, we consider the issues raised by AusNet's proposal can be better assessed in the context of its 2028−33 access arrangement proposal.

Details of our assessment and reasons for our draft decision are set out in the sections below. Stakeholder submissions are available at our website, along with AusNet's proposal.

This draft decision does not canvass elements of AusNet's approved 2023−28 access arrangement which AusNet did not propose to vary. This includes reference services, reference tariffs, cost pass throughs and incentive schemes, amongst other things. These elements remain unchanged from our 2023 final decision.

We note that the NGR provides network service providers, such as AusNet, with opportunity to apply to vary their approved access arrangement but customers do not have the same opportunity. This asymmetry of opportunity has not influenced our draft decision on AusNet's proposal but we consider it noteworthy given the novelty of this process.

Next steps

Following this draft decision, AusNet can submit to us a revised proposal in accordance with rule 60 of the NGR. Should AusNet choose to do so, it must be provided to us no later than **14 March 2025**. In response, stakeholders will have opportunity to provide further written submissions by **11 April 2025**. We intend to release our final decision by **mid-May 2025**.

Contents

1 AusNet's proposal

This section summarises AusNet's proposal and briefly summarises relevant elements of our 2023 final decision.

1.1 AusNet's proposal

AusNet's proposal seeks to:[8]

- increase AusNet's total revenue over the 2023−28 period by 7.7% or $98.1 million ($nominal, smoothed)
- increase its accelerated depreciation from $105 million already approved by the AER to $175 million ($2022−23)[9]
- increase its opex allowance by $8.2 million ($2022−23), reflecting higher ESV levies, an expected increase in the number of abolishments performed annually[10] and lower output growth
- reduce its capex allowance by $59.6 million ($2022−23) to account for reduced customer connections and the ESCV decision to establish cost reflective connection tariffs for small (volume) customers.

Table 1 sets out AusNet's proposed smoothed revenue requirement compared to the approved revenue requirement in its 2023−28 access arrangement. AusNet submitted that, in real terms, its proposal would see price changes of 8.87% per annum over the 3 remaining years of the 2023−28 period.

Table 1 AusNet's proposed smoothed revenue requirement and price path

	2023−24	2024−25	2025−26	2026−27	2027−28	Total
Revenue ($m, nominal, smoothed)						
AER 2023 final decision	230.2	243.4	256.0	266.2	274.5	**1,270.3**
AusNet's proposal	230.2	243.4	270.4	298.1	326.3	**1,368.4**
Annual real price change						
AER 2023 final decision	2.41%	2.41%	2.41%	2.41%	2.41%	n/a
AusNet's proposal	2.41%	2.41%	8.87%	8.87%	8.87%	n/a

8 NGR, rule 65(1).

9 AusNet proposed $200 million in accelerated deprecation during the 2023−28 reset.

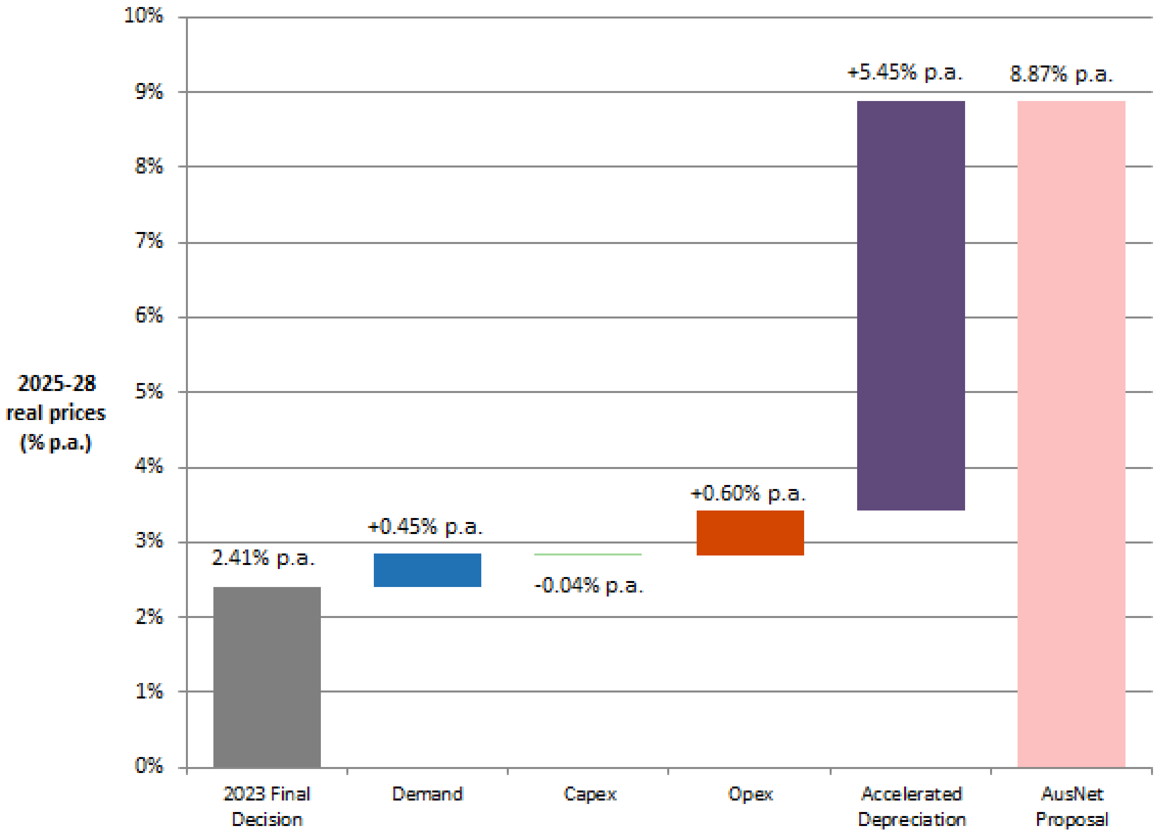
10 AusNet's approved 2023−28 access arrangement includes an ex-ante opex allowance for abolishment but also includes a true-up mechanism to correct for under (over) recoveries that will be recovered from customers (returned to customers) in future regulatory years.

Source: AER, *2023–28 final decision PTRM, updated for 2024–25 return on debt,* January 2024; AusNet, *GAAR variation 2024–28 PTRM*, September 2024.

Figure 1 illustrates the drivers of tariff changes under AusNet's proposal:

- accelerated depreciation represents the bulk of AusNet's proposed tariff increase (5.45% of the total 8.87%)
- capex represents a minor tariff reduction (-0.04%)
- updated demand pushes tariffs up (0.45%), more than offsetting the capex-driven tariff reduction
- opex also pushes tariffs up (0.6%).

Figure 1 Drivers of tariff changes from AusNet's proposal



In its proposal, AusNet referenced the following initiatives by the Victorian Government and ESCV as the reasons for it seeking the variation:

- from 1 January 2024, the Victorian Government has banned new gas connections for new dwellings, apartment buildings, and residential subdivisions requiring planning permits
- from 1 January 2025, the updated gas distribution code of practice requires gas distributors to impose full upfront charging on customers for new gas connections
- during 2024, the Victorian Government consulted on a RIS on an appliance ban for rental properties

- in late 2024, the Victorian Government published for consultation a RIS which looks at electrifying commercial buildings and introducing an end-of-life appliance replacement ban for residential customers.

With respect to the above initiatives, AusNet submitted:

> This is a material change to our operating environment, such that the assumptions that underpinned the Final Decision for our AA, no longer reasonably represent the expected future circumstances of our network. Importantly, the customer number forecast approved by the AER had our residential customer numbers growing throughout the regulatory period. This continued growth is no longer a credible forecast. We are already seeing policy changes impact our network with the projected rate of gas reticulation declining significantly, a rapid take up of electrification incentives and increasing abolishments and dormant connections. We reasonably expect the new policies will further accelerate customers' transition away from gas. [11]

AusNet further submitted:

> In the near term, this shift means difficult decisions need to be made to make the transition as equitable as possible for both current and future customers. Early actions such as faster capital recovery is the best way to protect customers and enable us to continue managing our network safely and reliably for as long as it is needed by Victorians.
>
> Stabilising the long-term price, recovering sunk costs and managing the impacts of a network that is declining are best addressed while the customers for which the sunk investment was made remain on the network. Putting off decisions around sunk cost recovery for some future point is no longer tenable – it is markedly unfair to knowingly place most of the recovery on the future customer base, most likely to be those that are least able to transition through no fault of their own.
>
> As a result of the above, we are proposing to increase our accelerated depreciation from the amount of $105m approved by the AER to $175m. [12]

1.2 AusNet's approved 2023−28 access arrangement

On 2 June 2023, we approved AusNet's gas access arrangement for the 2023−28 access arrangement period. Relevantly, our 2023 final decision incorporated:

- Total smoothed revenue of $1,270.3m ($nominal). This was $78.7 million ($nominal), or 5.8%, lower than AusNet's 2023 revised proposal.
- $105 million ($2022−23) in accelerated depreciation. This was $95 million ($2022−23), or 48%, lower than AusNet's 2023 revised proposal.

[11] AusNet Services, *AusNet Gas Access Information 24–28,* September 2024, p. 2.

[12] AusNet Services, *AusNet Gas Access Information 24–28,* September 2024, p. 2.

- Total opex of $349.8 million ($2022−23).[13] This was $14.5 million ($2022−23), or 4.2%, higher than AusNet's 2023 revised proposal.

[13] This amount was exclusive of ancillary reference services and inclusive of debt raising costs.

2 Demand forecasts

This section sets out our draft decision on AusNet's updated demand forecasts for the remainder of the 2023–28 access arrangement period.

2.1 AER draft decision

Our draft decision is to not accept AusNet's proposed demand forecast for the 2023–28 period. We are not satisfied that AusNet's proposed variation to its connections and demand forecast complies with rule 74 of the NGR. That is, we are not satisfied that the forecast represents the best forecast or estimate possible in the circumstances. AusNet should revisit its forecast in any revised proposal.

We do not accept AusNet's proposed decline in customer numbers. We consider:

- the decline is slower than AusNet is anticipating over the remaining 3 years of the period
- any changes to the forecasts are immaterial to our final decision forecast for the 2023–28 access arrangement period
- an adjustment to the demand forecast and capex is not warranted.

2.2 AusNet's proposal

As discussed in section 1.2 AusNet submitted that there has been a material change of circumstances since we made our final decision on its 2023–28 access arrangement in June 2023.[14] In particular, AusNet considers that the following have had an impact on the level of gas connections and resulting forecast capex required to connect customers to its gas network:[15]

- gas connection ban

  From 1 January 2024, new dwellings, apartment buildings, and residential subdivisions requiring new planning permits in Victoria are not allowed to be connected to the reticulated gas network. This includes all new public and social housing delivered by the Victorian Government. This ban extends to small dwellings that were exempt from planning permits and was given effect through amendments to Victoria's planning provisions.

- up front connection charges

  From 1 January 2025, developers or residential homeowners are required to pay the full upfront cost of their new gas connection. This works as a disincentive to connect to gas as prior to this change, connecting customers were not required to fund the full cost of the connection.

- gas substitution road map update

  Updates to the Victorian Gas Substitution Roadmap will bring further incentives to Victorians to consider electrification and encourage a shift away from gas given the net

[14] AusNet Services, *Access Arrangement Information 2024–28*, September 2024, p. 7.

[15] AusNet Services, *Access Arrangement Information 2024–28*, September 2024, p. 8.

zero and decarbonisation objectives. This includes incentives to install electricity friendly appliances (such as energy efficient reverse cycle air conditioning and heat pump or solar hot water) as well as the removal of the incentives to install gas appliances for heating, hot water and cooking.

- RIS process for minimum standards for rental properties and rooming houses

  The Victorian Government has released a RIS for consideration, which proposes additional minimum standards for rental properties and rooming houses relating to energy efficiency and end of life replacement of gas appliances with electric alternatives.

AusNet's gas network growth is driven predominantly by new estate developments. Given changes in government policies, AusNet anticipates a large drop in new connections. [16] Table 2 below outlines AusNet's proposed changes in forecast residential gas connections for the remainder of the access arrangement period. AusNet is forecasting a 3.5% reduction in residential customer numbers by the end of the 2023–28 access arrangement period compared to our 2023 final decision.

Table 2 AusNet's proposed total residential customer numbers compared to our 2023 final decision

	2023–24	2024–25	2025–26	2026–27	2027–28
AER Final Decision 2023	781, 161	792,591	802,844	808,824	812,193
AusNet Services Proposal	781,161	792,591	791,983	789,892	783,990
Difference (customer numbers)	–	–	-10,861	-18,932	-28,204
Difference (%)	–	–	-1.4%	-2.3%	-3.5%

Source: AusNet, *Access Arrangement Information 2024–28*, 30 September 2024, p. 22; AER*, AER - Final decision - AusNet 2023–28 - PTRM - 2024–25 return on debt update - January 2024*, January 2024; AusNet, *GAAR Variation 2024-28 PTRM - 30 Sep 2024*, September 2024.

Note: Numbers may not sum due to rounding.

Further, Table 3 below outlines AusNet's proposed changes in forecast residential consumption for the remainder of the access arrangement period. AusNet is forecasting a 0.1% increase in residential customer consumption for the remaining 3 years of the 2023–28 access arrangement period compared to our 2023 final decision.

Table 3 AusNet's proposed total residential gas consumption (TJ) compared to our 2023 final decision

	2023–24	2024–25	2025–26	2026–27	2027–28	Total
AER Final Decision 2023	30,595.9	30,156.2	29,338.9	27,941.9	26,044.3	144,077.2
AusNet Proposal	30,595.9	30,156.2	29,101.1	27,927.9	26,467.2	144,248.3

16 AusNet Services, *Access Arrangement Information 2024–28*, September 2024, p. 11.

	2023–24	2024–25	2025–26	2026–27	2027–28	Total
Difference	–	–	-237.8	-14.0	422.9	171.1
Difference (%)	–	–	-0.8%	-0.1%	1.6%	0.1%

Source: AusNet, *Access Arrangement Information 2024–28*, 30 September 2024, p. 22; AER*, AER - Final decision - AusNet 2023–28 - PTRM - 2024–25 return on debt update - January 2024*, January 2024; AusNet, *GAAR Variation 2024-28 PTRM - 30 Sep 2024*, September 2024.

On the basis of AusNet's updated customer numbers and consumption forecasts, AusNet proposed to reduce the corresponding forecast connection capex and defer a small portion of its augmentation program.[17] This is discussed further in section 3.2 below on capex.

2.3 Stakeholder views

We received 4 submissions from stakeholders on the proposed variation to demand, with the primary focus being on accelerated depreciation.

The Victorian Minister for Energy and Resources submitted:

> Victoria encourages the AER to closely scrutinise whether those revised forecasts are evidence of a material or significant change in demand, or simply represent a steady state for residential customer numbers and demand over the remaining period to 30 June 2028 and are not representative of a dramatic change in demand that warrants a re-opening.[18]

AGL submitted:

> While gas network usage is set to rapidly decline, particularly in the residential sector, the rate of electrification and the extent of its impact on customer numbers and asset stranding is still uncertain… There is still a level of uncertainty associated with the government policies cited in AusNet's submission...[19]

The Victorian Council of Social Services (VCOSS) submitted:

> …the AusNet forecast relies on the pace of household electrification in Victoria increasing dramatically. In this, AusNet predictions appear to stem from Victorian Government policy proposals announced in the Gas Substitution Roadmap Update that are not yet locked in, including new minimum energy efficiency standards for rentals, and electrification policies that would require replacing gas appliances with electric alternatives at the end of life. Final decisions on these policies have not been made, so it is not reasonable for AusNet to rely – in this instance – on the exact timeframes laid out in the Gas Substitution Roadmap Update.[20]

[17] AusNet Services, *Access Arrangement Information 2024–28*, September 2024, p. 24.

[18] Victorian Minister for Energy and Resources, *Submission on AusNet Services' variation proposal*, December 2023, pp. 2–3.

[19] AGL, *Submission on AusNet Services' variation proposal*, November 2023, p. 1.

[20] VCOSS, *Submission on AusNet Services' variation proposal*, November 2023, p. 2.

Environment Victoria submitted:

> The significant policy changes proposed by the Victorian government are highly contested and their timing and exact form is yet to be confirmed. Further policies can be expected over time. It would not be in the interests of consumers for networks to reopen their access arrangements each time something changes.[21]

We have taken these submissions into account in developing the positions set out in this draft decision.

2.4 Reasons for draft decision

For the reasons outlined below, our draft decision is to not accept a variation in the demand forecast.

Rule 74(2) of the NGR requires forecasts in access arrangement proposals to be arrived at on a reasonable basis, and to represent the best forecast possible in the circumstances. We accepted AusNet's demand forecasting methodology in our 2023 final decision but substituted a higher connections forecast than was proposed by AusNet.[22]

We have reviewed the reasonableness of AusNet's updated connections and consumption forecasts compared to those in place for our 2023 final decision, including by obtaining an independent assessment by Oakley Greenwood,[23] which considered whether AusNet has accounted for relevant information and made reasonable assumptions in response to recent policy changes in Victoria, especially regarding the decline in new connections.

We have had considered the Victorian RIS on minimum standards for rental properties and rooming houses at a high level.[24] The RIS was released by the Victorian Government in late November 2024. To the extent any policy interventions arising from the RIS could impact customer numbers or usage during the remaining years of the 2023−28 access arrangement period, we will be able to consider the implications in the context of assessing an AusNet revised proposal.

Having had regard to Oakley Greenwood's independent assessment, with which we agree, we consider that AusNet's connections forecast contains a number of unjustified assumptions. Applying more realistic assumptions results in a slower decline in connections than proposed by AusNet (see Table 4 below). As a result, we consider that AusNet's proposed changes in customer numbers in the remaining years of the period, compared to our 2023 final decision, are not material.

The largest impact on AusNet's updated customer numbers comes from its perception of a 'consumer sentiment effect'. AusNet assumed that only 60% of eligible customers will

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21 Environment Victoria, *Submission on AusNet Services' variation proposal*, November 2023, p. 2.

22 For our reasoning in our 2023 final decision, see: AER*, final decision, AusNet Services gas access arrangement 2023–28 – Attachment 12 – Demand forecast*, June 2023, p. 4.

23 Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, December 2024.

24 Engage Victoria, *Minimum Standards for Rental Properties and Rooming Houses*.

connect to the gas network due to reduced sentiment towards gas, and that this percentage will decrease to 20% by 2029. However, more recent information provided by AusNet in response to workshops and information requests[25] indicated that consumer sentiment has actually improved since the earlier survey was undertaken.[26] This suggests that there is uncertainty regarding sentiment and this represents a risk to the accuracy of AusNet's forecasting more broadly. As such, Oakley Greenwood's recommendation is to remove this component of the forecast.

Further, an error has been identified in AusNet's modelling (which AusNet and its consultant CIE have acknowledged). AusNet's forecast models the policy change a year early, starting in 2023 rather than 2024.[27] This is significant because the modelling forecasts only minor effects on new customer connections in the policy's early years, with its effects cumulatively building over the later years. Because AusNet's modelling incorrectly starts the policy change a year earlier, there is a larger apparent decline in new customer connections compared to our 2023 final decision.

In reviewing the connections forecast, and having considered Oakley Greenwood's analysis, we consider inclusion of the 'upfront connection charge on new connection numbers' variable in the forecasting approach was reasonable. However, there are two input assumptions we do not consider appropriate:

- AusNet estimated the average retail gas bill at $948 per annum (based on a CANSTAR rating survey in December 2023).[28] However, the ESCV published median retail bill for a residential customer connected to AusNet's network is $2,016 for the year 2023–24.[29] This impacts the customer number modelling. AusNet's modelling calculates the sensitivity between the upfront connection charge ($1711.64) and on-going charges (retail bill) as part of the elasticity of demand used to work out the percentage reduction in customer connections. The higher on-going charge means there is less impact on demand than AusNet forecasts.[30]
- AusNet undertook its net present value (NPV) analysis over 10 years. We consider this is unlikely to align with a customer's perception of the economic life of its gas connection, as most gas appliances exceed 10 years of life. Oakley Greenwood advised that 15 years is likely to be more reasonable. We find Oakley Greenwood's assumption more reasonable. This reduces the modelled speed at which customers seek to disconnect from gas.[31]

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25 AER and AusNet Services, demand forecasting workshop, 18 November 2024.

26 Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, 19 December 2024, pp. 6–7.

27 Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, 19 December 2024, p. 6.

28 Canstar Blue, *What is the average gas bill*, 5 January 2025.

29 ESCV, *Victorian Energy Market Report – September 2024*, September 2024, p. 23.

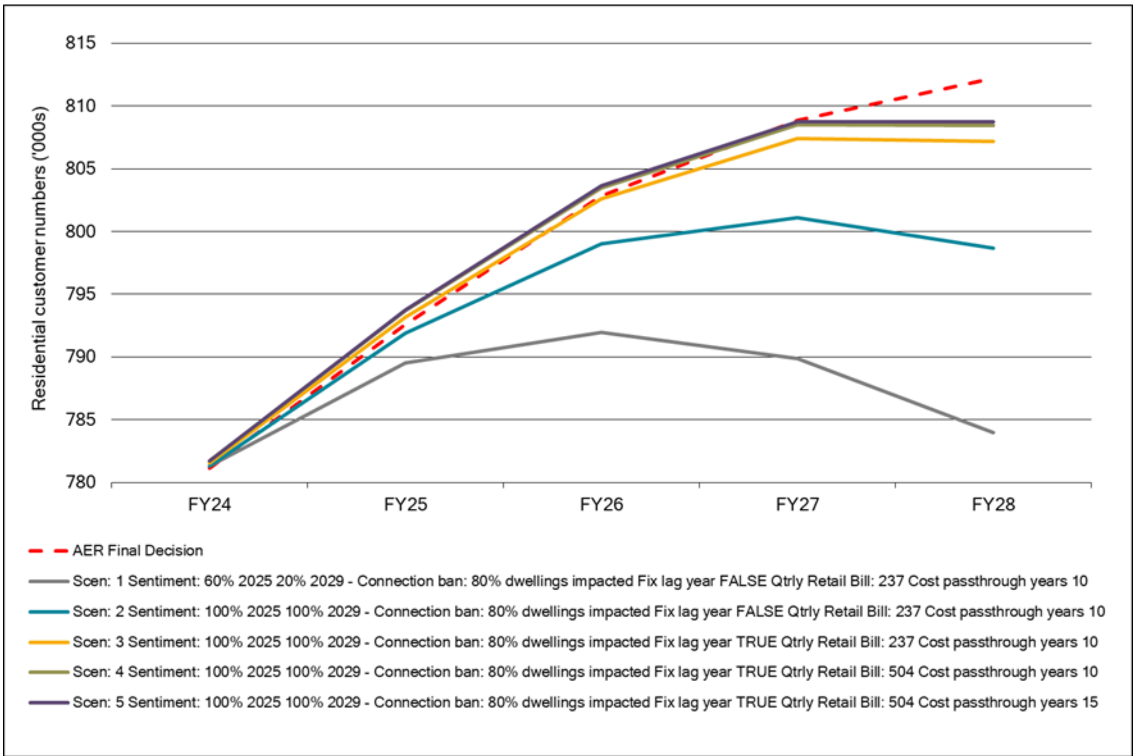
30 Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, 19 December 2024, p. 5.

31 Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, 19 December 2024, p. 6.

The above adjustments are expressed in the following scenarios outlined in Figure 2 below. The results under each scenario are relative to AusNet's proposal forecast, and each scenario is cumulative:

- Scenario 1: AusNet's variation forecast
- Scenario 2: Scenario 1 with the effect of 'consumer sentiment' removed
- Scenario 3: Scenario 2 with the planning approval lag start year set to 2024 (original start year was 2023, due to the formula error)
- Scenario 4: Scenario 3 with the retail bill amount increased in line with the ESCV's published median retail bill.
- Scenario 5: Scenario 4 with the NPV analysis years increased from 10 to 15.

Figure 2 Residential connection number scenarios verses AusNet's forecast



Source: Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, 19 December 2024, p. 12.

Having assessed AusNet's customer number forecast and Oakley Greenwood's analysis, we consider that Oakley Greenwood has identified a number of issues with AusNet's forecast. We consider Oakley Greenwood's alternative forecast is more reasonable.

Table 4 sets out our residential customer numbers making the adjustments outlined above in line with scenario 5.

Table 4 AER's alternative forecast for AusNet Services' residential customer numbers

	2023–24	2024–25	2025–26	2026–27	2027–28
AER's Final Decision (June 2023)	781,161	792,591	802,844	808,824	812,193
AusNet Proposal	781,161	792,591	791,983	789,892	783,990
AER's alternative forecast	781,161	792,591	802,958	808,867	808,742
Difference (customer numbers) compared to the 2023 final decision	–	–	114	43	-3,451
Difference between the 2023 final decision and AER's alternative forecast (%)	0.00%	0.00%	0.01%	0.01%	-0.42%

Source: Oakley Greenwood, *Review of AusNet Services' Access Arrangement Variation demand forecast*, 19 December 2024, p. 12; AER analysis.

AusNet's updated forecast for residential customer consumption is 0.1% higher than the forecast in our 2023 final decision (see Table 3). The forecast and approach adopted is largely in line with our 2023 final decision and is not materially different. We do not have any concerns with the forecast for residential consumption.

Our forecasting review reaffirms that our demand forecasts set out in our 2023 final decision are in line with AEMO's gas forecasts and that the actual customer numbers and consumption forecast for the first year of the period (2023–24) do not diverge much. Actual customer numbers for 2023–24 were 3,871 more than anticipated (0.5% increase) and actual customer consumption was less than forecast (5.3% decrease).[32]

Our alternative estimate for residential connections by the end of the period is 808,742 customers – compared to AusNet proposed variation of 783,990. This represents 3,451 less than our 2023 final decision of 812,193 connections by the end of the period (2027–28) (see Table 4). We consider the reduction in residential connections is not materially different to our forecast determined in our 2023 final decision.

Regarding consumption, we also consider the variation in this forecast (0.1% increase, see Table 3) is not materially different to our 2023 final decision. Further, there is also uncertainty

32 AusNet Gas Services 2023–24 – Annual – RIN Response – Actual – 29 November 2024; and AER analysis.

regarding the impact and timing of the policy changes on demand in the short term as highlighted by submissions.

We consider it more appropriate to review the demand forecast as part of the full access arrangement revision commencing in 2027, rather than on an ad hoc basis in response to new or updated government policy (which may change again prior to the revision period).

2.5 Revisions

Table 5 sets out the nature of the amendments in relation to demand forecasts that are required to make the proposal acceptable to the AER.[33]

Table 5 Revisions – demand forecast

Revision	Amendment
Revision 2.1	Provide additional information or further amendments to address the matters set out above in respect of the proposed demand forecast. Alternatively, Ausnet may wish to consider whether the 2023 final decision on demand forecast remains appropriate and submit an amendment on that basis. Any further information or amendments must be provided in accordance with, and subject to the limitations set out in, NGR Rule 60.

33 NGR r.59(2).

3 Capital expenditure

This section sets out our draft decision on AusNet's updated capex for the remainder of the 2023–28 access arrangement period.

Capex refers to costs and expenditure of a capital nature incurred to provide, or in providing, pipeline services.[34] This investment mostly relates to assets with long lives and these costs are recovered over several access arrangement periods.

3.1 AER draft decision

Our draft decision is to not accept AusNet's proposed variation in its capex in accordance with the new capex criteria, under rule 79(1) of the NGR. We consider our 2023 final decision on AusNet's capex reflects capex that would be incurred by a prudent service provider acting efficiently. As set out in section 3 of this draft decision, we consider any actual variation from the forecasts within our 2023 decision is unlikely to be material.

3.2 AusNet's proposal

AusNet proposal to reduce the forecast connection capex and defer a small portion of its augmentation program in response to its proposed variation in the demand forecasts. AusNet submitted that these adjustments are necessary to reflect its expectation of fewer new connections over the 2023−28 access arrangement period than was reflected in our 2023 final decision. Adjustments to forecast residential customer numbers drive most adjustments to forecast connections capex. The proposed changes in capex are set out in Table 6**.**

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34 NGR, r. 69.

Table 6 AusNet's proposed capex, comparison (millions, $2022–23)

Category	AER Final Decision 2023	AusNet Services Proposal	Difference ($)	Difference (%)
Mains replacement	132.3	132.3	–	–
Residential new customer connections	158.8	121.7	-37.1	-23.4
Commercial and industrial new customer connections	28.2	27.2	-1.0	-3.5
Residential meter replacement	25.6	25.6	–	–
Commercial and industrial meter replacement	8.1	8.1	–	–
Augmentation	19.8	15.1	-4.7	-23.7
IT capex	72.0	72.0	–	–
SCADA	3.2	3.2	–	–
Other	56.3	56.3	–	–
Total gross capex	**504.4**	**461.6**	**-42.8**	**-8.5**
Capital contributions	76.8	93.6	16.8	21.8
Total net capex	**427.6**	**368.0**	**-59.6**	**-13.9**

Source: AusNet, *Access Arrangement Information 2024–28*, 30 September 2024, p. 24; AusNet, *ASG - Revised proposal - Access Arrangement 2024–28 - Capex model - 24 January 2023*, January 2023; AusNet, *GAAR Variation 2024-28 Capex Model - 30 Sep 2024*, September 2024.

3.3 Stakeholder views

We received 2 submissions on the proposed variation to capex from Energy Consumers Australia (ECA) [35] and Lighter Footprints.[36] Both submissions stated that, in the context of a proposed increase to accelerated depreciation, AusNet should minimise its proposed capex program, even beyond its proposal to reduce connections and augmentation capex.

We have taken these submissions into account in developing the positions set out in this draft decision.

3.4 Reasons for draft decision

Rule 74(2) of the NGR requires forecasts in access arrangement proposals to be arrived at on a reasonable basis and to represent the best forecast possible in the circumstances.

We do not consider that the forecast advanced by AusNet in its proposal represents the best forecast possible in the circumstances.[37] We consider that the 2023–28 access arrangement

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35 ECA, *Submission on AusNet's variation proposal - November 2024*, November 2024.

36 Lighter Footprints, *Submission on AusNet's variation proposal - November 2024*, November 2024.

37 NGR, r. 74(2).

period forecast remains the best forecast possible in the circumstances. This is because the forecast in the number of customers remains materially unchanged from our 2023 final decision (as discussed in section 2.4 above). Since we do not accept AusNet's proposed variation to its demand, we do not accept AusNet's proposed reductions to its connections capex and augmentation capex which would arise from its revised customer numbers and consumption forecast.

In not accepting the variation in the demand forecast, we are also not accepting a change to the forecast capex for the 2023–28 access arrangement period on the basis that we do not consider the change to be necessary nor material.

3.5 Revisions

Table 7 sets out the nature of the amendments in relation to capex that are required to make the proposal acceptable to the AER.[38]

Table 7 Revisions - capex

Revision	Amendment
Revision 3.1	Provide additional information or further amendments to address the matters set out above in respect of the proposed capex. Alternatively, Ausnet may wish to consider whether the 2023 final decision on capex remains appropriate and submit an amendment on that basis. Any further information or amendments must be provided in accordance with, and subject to the limitations set out in, NGR Rule 60.

38 NGR r.59(2).

4 Operating expenditure

This section sets out our draft decision on AusNet’s updated opex for the remainder of the 2023–28 access arrangement period.

Opex is the operating, maintenance and other non-capital expenses incurred in the provision of pipeline services. Forecast opex is one of the building blocks we use to determine a service provider’s total revenue requirement.

4.1 AER draft decision

Our draft decision is not to accept AusNet’s proposal in respect of its opex forecast of $358.0 million ($2022–23)[39] for the 2023–28 access arrangement period. We are not satisfied AusNet’s proposed total opex forecast reflects the opex criteria[40] and the requirements for forecasts and estimates.[41] We consider:

- ESV levies payable by AusNet have already been accounted for in our 2023 final decision.
- The forecast of abolishments in our 2023 final decision remains the best possible forecast in the circumstances and the existing true-up mechanism in AusNet’s 2023–28 access arrangement will compensate it for any divergence from that forecast.
- AusNet’s proposed variation in the forecast rate of change for output growth is immaterial and was not arrived at on a reasonable basis.

4.2 AusNet’s proposal

AusNet’s proposed opex forecast of $358.0 million ($2022–23)[42] is $8.2 million, or 2.3%, above the forecast we approved in our 2023 final decision. AusNet has proposed three variations to the opex forecast we approved in our 2023 final decision:

1. an additional $5.1 million for higher ESV levies
2. an additional $5.0 million for higher abolishment costs
3. a reduction of $1.9 million for lower output growth.

4.3 Stakeholder views

We received 3 submissions on AusNet’s proposal which discussed opex issues from ECA, EUAA, and the Institute for Energy Economics and Financial Analysis (IEEFA). ECA

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39 AusNet, *GAAR Variation 2024–28 PTRM*, 30 September 2024.

40 Under rule 91 of the National Gas Rules (NGR), opex ‘must be such as would be incurred by a service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services.’ Where opex satisfies the test in rule 91, we say it ‘satisfies the opex criteria’.

41 Under rule 74 of the NGR, information in the nature of the forecast or estimate must be supported by a statement of the basis of the forecast/estimate. Further, forecasts and estimates must be arrived at on a reasonable basis and must represent the best forecast or estimate possible in the circumstances. Where a forecast or estimate meets the requirements of this rule we say it ‘satisfies the forecasts and estimates criteria’

42 AusNet, *GAAR Variation 2024–28 PTRM*, 30 September 2024.

submitted that the proposal should consider the impact of changes in the policy landscape on all cost elements.[43] Similarly the IEEFA submitted that if we accept AusNet's justification for reopening its access arrangement, we ought to also review all capex and opex in AusNet's proposal, to ensure it is kept to the minimal level required to continue safely operating the network while AusNet's demand declines.[44]

The EUAA supported the proposed opex increase, mostly due to higher ESV levies and AusNet's proposed impact of a higher volume of subsidised abolishments.[45]

We have taken these submissions into account in developing the positions set out in this draft decision.

4.4 Reasons for draft decision

Rule 74(2) of the NGR requires forecasts in access arrangement proposals to be arrived at on a reasonable basis, and to represent the best forecast possible in the circumstances.

Rule 91(1) of the NGR requires that opex must be such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services in a manner consistent with the achievement of the NGO.

We have considered AusNet's proposed total opex of $358.0 million ($2022–23) which reflects three variations compared to the opex forecast we approved in our 2023 final decision. We consider that these variations do not meet the requirements for forecasts and estimates (and specifically that they have been arrived at on a reasonable basis and represent the best forecast or estimate possible in the circumstances),[46] and they do not produce a total opex forecast that reflects the opex criteria.[47] We have set out our consideration of each of these three variations below. Given we do not consider any of these variations are reasonable, we do not consider that AusNet's total opex forecast meets the requirements for forecasts and estimates or reflects the opex criteria. Rather, we consider our total opex forecast in the 2023 final decision best meets these requirements and criteria.

ESV levies

We do not consider that AusNet's proposed step change for the ESV levy meets the requirements for forecasts and estimates.[48] As set out below, we consider this cost has already been appropriately accounted for in our final 2023 decision forecast for the 2023–28 access arrangement period.

AusNet proposed a new step change of $5.1 million to cover the expected difference in ESV levies in its opex forecast. It proposed escalating its actual invoice for ESV levies for 2024–25 by 3% year on year to forecast its ESV levies for 2025–26, 2026–27 and 2027–28.

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43 ECA, *Submission on AusNet's variation proposal*, November 2024, p. 2.

44 IEEFA, *Submission on AusNet's variation proposal*, November 2024, p. 4.

45 EUAA, *Submission on AusNet's variation proposal*, November 2024, p. 2.

46 NGR, r. 74.

47 NGR, r. 91.

48 NGR, r. 74.

AusNet stated that the ESV levy it pays increased substantially (by 42%) in 2023–24, after we made our 2023 final decision, continuing a trend over recent years of increases averaging around 10% per year. It also stated that ESV responsibilities continue to increase as the energy transition proceeds. It further advanced that, while the current increase is substantial, it is not above the 1% of allowed revenue that would meet a cost pass through threshold.[49]

Our 2023 final decision allowed for ESV levies to be included in base opex which we then trended forward, including by our price growth forecast. As also explained in our draft decision for the 2023–28 access arrangement period:

> In this regard we acknowledge that some costs may increase by more than the forecast rate of change; however, this is likely offset by other costs that increase by less than the forecast rate of change or by decreases in other cost categories over the 2023–28 access arrangement period.[50]

In our top-down assessment approach, we do not consider cost categories individually, but instead assess opex at a total level. Our approach allows for some opex cost categories to increase faster than the trend component and some opex cost categories to increase slower than the trend component.

Approving a step change for one cost category that is increasing more rapidly than the total opex rate of change, but not considering those categories increasing at a slower rate, would introduce an upward bias and overstate total opex.

In this context, we reviewed AusNet's total actual opex for 2023–24 and found it was $5.8 million lower than the forecast we approved in our 2023 final decision. This shows that other categories of opex increased by less than the total opex trend or went down.

AusNet did not identify these other categories of opex nor did it propose adjustments to account for any other changes. We consider that adding opex for increases in one cost category is unnecessary, and to do so without considering the changes to other categories would overstate the opex required. This view is consistent with the views expressed by some stakeholders, such as ECA and IEEFA, that we should consider the changes in all costs, not just those identified by AusNet.

Abolishments opex

We do not consider AusNet's proposed revision to the forecast abolishment costs meets the requirements for forecasts and estimates.[51] We consider the net disconnection forecasts AusNet relied on for its abolishment forecast are not a reasonable basis to forecast the number of abolishments over the remainder of the 2023–28 access arrangement period. This is because many customers leaving the gas network will request a disconnection rather than an abolishment.[52] After we accounted for this, we found AusNet's revised forecast to be

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[49] AusNet, *Gas Access Arrangement Variation – 2024–28*, pp. 25–27.

[50] AER, *AusNet 2023–28 – Draft Decision – Attachment 6 – Operating expenditure*, December 2022, p. 19.

[51] NGR, r. 74.

[52] Disconnection involves capping the customer's supply at the meter. Abolishment (or permanent disconnection) involves severing the customer's connecting pipe from the mains, sealing the mains, removing gas from the connecting pipe, resealing the ground surface and making the site safe. Abolishment may also require traffic control, depending on the location.

close to our 2023 final decision abolishment forecast. Given this, we are satisfied that the forecast of abolishments included in our 2023 final decision remains the best forecast possible in the circumstances for the 2023–28 access arrangement period. We also note that this expenditure is subject to a true-up for the actual number of abolishments via the tariff variation mechanism.

In our 2023 final decision, we determined that network users wishing to abolish their gas connections should not pay for the full cost of the service. We determined a discounted price to be paid by the network user and included an amount in forecast opex for the portion of abolishment cost that would be socialised.

In its proposal, AusNet proposed a revised forecast of the number of abolishments that will be requested over the remainder of the 2023–28 access arrangement period. It proposed there will be 7.7% per cent more abolishments in 2025–26, 2026–27 and 2027–28 than we included in our 2023 final decision. It proposed an increase of $5.0 million to reflect this increase in the forecast number of abolishments.

AusNet commissioned CIE to update its demand modelling over the 2023–28 access arrangement period. This included updated forecasts of residential customer net disconnections (disconnections plus abolishments less reconnections).[53] CIE forecast an increase in net disconnections of 26,774 over the remaining 3 years of the 2023–28 access arrangement period compared to historical average growth. However, CIE did not provide forecasts of disconnections, abolishments or reconnections individually. It only forecast the net figure.

Our 2023 final decision approved an opex forecast for the proportion of abolishment costs to be socialised. This forecast was based on AusNet's submitted abolishment forecast which we modified to account for:

- expected customer behaviour patterns in response to Victorian Government policies where, due to customers slowly becoming aware of policy intent and the time required for most households to accommodate the change in circumstances:
  - abolishments would increase over time instead of following the flat profile reflected in historical abolishment rates
  - increases in the rate of abolishments would likely lag behind the dates of the related policy changes.
- the likelihood that some customers (estimated at 26% of permanent disconnections) would perceive value in having a dormant connection on their property and that these customers will request a disconnection service, rather than an abolishment service.

In its proposal, AusNet used CIE's forecast number of residential net disconnections as its forecast number of residential abolishments.[54] However, AusNet also stated that its network currently accommodates around 15,000 long term zero consuming customers (zero gas consumption over a period of greater than 12 months), which is around 2% of its customer base. It noted that this percentage is growing. It also noted that in the last year zero

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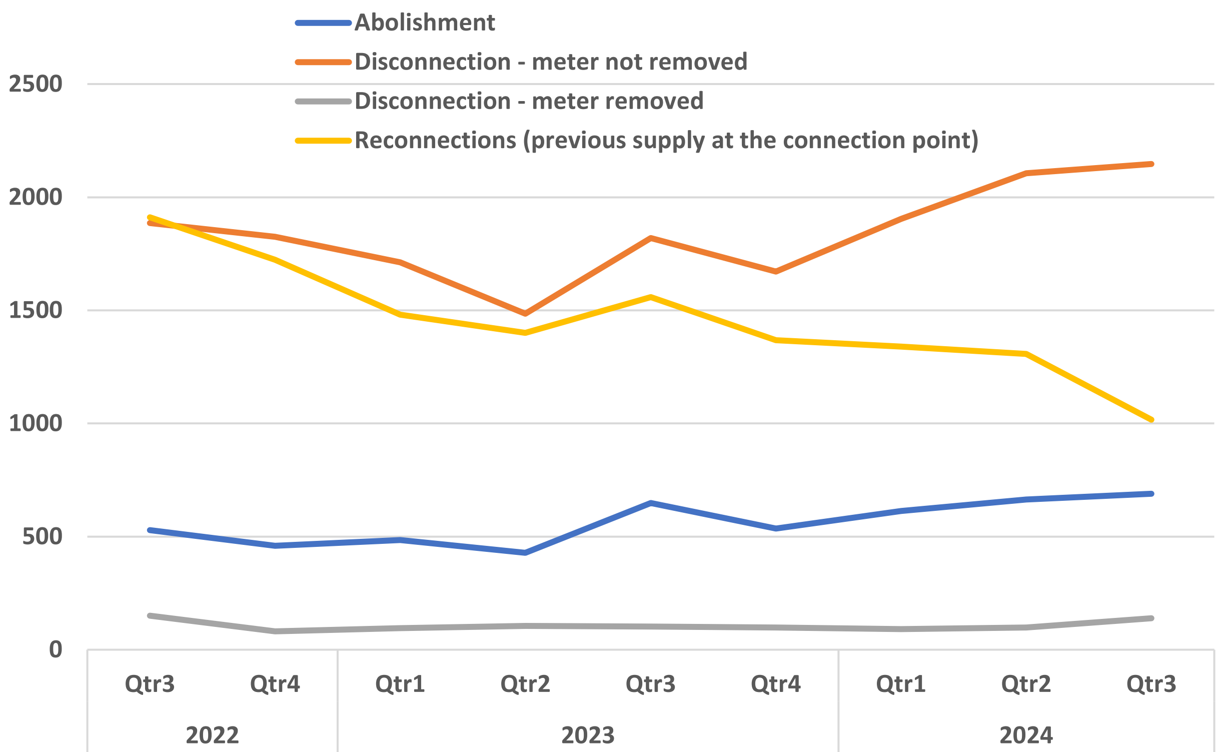
[53] CIE, *GAAR 2024–28 – Appendix 1 – CIE Demand Forecast Update*, 2 July 2024, pp. 46–48.

[54] AusNet, *Response to information request #IR001*, 15 November 2024, p. 2.

consuming customers have grown by around 20%, and that it is 'highly probable that this shift is indicative of a broader trend of customers using disconnections as a means of functionally abolishing'.[55] CIE also notes in its report that the number of dormant meters (dormant for at least 3 months) has increased by 35% since June 2022.[56] This indicates that many customers that are no longer consuming gas are choosing to retain their gas connection and are requesting a disconnection rather than an abolishment.

This is supported by disconnection data showing that the number of disconnections is rising while the number of reconnections is falling, indicating that many customers who are disconnecting are not reconnecting (see Figure 3).

Figure 3 Disconnection, reconnection and abolishments,



Source: AER, *Gas quarterly disconnection reporting*, 29 October 2024.

AusNet, however, stated that CIE developed its revised net disconnection forecast using a bottom-up assessment and, as such, it did not need to apply an adjustment to the revised net disconnection forecast to forecast abolishments.[57]

However, CIE's net disconnection forecast does not distinguish customers 'functionally abolishing' via a disconnection from those requesting an abolishment. That is, CIE did not separately forecast the number of disconnections, abolishments and reconnections. It only forecast the net figure. Historically, the number of abolishments has roughly equalled the number of net disconnections and the number of reconnections has followed the number of disconnections. However, we now see a trend of decreasing reconnections and rising

55 AusNet, *Gas Access Arrangement Variation – 2024–28*, pp. 55–56.

56 CIE, *GAAR 2024–28 – Appendix 1 – CIE Demand Forecast Update*, 2 July 2024, p. 26.

57 AusNet, *Response to information request #IR001*, 15 November 2024, p. 2.

disconnections. This is consistent with some customers permanently leaving the network by requesting a disconnection. AusNet's proposal that the forecast number of abolishments should equal the forecast number of net disconnections is inconsistent with the trend we see in disconnections, reconnections and abolishments.

In our 2023 final decision, we estimated that 74% of net disconnections will be abolishments. If we apply this to AusNet's updated net disconnections forecast, the forecast number of abolishments is similar to the forecast in our 2023 final decision (1,420 abolishments higher over the 2023–28 period).

We have also looked at how accurate the forecast number of abolishments in our draft decision has been to date. The connection data AusNet reports to us shows that AusNet undertook 2,461 abolishments in 2023–24, which is two abolishments less than the 2,463 abolishments which we forecast for 2023–24 in our 2023 final decision. We are satisfied that the forecasts we approved in the 2023 final decision have been accurate to date.

Further, as discussed in section 2.4, we engaged Oakley Greenwood to review AusNet's connections forecast. Having considered Oakley Greenwood's analysis, we consider AusNet's proposed decline in customer numbers is not warranted. Making the adjustment recommended by Oakley Greenwood, which we consider is accurate, our new forecast number of customers is not materially different to the forecast in our 2023 final decision.

Having regard to the above, we consider that the forecast abolishment costs in AusNet's proposal was not arrived at on a reasonable basis and does not satisfy the forecasts and estimates criteria. We consider the abolishments forecast in the 2023 final decision remains the best forecast possible in the circumstances.

Finally, we note that abolishment costs are subject to a true-up for the actual number of abolishments via the tariff variation mechanism. AusNet will recover costs for the actual number of abolishment services it provides through this mechanism.

Output growth

We do not consider AusNet's proposed variations to forecast output growth to be material or meet the requirements for forecasts and estimates.[58] As set out below, we consider output growth has already been appropriately accounted for in our 2023 final decision forecast for the 2023–28 access arrangement period.

AusNet lowered its forecast of output growth to reflect the lower forecasts of energy throughput and customer numbers that it submitted with its proposal due to 'shifts in the regulatory and policy environment'. It stated that these changes are based on the revised demand and customer number forecasts provided by its consultant, CIE.[59]

This reduced its opex forecast by $1.9 million.

58 NGR, r. 74.

59 AusNet Services Gas, *Gas Access Arrangement Variation – 2024–28*, p. 25.

We have reviewed the proposed amendments to forecast output growth and have identified several issues with AusNet's proposal. Addressing these would increase the forecast rate of change relative to AusNet's proposal.

We consider that this proposed variation does not meet the requirements for forecasts and estimates because:

- AusNet did not update its forecasts of customer numbers and throughput for 2023–24 and 2024–25 on the basis that it was not proposing a change in forecast opex for these years. Consequently, it only updated its forecasts for 2025–26 to 2027–28. However, given the cumulative impact of the rate of change, we consider it necessary to update the forecasts for 2023–24 and 2024–25 to get the best forecasts of the remaining years in the period.
- As discussed in section 2.4, having considered Oakley Greenwood's analysis, we consider that AusNet's proposed decline in customer numbers is not warranted.
- AusNet applied the updated forecast growth rate for energy throughput for residential and commercial customers for 2025–26 to 2027–28 to the existing forecast of total throughput for 2024–25. Total throughput includes residential and commercial customers as well as industrial customers. AusNet stated that its proposed changes to forecast output growth were based on the revised demand and customer number forecasts provided by CIE.[60] However, CIE did not provide forecasts of industrial throughput (only maximum hourly quantities). Furthermore, the policy changes that CIE sought to model primarily impact residential customers and are not aimed at industrial customers. We consider that applying the revised forecast change in residential and commercial throughput overstates the impact of the policy change on total throughput.
- AusNet did not revise its forecast of productivity growth. The productivity growth forecast we applied in the 2023 final decision included returns to scale. Consequently, any downward revision to output growth should reduce productivity growth due to lower returns to scale. The net impact of this is that any reduction in output growth should be partially offset by a reduction in productivity growth.

Given these concerns, we consider that AusNet's revised forecast rate of change was not arrived at on a reasonable basis and does not satisfy the requirements for forecasts and estimates.[61] We consider that the 2023 final decision forecast rate of change remains the best forecast possible in the circumstances.

4.5 Revisions

Table 8 sets out the nature of the amendments in relation to opex that are required to make the proposal acceptable to the AER.[62]

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60 AusNet Services Gas, *Gas Access Arrangement Variation – 2024–28*, p. 25.

61 NGR, r. 74.

62 NGR r.59(2).

Table 8 Revisions - opex

Revision	Amendment
Revision 4.1	Provide additional information or further amendments to address the matters set out above in respect of the proposed opex. Alternatively, Ausnet may wish to consider whether the 2023 final decision on opex remains appropriate and submit an amendment on that basis. Any further information or amendments must be provided in accordance with, and subject to the limitations set out in, NGR Rule 60.

5 Accelerated depreciation due to stranded asset risk

This section sets out our draft decision on AusNet's proposed additional $70 million accelerated depreciation for the 2023–28 access arrangement period.

Accelerated depreciation is a regulatory tool we use to reduce asset stranding risk arising from demand uncertainty in the gas sector. While accelerated depreciation leads to higher revenues over an access arrangement period, it can help reduce asset stranding risk to some extent by reducing the residual capital base to be recovered from a smaller customer base in the long term.

5.1 AER draft decision

Our draft decision is to not accept AusNet's proposed $175 million ($2022–23) accelerated depreciation for the 2023–28 access arrangement period, which reflects a $70 million increase to the $105 million we approved in our 2023 final decision. For the reasons outlined in section 5.4, we consider that the $105 million in accelerated depreciation which was approved in our 2023 final decision remains appropriate.

5.2 AusNet's proposal

In our 2023 final decision, we approved $105 million accelerated depreciation for the 2023–28 access arrangement period for reducing stranded asset risk associated with long term demand uncertainty. The $105 million was determined based on a 1.5% per annum 'base' annual real price path constraint.[63]

AusNet has proposed increasing the amount of accelerated depreciation to $175 million for the 2023–28 access arrangement period. The proposed increase in accelerated depreciation would result in a higher 'base' annual real price increase of 8.0% per annum over the remaining 3 years of the 2023–28 period compared to the 1.5% limit set at the 2023 final decision.[64]

AusNet submitted that the proposed increase is due to material policy changes introduced by the Victorian Government (as discussed in section1.1) which leads to an increased risk of asset stranding. It stated that from these changes, the outlook for gas is impacted and the path to electrification has been strengthened.

5.3 Stakeholder views

We received 13 submissions that referenced AusNet's accelerated depreciation proposal from AGL, IEEFA, Environment Victoria, Origin Energy (Origin), ECA, Brickworks, ENA, EUAA, Lighter Footprints, Darebin Climate Action Now (DCAN), VCOSS and the Victorian

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[63] This 1.5% p.a. was excluding incentive scheme revenue adjustments. These adjustments added a further 0.9% p.a. to AusNet's real price path.

[64] "Base" real price changes exclude the price effect of incentive scheme revenues. Incorporating incentive scheme revenues will give different annual price impacts. For example, in the executive summary of this draft decision paper we refer to annual price impacts incorporating incentive scheme revenues.

Minister for Energy and Resources. The majority of these stakeholders did not support the proposed increase in accelerated depreciation.

The Victorian Minister for Energy and Resources submitted that AusNet has not justified the $70 million increase in accelerated depreciation (to $175 million), given its proposed forecasts for residential demand and customer numbers do not demonstrate a material decline. [65]

IEEFA submitted that Victoria's recent policy developments are not unexpected. It stated the nature and timing of policy implementation is always uncertain but the fact that specific policies have been legislated or proposed since the AER's 2023 final decision does not automatically reflect an unforeseen change in AusNet's circumstances. [66]

IEEFA, VCOSS and the Victorian Minister for Energy and Resources submitted that an access arrangement variation proposal is not the most efficient way to address the issues of declining demand. They are concerned that the outcome of AusNet's proposal will potentially influence other gas networks to seek similar variations, leading to a piecemeal response to the issues. [67]

AGL described the access arrangement variation proposal process in general, as unsustainable and submitted that further consideration of AusNet's accelerated depreciation should be deferred until the next access arrangement period. [68] Environment Victoria submitted that reopening access arrangements to reflect changes in outlook was not in the interests of consumers. [69]

ECA, DCAN and Lighter Footprints consider that any increase in accelerated depreciation must not be accepted unless AusNet has minimised its costs across all sections of its proposal to reflect the long-term decline in demand. [70]

IEEFA, Environment Victoria, VCOSS and the Victorian Minister for Energy and Resources consider that under the price cap mechanism the gas networks have been provided with adequate opportunity to recover more than their efficient costs due to actual demand being consistently higher than the forecast levels. [71]

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65 The Victorian Minister for Energy and Resources, *Victorian Government Submission to AER on AusNet GAAR variation proposal,* December 2024, p. 3.

66 IEEFA, *Submission on AusNet's variation proposal*, November 2024, pp. 1–3.

67 IEEFA, *Submission on AusNet's variation proposal*, November 2024, p. 1; VCOSS, Submission on AusNet's variation proposal, November 2024, pp. 1 and 3; The Victorian Minister for Energy and Resources, *Victorian Government Submission to AER on AusNet GAAR variation proposal,* December 2024, pp. 1–2.

68 AGL, *Submission on AusNet's variation proposal,* November 2024, pp. 1–2.

69 Environment Victoria, *Submission on AusNet's variation proposal,* November 2024, p. 3.

70 ECA, *Submission on AusNet's variation proposal*, November 2024, pp. 3–4; DCAN, *Submission on AusNet's variation proposal,* November 2024, p. 1; Lighter Footprints, *Submission on AusNet's variation proposal,* November 2024, p. 2.

71 IEEFA, *Submission on AusNet's variation proposal, November 2024*, p. 4; Environment Victoria, *Submission on AusNet's variation proposal,* November 2024, p. 2; VCOSS *Submission on AusNet's variation proposal,* November 2024, pp.1–3; The Victorian Minister for Energy and Resources, *Submission on AusNet's variation proposal*, November 2024, pp. 1–2.

AGL and Origin submitted that affordability and price stability remained important for households while DCAN and VCOSS stated the importance of protecting vulnerable customers during this energy transition.[72]

AGL noted that the rate of electrification and the extent of its impact on customer numbers and asset stranding is still uncertain. It submitted that the significant level of uncertainty in the government policies cited in AusNet's proposal meant that further consideration of accelerated depreciation in AusNet's gas network should be deferred to the next regulatory period (commencing in 2028).[73]

ECA and VCOSS submitted there should be a broader policy framework in place to protect consumers and gas networks should develop a robust long term asset management plan to deal with the decline in demand.[74]

Submissions from industrial stakeholders broadly supported AusNet's case for an increased accelerated depreciation:

- Brickworks and ENA submitted that the operating environment has materially changed since our 2023 final decision and AusNet's stranding risk has increased due to the push for electrification.[75]
- Brickworks highlighted the social inequity of industrial customers remaining on the network as more residential and commercial customers disconnect.[76]
- EUAA stated the importance of the 'regulatory contract' which affords a network a reasonable rate of return and opportunity to recover costs.[77]

5.4 Reasons for draft decision

We acknowledge that Victorian Government policies on gas substitution have evolved since the 2023 final decision. However, we consider AusNet has not justified the proposed additional accelerated depreciation based on either short-term or long-term impacts arising from the policy changes that AusNet referenced in its proposal.

At the time of our 2023 final decision, the case for accelerated depreciation was considered in the context of demand uncertainty. The Victorian Gas Substitution Roadmap indicated that the Victorian Government is committed to the net zero emissions target by 2050. We recognised that this would mean a limited role for natural gas beyond this date. The decline in gas demand was evidenced by the 2023 Gas Statement of Opportunities (GSOO) which

[72] AGL, *Submission on AusNet's variation proposal,* November 2024, pp. 1–2. Origin, *Submission on AusNet's variation proposal,* November 2024, p. 1; DCAN, *Submission on AusNet's variation proposal*, November 2024, p. 1; VCOSS, *Submission on AusNet's variation proposal Submission on AusNet's variation proposal*, November 2024, pp. 3–4.

[73] AGL, *Submission on AusNet's variation proposal,* November 2024, p. 1.

[74] ECA, *Submission on AusNet's variation proposal*, November 2024, p. 3; VCOSS, *Submission on AusNet's variation proposal,* November 2024, p. 4.

[75] Brickworks, *Submission on AusNet's variation proposal, November 2024*, p. 1; ENA, *Submission on AusNet's variation proposal,* November 2024, p. 1.

[76] Brickworks, *Submission on AusNet's variation proposal*, November 2024, p. 1.

[77] EUAA, *Submission on AusNet's variation proposal*, November 2024, p. 1.

showed a material decline in gas consumption over the long term. The future role for hydrogen and other renewable gases was also uncertain at the time.[78]

After publication of the 2023 final decision, the Victorian Government announced several key reforms of the Gas Substitution Roadmap.[79] While these policy reforms target rapid electrification for homes and businesses, their speed of adoption by customers and their overall impact in reducing gas demand remain uncertain at the present time. We agree with the views expressed by stakeholders that Victoria's policy developments since the 2023 final decision do not automatically reflect an unforeseen change in AusNet's circumstances.

AusNet submitted that its proposed increase to accelerated depreciation is due to increased stranding risk as a result of material policy changes introduced by the Victorian Government since the 2023 final decision.[80] However, we consider AusNet has not demonstrated that demand outlook has been materially affected by its referenced policy developments since the 2023 final decision (as discussed in section 1.1).

As set out in section 2.1, AusNet is forecasting a reduction of 3.5% in the residential customer numbers by the end of the 2023–28 access arrangement period, relative to forecasts for the 2023 final decision.[81] However, it proposed a demand consumption volume largely consistent with that of the 2023 final decision for the remaining 3 years of the 2023–28 period. We consider the customer numbers and consumption remain largely consistent with our forecasts at the time of our 2023 final decision. As such, we do not consider forecast demand has significantly changed in the short-term since the 2023 final decision, such to warrant a variation.

We do not consider that there is sufficient evidence to support AusNet's assertion that long term gas demand will decline materially faster than the forecasts at the time of the 2023 final decision. For residential and commercial customers in Victoria, the 2024 GSOO shows a similar level of gas consumption in the short to medium term relative to the 2023 GSOO, but a slightly steeper decline from around 2034 onwards (Figure 4).[82] The 2024 GSOO shows a 71% decline by 2042 relative to current levels, while in the 2023 GSOO the decline by 2042 is 63%.

In contrast, for industrial customers, the 2024 GSOO shows a stable demand trajectory over the long-term and a moderate increase relative to the 2023 GSOO. As such, total demand volumes (for residential, commercial and industrial customers combined) do not differ materially between the 2024 GSOO and the 2023 GSOO (Figure 5).

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78 AER, *Final decision – AusNet gas services, Access arrangement 2023–28, Attachment 4*, Regulatory depreciation, June 2023, pp. 7–8.

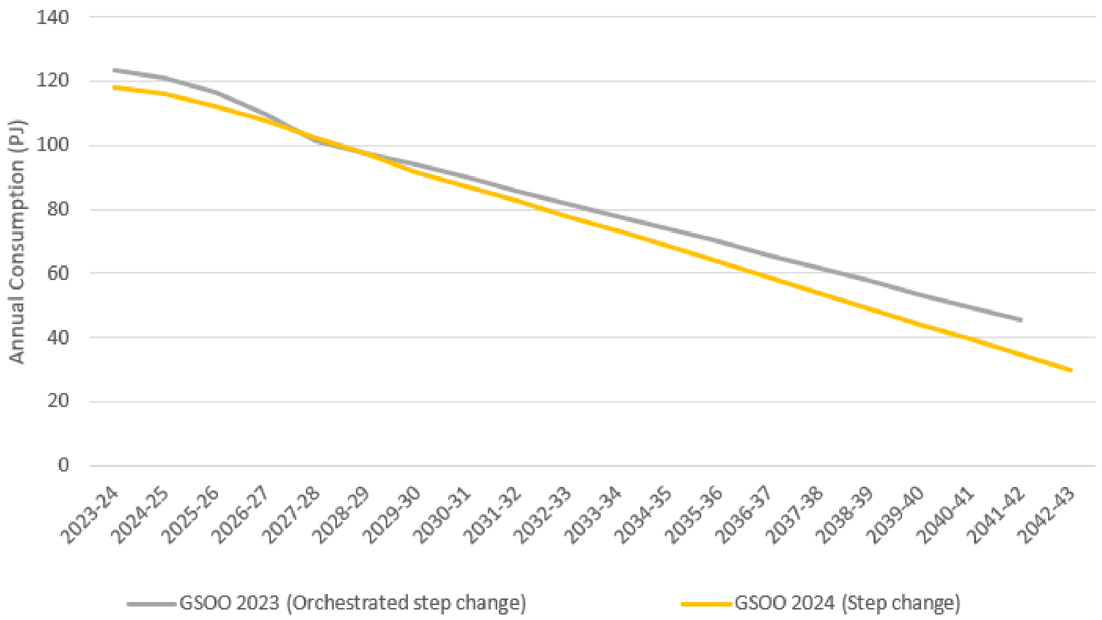
79 Victoria State Government, Gas Substitution Roadmap Update, December 2023, pp. 2–7.

80 AusNet Services Gas, *Gas Access Arrangement Variation – 2024–28*, pp. 2, 7–10.

81 Relative to the 2023 final decision, AusNet forecasts a 1.4% reduction in 2025–26, a 2.3% reduction in 2026–27 and a 3.5% reduction in 2027–28.

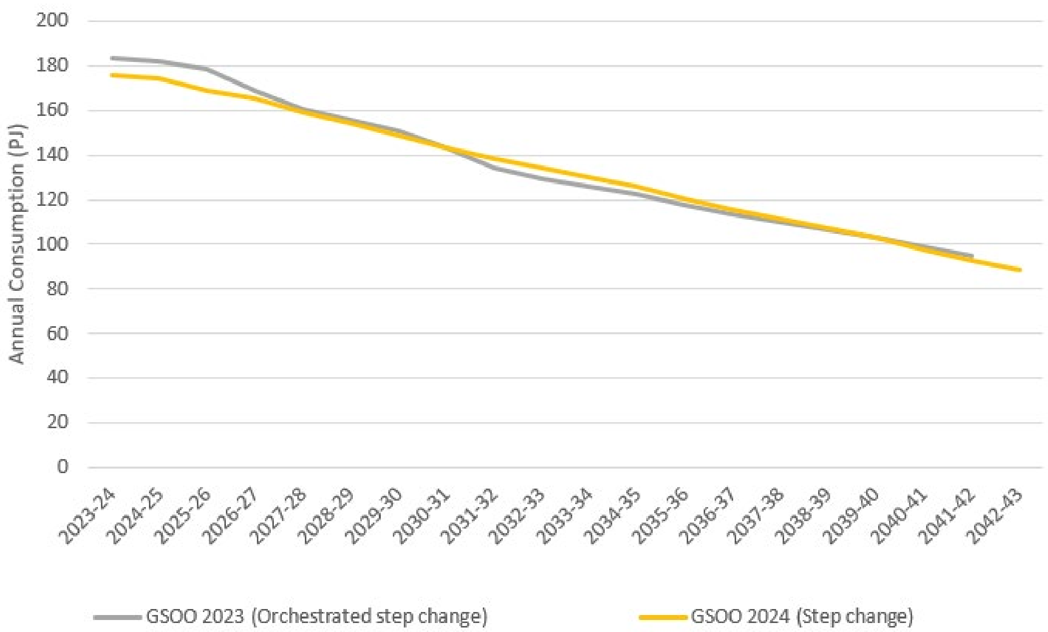
82 For this comparison we have used the most likely scenarios for each version of the GSOO. In GSOO 2023 this is 'Orchestrated Step Change' and for GSOO 2024 this is 'Step Change'.

Figure 4 Residential and commercial gas throughput outlook – AEMO GSOO for Victoria



Source: AER analysis, AEMO 2023 GSOO version 21 April 2023 and AEMO 2024 GSOO version 21 March 2024 (available https://aemo.com.au/energy-systems/gas/gas-forecasting-and-planning/gas-forecasting-data-portal).
Note: Excluding industrial customers. The GSOO series shown reflect the most likely scenario.

Figure 5 Total gas throughput outlook for residential, commercial and industrial customers – AEMO GSOO for Victoria



Source: AER analysis; AEMO, 2023 GSOO version 21, April 2023; AEMO, 2024 GSOO version 21, March 2024; Available at https://aemo.com.au/energy-systems/gas/gas-forecasting-and-planning/gas-forecasting-data-portal.
Note: The GSOO series reflect the most likely scenario.

Price stability and affordability

AusNet's proposed variation, if accepted, would result in an increase in network prices by nearly 9% per annum in real terms over the remaining 3 years of the 2023–28 access arrangement period. After accounting for inflation, network prices would be forecast to increase by about 12% per annum. We consider this level of price increase to be significant. As shown in Figure 1, most of this increase is due to the proposed higher accelerated depreciation.

While accelerated depreciation can be used to reduce stranded asset risk to some degree, it must be carefully considered. The level of accelerated depreciation should reflect the specific circumstances of the regulated business, and more importantly, the scale of price adjustments should be reasonably made without creating price shocks.[83] One of the key issues raised by stakeholders on the topic of accelerated depreciation is the need to provide price affordability and stability to protect vulnerable customers.[84]

Consistent with our Information paper on Regulating gas pipelines under uncertainty, we consider that adopting a policy of accelerating depreciation without some predefined limits could result in large and repeated increases in future gas prices.[85] As demand declines, network prices and customer bills are expected to rise over time as more customers leave the network. Further increases in accelerated depreciation in this environment could exacerbate upward pressure on prices, potentially triggering an unintended disconnection spiral. This outcome would not align with the long-term interests of customers.

While accelerated depreciation can help reduce asset stranding risk, it has limitations and on its own cannot resolve the issues faced by the gas networks and customers from a declining network. We agree with stakeholder submissions that addressing the broader issues in the gas sector requires a more holistic approach. As such, accelerated depreciation does not remove the need to resolve the broader policy question involving consumers, network businesses and governments regarding who should pay for the costs of stranding risk associated with past capital investments, or when and how this will occur.

We acknowledge that industrial customer stakeholders are concerned with the social equity of industrial customers in hard-to-abate sectors remaining on the network as more residential and commercial customers disconnect. We consider that any holistic long-term plan will need to consider the price impacts on different customer groups.

On balance, we do not consider that adopting additional accelerated depreciation is appropriate in the circumstances.

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83 AER, *Regulating gas pipelines under uncertainty – Information paper*, November 2021, p. 29.

84 DCAN, *Submission to AusNet Services Access Arrangement 2023-28 Variation proposal*, November 2024, p. 1; VCOSS, *Submission to AusNet Services Access Arrangement 2023-28 Variation proposal*, November 2024, pp. 3–4.

85 AER, *Regulating gas pipelines under uncertainty – Information paper*, November 2021, p. 32.

5.5 Revisions

Table 9 sets out the nature of the amendments in relation to accelerated depreciation that are required to make the proposal acceptable to the AER.[86]

Table 9 Revisions – accelerated depreciation

Revision	Amendment
Revision 5.1	Provide additional information or further amendments to address the matters set out above in respect of the proposed accelerated depreciation. Alternatively, AusNet may wish to consider whether the 2023 final decision on accelerated depreciation remains appropriate and submit an amendment on that basis. Any further information or amendments must be provided in accordance with, and subject to the limitations set out in, NGR Rule 60.

86 NGR r.59(2).

Glossary

Term	Definition
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
AusNet	AusNet Gas Services
capex	capital expenditure
CIE	Centre for International Economics
ECA	Energy Consumers Australia
ENA	Energy Networks Association
ESCV	Essential Services Commission of Victoria
ESV	Energy Safe Victoria
EUAA	Energy Users Association of Australia
GSOO	Gas Statement of Opportunities
IEEFA	Institute of Energy Economics and Financial Analysis
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
NPV	net present value
opex	operating expenditure
PTRM	post-tax revenue model
RIN	regulatory information notice
RIS	regulatory impact statement
TJ	terajoule