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Sent by email: AERgasreform@aer.gov.au

Dear Arek

AER Pipeline Information Disclosure Guidelines issue paper

Thank you for the opportunity to provide feedback on the AER's Pipeline Information Disclosure (**PID**) Guidelines issues paper.

We are responding to the PID guideline issues paper in our capacity as an owner of a scheme pipeline (Jemena Gas Networks) and of multiple non-scheme gas transmission pipeline assets throughout eastern and northern Australia.

The PID guidelines (**Guideline**) should support Part 10 of the National Gas Rules (**NGR**) to improve information transparency of gas pipeline service providers. Broadly, we are supportive of a number of the directions that the AER proposes for its draft Guideline, however, note that until we see the draft Guideline it is difficult for us in some cases to respond to the AER with certainty about our ability to provide information, or whether the information sought is consistent with Part 10 of the NGR.

We have provided detailed feedback on a number of areas of the issues paper in the attachment to this letter. Broadly, we highlight that:

- Scheme pipelines should not be made to duplicate information that is provided through the existing regulatory framework (including the access arrangement review process) to avoid unnecessary data gathering and review costs, and potentially inconsistent or redundant information for users.
- We support the AER's approach of adopting the reporting obligations under the AER's Non-scheme Pipeline Financial Reporting Guidelines and the Non-scheme Pipeline Information Disclosure Compliance Bulletin (September 2022), and modifying where necessary for new NGR requirements. We consider that this is the most efficient approach as we already have systems and processes in place to support the data capture necessary to comply with these requirements.
- Given fundamental differences in how the book value of assets and the recovered capital method (RCM) are determined, it is not clear how a reconciliation between book value of assets and RCM would be undertaken beyond simply showing the book value on one side, the RCM value on the other, with the difference explained at a high level (i.e. goodwill included in book value but not RCM). We question the usefulness of this approach for users, and we are also concerned at the potential effort required.
- We have concerns about the AER's proposal for service providers to publish forecast financial information for planned pipeline capacity expansions and extensions. We note that the new Part 11 access negotiation framework in the NGR appropriately provides prospective users with significant protections including the ability to access this information in accordance with the information standard.

- The inclusion of decommissioning costs in the RCM is consistent with service providers having a reasonable opportunity to recover at least their efficient costs as stipulated by the National Gas Law (**NGL**) revenue and pricing principles for scheme pipelines and the NGR pricing principles for non-scheme pipelines. Therefore, we agree with the continued ability for service providers to include decommissioning costs in a pipeline's RCM values.

Should you have any questions please do not hesitate to contact James Harding, Gas Networks Regulation Manager, at [redacted]

Yours sincerely

[redacted]

Ana Dijanosic

General Manager Regulation

Attachment: Feedback on PID guidelines issues paper

Section 3.3 Financial Statements

We will consider this area further once we have visibility of the requirements in the draft Guideline.

Section 3.3.1 Guidance on methods, principles, and inputs

With regards to the non-scheme pipeline financial reporting template, the AER notes the potential duplication of information requirements for scheme pipelines, such as the existing requirement to report depreciation information under the access arrangement process through the stringent annual reporting requirements under the Regulatory Information Notices (**RINs**). We believe that scheme pipelines should not be made to duplicate the reporting of information that is provided through the existing regulatory framework (including through the AER's access arrangement review process) to avoid unnecessary data gathering and review costs, and potentially inconsistent or redundant information for users.

With regards to asset lives, we consider that if the Guideline continues to set out standard lives, it should also continue to allow service providers to report based on alternative asset lives provided that they disclose these alternative lives and explain why it is more appropriate to adopt an alternative to the Guideline's standard lives.

Section 3.3.2 Reconciliation of financial and asset valuation information

We consider that reconciliation of book value of assets versus the recovered capital method (RCM) is not overly meaningful, and may take considerable effort.

Book value is an accounting concept whereas the RCM is an economic concept. The key difference between the two methods is:

1. The book value asset valuation calculates depreciated book value plus or minus any additions or disposals. Depreciation is calculated based on an accounting perspective of asset lives which reflects the expected utility of the assets to the entity. Also, the book value will reflect the impact of any revaluations (e.g. to market value) and may include acquisition goodwill or write downs, which are unlikely to be reflected in the mechanics of the RCM given its focus on historical cash flows.
2. The RCM asset valuation calculates the depreciated cost of constructing the pipeline, with the depreciation component reflecting the return of capital generated since the pipeline was constructed (i.e. revenue less operating expenditure less the return on capital less net tax liabilities). RCM determines the residual value of the asset by showing the capital that has been recovered from users since the pipeline was constructed. For completeness, we also note that a pipeline's revenue (and therefore return on capital) may be subject to considerable variability in a workably competitive market over the life of an asset—in contrast to the depreciation applied to a book value, return on capital may not necessarily occur linearly over an asset's life.

Given that the accounting useful life of each asset is based on the estimated expected utility to the entity, the accounting value does not necessarily align with the economic cost recovery for the asset. For example, if the asset management policy of the entity involves disposal of assets after a specified time or after consumption of a specified proportion of the future economic benefits embodied in the asset, the useful life of an asset may be shorter than its economic life. The estimation of the useful life of the asset is a matter of judgement based on the experience of the entity with similar assets.

In addition, information for purchased pipelines which use the RCM asset valuation may be limited and restrict the ability of services providers being able to reconcile to book value. Therefore, reconciling the two methods may take considerable effort, and it is also not clear what (if any) usefulness this information would provide to prospective users.

Given these fundamental differences it is not at all clear how a reconciliation between book value of assets and RCM would be undertaken beyond simply showing the book value on one side, the RCM value on the other, with the difference explained at a high level (i.e. goodwill in book value).

We also note that the AER will need to consider the treatment of working capital for RCM purposes when deciding on timing of capex. Currently there is no allowance made for working capital requirement in RCM for non-scheme pipes.

We consider that the Guidelines should not require that fields in the statement of financial assets and the RCM that have the same definition must have the same values, with an explanation in the basis of preparation where they do not have the same values. Owing to similar methodological differences between book values and RCM as set out above, this is likely to take considerable effort without producing a clear net benefit for report users.

Section 3.3.3 Summary of financial information

We will consider that the AER's current summary table is sufficient and will review these requirements in the draft Guideline.

Section 3.3.4 Reporting of pipeline capacity expansions and extensions

We have concerns about the AER's proposal for service providers to publish forecast financial information for **planned** pipeline capacity expansions and extensions, as opposed to **actual** information for built capacity expansions and extensions.

Firstly, given the scale of such investments, it is our experience that estimated costs (in businesses cases) of planned expansions or extensions of pipeline assets are unlikely to match final construction costs, and in some cases can be materially greater depending on many factors including the complexity of the project, the project risk and assignment of those risks. The assignment of project risks (including but not limited to environmental approvals, land access, soil contamination or the presence of underground services) in particular may have a material impact on estimated and actual costs and on the prices paid by users of an expansion or extension, yet may also be extremely difficult to quantify.

We voluntarily share information on planned expansions and extensions (including estimated costs) with prospective users at the time they seek access to services which require us to undertake such works. This information forms the basis of negotiations between us and the prospective users, and represents the best information we have at the time. We also note that the new Part 11 access negotiation framework in the NGR provides prospective users with the ability to access this information should a service provider not be forthcoming with it during negotiations, in addition to the prospective user also having access to the dispute resolution mechanisms in Part 12 in the case of a pipeline expansion. On the basis of these existing bilateral information sharing practices and mechanisms, it is not clear why further disclosure is required.

We also consider that NGR r.103(2)(a)(iii)(C) does not require financial reporting on planned extensions or expansions but rather is about publishing information associated with the pipeline asset base in respect of a financial year, or for built expansions and extensions pipeline assets. We are interested in the AER's views as whether it agrees with our interpretation of the NGR, and if not, where in the NGR the AER is provided with power to require service providers publish in the financial statements information on planned pipeline capacity extensions and expansions.

Finally, we note that any obligations to report the cost of pipeline extensions or expansions which have been built should only apply on a prospective basis from when the Guideline takes effect. The reporting of costs for expansions or extensions which have occurred historically would represent a significant burden to pipeline operators which may not have access to such information at a granularity beyond that which is already reported by non-scheme pipelines in the existing templates (for example, in tables 4.1 and 4.1.1)—particularly where these projects occurred a long time ago or under the prior ownership of another business.

We are happy to meet with the AER to discuss this area further.

Section 3.4 Allocation of costs between pipeline services

For clarity, we would appreciate the AER confirming that the 'allocation of costs between pipeline services' means the allocation of costs to the types of pipeline service published by the service provider under NGR r.101B(3), and not to individual contracts for pipeline services.

With regards to whether the AER should prescribe a cost allocation method for allocating direct costs to each service, we note that there are too many differences between businesses and services for AER to prescribe a consistent cost allocation method. We consider that the AER's proposed position on allocation of costs, subject to the clarification above, will achieve the appropriate balance of consistency in approach and flexibility for different business models, noting also the specified cost allocation principles in r.103(4). We also note that service providers will clearly set out their cost allocation approach adopted in their basis of preparation.

Section 3.5 Cost allocation principles

We consider that the cost allocation principles in NGR r.103(4) are comprehensive requirements to ensure that the service providers' cost allocation approaches are appropriate and transparent.

Non-Scheme Pipelines

Section 4.2.1 Asset valuation approach for non-scheme pipelines

See our response to the AER's issues paper section 3.3.2 above with regards to reconciling between the RCM and book value of assets.

We also note, that in cases where we have acquired a pipeline, particularly some time ago or where the information is beyond 7 years of age, we may not necessarily have the information sought by the AER. We suggest that in any cases where there is a clear and demonstrable net benefit to service providers publishing 'back-cast' historical information as a once-off in the initial round of reporting, the AER place a best endeavours obligation on us to provide the information and that such information not be subject to the assurance requirements.

We also consider that any obligation on us to provide asset valuation reconciliation information should be at an aggregated (pipeline) level, that is, not at a disaggregated level (asset classes), as in many cases we do not capture information on that basis. It is also not clear how report users would find disaggregated information useful, particularly in cases where this information may need to be 'estimated' by the pipeline operator by pro-rating their aggregate information.

Section 4.2.2 Approach to estimating the rate of return

We note that the AER must note the following in relation to its proposed approach to setting the rate of return (**ROE**):

- While AER's rate of return instrument (**RoRI**) approach can provide some directional information to stakeholders it will not accurately reflect the actual risk free rate averaging period for the service providers which is confidential and not available to stakeholders. The AER should set stakeholder's expectations in this regard.
- The setting of the ROE parameters for market risk premium (**MRP**) and gamma should only apply prospectively and not retrospectively as they rely on historical data series which changes over time. There may also be different ways the parameters are determined over time. For example, the AER has previously given weight to Dividend Growth Model along with historical estimates for measuring MRP, similarly the gamma has been previously estimated using dividend drop off method. Therefore, it is important that these parameters currently determined by the AER are applied only prospectively as applying retrospectively could result in material misstatement of returns and mislead stakeholders.

Section 4.2.3 Decommissioning costs

We concur with the AER that estimating future decommissioning costs is very difficult given the uncertainty around the scope, costs, and timing of decommissioning. However, there is a material risk that these costs could be substantial when incurred. It should be expected that estimates of future decommissioning costs may differ substantially between service providers, or even between the pipelines operated by a service provider. Differences will arise from different regulatory obligations across jurisdictions for pipeline decommissioning, different pipeline construction and land access arrangements between pipelines and different risks associated with land use around different pipelines. Even for any one particular pipeline, the determination of the necessary remediation activities and estimation of their costs may involve significant engineering professional judgement, and the decommissioning activities deemed efficient and prudent given the risks associated with a particular asset may also change over time as regulatory requirements, engineering practices, the physical environment and the pipeline itself change.

However, decommissioning costs are costs that service providers will face to satisfy legal and licensing requirements under various jurisdictional acts. Australian Standard AS 2885 also sets out approaches to pipeline decommissioning and abandonment, including the need to assess and mitigate the risks associated with ground subsidence where an abandonment in place approach is adopted, and the need for any pipeline removal activities to meet safety and environmental requirements which are similar to those that apply to pipeline construction. The inclusion of decommissioning costs in the RCM is therefore consistent with service providers having a reasonable opportunity to recover at least their efficient costs as stipulated by the NGL revenue and pricing principles for scheme pipeline and the NGR pricing principles for non-scheme pipelines. Therefore, we agree with the continued ability for service providers to include decommissioning costs in a pipeline's RCM cost base. To the extent that further information about the basis for decommissioning cost estimates is required to inform user decision making, pipelines could potentially provide a high level description of key assumptions or methods within the reporting templates, to the extent such information is not already disclosed in pipelines' basis of preparation.

Section 4.2.4 Improving information on tax liability

The AER has stated that its '…preferred approach is for service providers to publish actual taxes paid and use these values when calculating recovered capital values through time. This should provide users with more meaningful information compared with using benchmark tax liabilities.'

This may be the case when a service provider owns a single pipeline and has no other business interests, but not when a business has multiple business assets (including multiple pipeline assets). In the latter case the actual tax liability incurred by each asset is reflective of the interest paid at the group level, and is also reflective of both tangible and intangible assets. We currently publish information about Jemena's group tax in our group's annual financial statements. However, the AER's financial reporting guideline for non-scheme pipelines ignores intangible assets when determining RCM value, but incorporates the reduction in tax costs arising from these assets, which is an inconsistent approach. Allocation of actual tax information does not provide more meaningful information unless the RCM value accounts for intangible assets.

To ensure consistency, either the reported tax liabilities need to be estimated using benchmark tax liabilities instead of allocation of group level tax cost, or the RCM needs to account for intangible assets if actual group tax needs to be allocated.

Section 4.3 Scheme Pipelines

We note that the Jemena Gas Network, a scheme pipeline, already reports capital base information as stated in the issues paper. Furthermore, historical asset value data is also reported when rolling forward the regulatory asset base as part of the access arrangement and RIN reporting processes. The AER should seek to minimise the extent to which the Guideline requires unnecessary duplication of reporting, as this will impose additional costs on service providers without providing any benefit to users.

Other Matters

As noted above, we consider that it is important that the AER distinguish between scheme and non-scheme pipeline requirements to ensure that existing scheme pipeline reporting requirements are not duplicated.

Section 5.1.3 Standing terms methodology requirements

Jemena supports the AER's acknowledgment of the different approaches service providers may use to determine standing prices. We note that this is particularly important for service providers that have acquired pipelines and consequently do not necessarily have all the information to be able to comply with one specific pricing methodology.

We note the AER's proposed information disclosure requirements depending on the specific approach that the service provider uses to calculate its standing price as set out in the issues paper, and broadly consider that these provide useful guidance to service providers.

Section 5.2.3 Basis of preparation

To the extent that the AER considers it necessary to mandate the use of a specific template for basis of preparation documents for consistency, we suggest considering the adoption of a format/layout similar to that which Jemena has used since the commencement of reporting under the AER's Financial Reporting Guideline for Non-Scheme Pipelines. We also employ a similar format to comply with RIN requirements for our gas and electricity distribution networks.

It is, however, unclear whether mandating a particular format for basis of preparation documents would necessarily reduce the likelihood of errors such as those referred to in the issues paper—such errors may instead be better controlled through business' own assurance processes.

Section 5.3.3 How and where service providers publish information

We have eight non-scheme pipeline assets which we show on a summary page on our website – see https://jemena.com.au/pipelines – which has links to supporting pages for each pipeline asset containing all information required to be published under Part 23 of the NGR (or, once the new obligations commence, Part 10) and other obligations. Part 10 information relevant to our scheme pipeline is also likely to be published in a similar format (i.e. on its own page). For service providers that have multiple pipelines (including distribution networks), we suggest that the presentation of information consistent with our current approach is likely to be the most useful in allowing prospective users and other interested parties to easily access information about the pipeline they are seeking.

Consistent with the AER's guidance on this topic in September 2022, we support the clear identification of Part 10 information through labels or headings and note the need to state clearly where any Part 10 information is not relevant or applicable in the pipeline's circumstances.

We also note the AER has previously informally indicated its intention to require publication of actual prices payable information in a specified table format. However, there is likely to be a balance required in prescribing any particular reporting format to ensure that information about commercially-negotiated services (which can vary considerably from customer to customer) can still be reported accurately and consistent with the requirements of the Rules, while also still being meaningful to users. Some flexibility in data presentation requirements is therefore still likely to be necessary. We also consider that it is important to allow for the inclusion of an optional explanation box for the published prices to enable pipeline service providers to provide additional information they consider may be necessary for users to have when interpreting information presented about a particular price/service. We would welcome further discussion with the AER about the presentation of actual prices payable information, including ways of ensuring that automated data extraction/reporting will be compatible with any proposed data presentation format requirements.

Section 5.4.2 Assurance Requirements

The assurance obligations imposed by the AER under the Guideline need to recognise that the scope of the obligation imposed on service providers must be limited to what the service providers are capable of receiving from an assurance practitioner – that is, assurance consistent with Auditing Standards. The NGR and corresponding Guideline do not bind an assurance practitioner. The assurance relationship between the service provider and the assurance practitioner is contractual, not regulatory, governed by independent auditing standards. For this reason, the regulatory obligation must be consistent with the contractual obligation which in turn is underpinned by Auditing Standards. Moving away from independently recognised audit standards risks undermining the purpose of the assurance being required. We note that NGR r.103(2)(f) gives the AER sufficient discretion to recognise the assurance framework in the Guideline.

We note the proposal to carry forward similar assurance requirements to those which currently exist under the AER's Financial Reporting Guideline for Non-Scheme Pipelines, and we broadly support this approach, notwithstanding the technical matters discussed below (which also exist under the current guideline).

Whilst NGR r.103(2)(f) specifies that the Guideline must 'provide for the manner in which the financial information, historical demand information and cost allocation methodology is to be certified as being true and fair', the sign off by an assurance practitioner will be limited to what is allowed under the relevant assurance standards proposed to be prescribed by the Guideline—in this case, Auditing Standards (ASA 800 and ASA 805), Standard on Review Engagements (ARE 2045) and Standard on Assurance Engagements (ASAE 3000).

With regards to the AER's proposed level of assurance, we understand that assurance practitioners will be able to provide a sign off sought by the AER in the case of the **limited assurance** required for service providers' RCM, historical demand and cost allocation method information.

However, in providing a **reasonable assurance** for the specified financial information, we understand that assurance practitioners will likely not be able to provide an opinion as to whether the financial information provided is 'a true and fair representation of the service provider's financial position'. Rather, per ASA 805 an assurance practitioner will likely be able to provide an opinion as to whether 'the financial report is prepared, in all material respects in accordance with the relevant presentation standards'. This is consistent with the approach taken by our assurance practitioners in relation to financial information required for non-scheme pipelines under the AER's Financial Reporting Guideline for Non-Scheme Pipelines.

We are happy to arrange a meeting with the AER and our assurance practitioners to discuss this matter further.

Section 5.5.3 Historical demand information

Although we note the Brattle commentary cited in the issues paper, we note that information about historical pipeline *revenues* (which may be more useful to prospective users than information about historical demand trends alone) are already published within the RCM information. We also note that AEMO's Bulletin Board contains a significant amount of historical pipeline demand information that is readily accessible to users.

Once the AER has provided further information about its preferred approach to historical demand data, we will assess our ability to provide this information (noting that historical information may not be available beyond certain points when current systems were implemented or records are kept), and provide further feedback at that time.

Section 5.6 Pricing Template

When designing the pricing template we suggest that consideration be given to the AER annual tariff approval processes for scheme pipelines and consider opportunities to merge this new requirement with existing regulatory processes.