14 February 2025

Dr Kris Funston
Executive General Manager – Network Regulation
Australian Energy Regulator

Submitted via email

Dear Dr Funston,

AER Draft Decision: Jemena Gas Networks Access Arrangement 2025-30

Energy Networks Australia (ENA) appreciates the opportunity to respond to the Australian Energy Regulator's (AER) Draft Decision on Jemena Gas Networks' proposed Access Arrangement revisions.

ENA is the national industry body representing Australia's electricity transmission and distribution and gas distribution networks. Our members provide more than 16 million electricity and gas connections to almost every home and business across Australia.

ENA supports the AER's focus in the review on a sustainable medium-term set of pricing and network services arrangements supporting the needs of all gas customers through the ongoing energy transition.

Assessment of renewable gas connections

Jemena has proposed approximately $80 million of capital expenditure to facilitate the connection of new renewable gas sources to its existing network, to assist in the decarbonisation of its network over time. From engagement undertaken, we understand Jemena's customers have supported investments toward this objective through time.

ENA supported recent National Gas Law (NGL) and Rule amendments which were designed to allow energy market institutions, including the AER, to better recognise emissions reduction commitments and promote regulatory outcomes which were consistent with public emissions reductions goals.

As the AER has observed, its decisions in these areas represent the first time that key rule revisions to support regulatory recognition of these goals have been applied.

ENA recognises that the AER has requested more information to assist it in making its determinations on rule 79 relating to conforming capital expenditure, and, potentially, relating to the separate speculative capital investment provisions.

In several areas, however, the AER's stated reasons for declining to approve the forecast do not appear to provide a clear set of guidance for Jemena, or any other gas network businesses operating under the Gas Rules, seeking to understand the basis of the approach taken.

In particular, the AER states:

> *We outline our considerations below:*
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> *• The business cases do not consider a counterfactual scenario where the feedstock (i.e. the biogas from decomposing organic material, that can be processed and converted to natural gas) can be used as an input for alternative emissions reductions methods. In particular, the feedstock can, and is, used for electricity generation, which would also contribute to emissions reduction. We consider JGN should provide cost benefit analysis of this counterfactual scenario to determine whether the biomethane production is the most efficient use of the feedstock.*[1]

The reasoning would appear to be that to have the capital expenditure considered, as supported by the new emissions reduction limb of the capital expenditure criteria, Jemena Gas Networks is required to discharge an exceedingly high evidentiary bar.

That is, Jemena is required to consider a range of counterfactual scenarios in which an intermediate product is used in an entirely different manner than how the network proposes, and the relative emissions implications of these scenarios. It then appears to require a cost benefit analysis to determine that the specific network proposed use of intermediate good is the 'most efficient' use of the feedstock, from amongst the alternatives.

ENA appreciates that any proposed network expenditure must be tested for prudency and efficiency, delivering efficient costs across current and future consumers. The additional tests suggested above, however, appears to step beyond this principle, and risk introducing a lack of predictability or clarity into how emissions reduction related expenditures may be assessed.

For example, it is unclear from the decision how this analysis should be bounded or conducted. The scope of the application of this approach across the range of intermediate inputs used to deliver network services is also unclear. By way of analogy, for example, if a network proposed to incur costs to equip a previously petrol fuelled vehicle fleet with electric vehicles, to support the delivery of network services, and recognise the emissions reductions of this step as part of its proposal, it is unclear whether a network be required to conduct an analysis of alternative use cases for the electric vehicles, and their likely emissions profile in different deployments.

ENA assumes this is not the intended outcome, yet on its face, these additional evidentiary requirements would appear to risk counteracting the intended policy outcome of the amendments of the NGL and Rules leading to regulatory decisions better able to integrate and promote actions consistent with national and State-based emissions reduction goals.

Better understanding of the principles the AER is considering applying in this area will assist policy makers, networks and their consumers to have aligned expectations around the practical operation of the changes agreed by Energy Ministers. This would also allow networks to bring forward appropriately evidenced expenditure proposals relating to emissions reductions, and all parties to consider any need for further Rules-based guidance in this area.

Proposed emissions measurement expenditure – Picarro technology

A further example of the need for a clear and consistent approach to the implementation of emissions reductions related expenditure proposal is the initial decision to reject a proposed step change for the expanded deployment of leakage monitoring vehicles.

Jemena's proposal highlights that the expansion of this program is strongly net present value positive, consistent with good industry practice internationally, and actively supported by 70 per cent of customer forum participants engaged on the proposal in forums.[2] Globally, utilities such as PG&E and

[1] AER (2024) Draft Decision – Attachment 5, p.26
[2] Jemena Attachment 6.2, Section 4.1, p.16-19

Italgas have trialled and adopted Picarro's monitoring systems, to assist in the emissions reporting, emissions reduction and to improve safety.

AER indicates that it does not regard the proposed expansion of the program of use to be efficient, due to an assessment that Jemena may not face regulatory requirements beyond surveys with 3 to 5 year cycles, consistent with labour-intensive walking surveys of Jemena's 26,000 km network.

The adoption of innovative technologies, which provide net present value benefits, and assist in emissions reductions targets - as well as lifting the emissions measuring and management capabilities of gas networks - is precisely the type of outcome that would be expected to be actively facilitated by amendments to the NGL and Gas Rules that were specifically design to allow for better recognition of emissions reduction policies and targets in AER economic regulatory determinations.

The wide use of comparable technologies and innovations by comparable businesses overseas, and the clear support for its proposed investments from Jemena customer forums, provide a strong basis for the AER to review its approach in this area.

Adjusting depreciation for potential changes to economic lives of network assets

ENA supports the proposal to recognise future demand uncertainty through adjustments to depreciation. These adjustments, as recognised by the AER in its Information Paper - Regulating gas pipelines under uncertainty[3], provide a flexible, symmetrical and NPV neutral tool to recognise potential changes in demand for gas network services.

The recognition of this uncertainty and use of this tool are consistent with the obligations on the AER to provide for a reasonable opportunity for recovery of efficiently incurred costs and provide critical forward-looking signals impacting the future cost of financing all new and ongoing network investment.

The AER, as well as Jemena in its engagement with its consumer stakeholders, rightly consider the need to manage any price shocks and consider the ongoing affordability in reaching any agreed depreciation allowance outcomes. The AER is proposing to place a '0% real price increase' ceiling on any proposals to adjust depreciation allowances to recognise evolving market information and demand risks, observing:

> *While we have targeted a 0% per annum 'base' real price increase limit for this draft decision, we note there may be scope to choose a different target 'base' real price path for consideration in the final decision. However, sufficient supporting evidence and adequate further customer consultation on the short-term price impacts of accelerated depreciation addressing affordability concerns will be needed to justify a higher 'base' real price increase limit. We acknowledge that economic conditions will evolve further before the final decision, and this will impact the values of the WACC and expected inflation.*[4]

ENA considers that the adoption of a regulator imposed real price constraint needs to be carefully considered alongside its potentially perverse impacts.

We note detailed evidence provided by Jemena that its proposed depreciation profile better meets the Gas Rules and Law requirements, including by providing greater pricing stability through time than the AER's proposed approach, or the straight-line depreciation approach used historically in conditions of steadily expanding demand.[5]

Where regulatory judgement and the exercise of discretion has been applied to impose an AER selected ceiling, there is an obligation on the AER to fully explain why the approach, and the individual

[3] AER (2021) Regulating gas pipelines under uncertainty - Information paper
[4] AER (2024) AER (2024) Draft Decision – Attachment 4, p.20
[5] HoustonKemp *Smoothing cost recovery when gas demand is declining: A report for Jemena Gas Networks*, 10 January 2025, p.19-30

selected ceiling, is consistent with the framework and promotes the long-term interests of current and future gas consumers.

As the AER highlights, depreciation approaches proposed by a network service provider must be supported by evidence and should reflect consumer consultation. Separately, however, any substituted AER determination on this matter must itself evidence why the selected approach and ceiling (including the setting of a 'zero change' ceiling) best promotes the NGO compared to other alternative values, taking into account the relevant revenue and pricing principles and applicable Gas Rules.

A particular feature of the AER's chosen approach, as recognised in the extract above, is that the real price constraint on depreciation adjustments is impacted by a range of historical and external factors, market and price level movements, and inflation forecasts. In turn, the impact of these factors also then interacts with changes in these values and forecasts since the time of the last determination, as well as the level and nature of incentive scheme payments.

The result of this is the level of adjustments are effectively bounded by a set of constraints which appear to bear no logical relationship to the specific decision about the optimal level of adjustments to depreciation profiles that the AER should allow.

ENA recognises the complexity, and countervailing factors which the AER is required to balance in reaching this specific determination.

While the draft decision discusses these issues, prior to coming to its proposed real price limit, what is not clear is how the AER has affirmatively satisfied itself that its selected value best satisfies the NGO and relevant principles in the National Gas Rules, and how it considers the impacts discussed above should systematically constrain the final selected real price constraint.

In circumstances where it is widely acknowledged that Jemena's network will be experiencing declining gas demand, and this demand will be significantly lower in 2050, it is important that sufficient and prudent action is taken.

In the absence of a clear capacity to have revised Access Arrangements address this within the five year price control periods, there are only a limited number of opportunities to take meaningful steps to support a smoother transition for customers and effectively manage stranding risk. The AER's final decision represents one such critical opportunity.

If you wish to discuss any of the matters raised in this letter further, please contact Garth Crawford, General Manager, Economic Regulation [redacted]

Yours sincerely,

[redacted]

Garth Crawford

General Manager, Economic Regulation