Jemena Gas Networks (NSW) Ltd

Revised 2025-30 Access Arrangement Proposal

Attachment 7.2

Depreciation

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Overview

This document sets out our response to the Australian Energy Regulator's (**AER**'s) draft decision[1] on depreciation for the 2025-30 period.

Depreciation amount

Our Revised 2025 Plan seeks regulatory depreciation for the 2025–30 period totalling $582.7 million of which $230 million comprises our revised proposal for accelerated capital recovery. This investment recovery is a critical part of our complementary package of initiatives to prudently respond to future gas uncertainty amid NSW and Australia's legislated emissions reduction targets.

Depreciation methods

Our revised proposal retains the depreciation methodological specifications approved in the AER's draft decision. These include:

- Use of straight-line depreciation using the year-on-year tracking method
- Our current standard asset lives for existing asset classes
- A new Future of Gas asset class for accelerated depreciation
- The use of forecast depreciation for the subsequent roll forward of our RAB in 2030.

Pace of remaining capital recovery

In preparing our Revised 2025 Plan, we have carefully considered the AER's reasoning for its $156 million draft decision for accelerated depreciation. The AER observed:

> *We consider the benefit of accelerated depreciation in terms of reducing stranded asset risk is greatest while there is still a large customer base to share the cost recovery of the capital base.*[2]

However, fundamentally the AER's draft decision fails to act upon this opportunity by limiting depreciation during the 2025-30 period to less than the amount of RAB growth our asset will experience. This means the draft decision approach, if retained in the final decision, would:

- forego the opportunity to have our expected largest remaining customer base contribute equitably to existing capital recovery, counter to our current customer's preferences
- worsen the accrued problem of investment recovery by driving net growth in our capital asset base by 2030.

Given the current uncertain environment we consider that a $230 million future of gas deprecation allowance is the bare minimum amount required, and must be coupled with the AER providing us the opportunity to undertake complementary renewable gas projects, and innovate in how we optimise costs through programs like the Picarro leak detection services.

Our $230 million proposal is conservatively low compared to feedback in our customer representative sample testing. That testing found customer preference for at least as much accelerated depreciation as our initial proposal. 72% of the statistically representative sample ranked the two highest price levels of accelerated

[1] AER, Draft decision Jemena Gas Networks (NSW) access arrangement 2025 to 2030 Attachment 4 – Regulatory depreciation, November 2024, (**depreciation draft decision**).

[2] AER, depreciation draft decision, November 2024, p.15.

depreciation —which correspond to $400 million and $300 million of 2025-30 accelerated depreciation—as their 1st preference.[3]

Summary of responses to the draft decision

Table OV–1 summarises the AER's draft decision on depreciation and our response.

Table OV–1: JGN's response to AER draft decision on depreciation

Topic/item	AER draft decision	JGN response
Depreciation methods		
Methodology to depreciate JGN's new and existing assets	Accepted	Approved approach retained – see section 2.2.
Accelerated depreciation		
The need to accelerate depreciation	Accepted, noting: 'given the uncertainty around future demand, we consider it prudent to allow some level of accelerated depreciation for JGN in the 2025–30 period as a precautionary step'[4] and 'JGN's proposal for accelerated depreciation has largely met the expectations set out in our Information paper'[5]	We accept and welcome the AER's draft decision. No response required.
The amount to accelerate	Not accepted JGN's $300 million proposal and instead provided for $156 million.	We have modified our proposed accelerated depreciation amount to $230 million and responded to the AER's draft decision reasoning. See section 3.

Attachments

Table OV–2 lists the attachments to our Revised 2020-25 Access Arrangement Proposal which provide further information on our response to the AER's draft decision and our revised depreciation amount and approach.

Table OV–2: Revised 2020 AA Proposal attachments on Demand

Attachment	Name	Author
2.1	JGN - Sagacity - RP - Att 2.1 - Accelerated Depreciation Research Report - 20241206	Sagacity
3.1	JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110	Houston Kemp Economists
7.2	JGN - RP - Att 7.2 - Depreciation - 20250115 – Public Response to the AER's draft decision - Depreciation	JGN
7.2A	JGN – Att 7.2A – Illustrative 2020-25 PTRM excluding revenue handback – 20250115	JGN (using AER PTRM)

[3] *JGN - Sagacity - RP - Att 2.1 - Accelerated Depreciation Research Report - 20241206 – Public*.

[4] AER, depreciation draft decision, November 2024, p.14.

[5] AER, depreciation draft decision, November 2024, p.16.

1. JGN's response to the draft decision

In its draft decision, the AER expressed:

- acceptance of our depreciation methodology
- acceptance of the need for accelerated depreciation, whilst asserting that JGN's policy risk for asset stranding is somehow less than that which applied at the time of making its June 2023 Victorian AA determinations
- an entirely different approach to deciding the amount of accelerated depreciation than JGN had proposed, or our customer engagement and research had supported, namely its zero real price path approach
- a view that the AER does not need to apply the rule 89 depreciation criteria to their intended effect due to its perception of a broader policy question needing to be considered by policy makers.

1.1 Our response to the accelerated depreciation amount

We have considered the AER's reasons for its draft decision to provide us with $156 million based on achieving a zero real price path outcome. We consider that targeting a zero real price path outcome in the current and foreseeable gas demand context:

- Is entirely inconsistent with the intent of the NGO, revenue and pricing principles, and rule 89 depreciation criteria
- Places undue weight on short-term policy measures (or a lack thereof) and fails to place enough weight on commonly held view about long-term gas demand forecasts amid the NSW legislated transition to net zero by 2050, and
- Fails our customer base by burdening future customers (which the AER acknowledges will be fewer) with higher prices than would otherwise be the case through both:
  - the lower depreciation amount, and
  - the way it has applied its real price path approach.

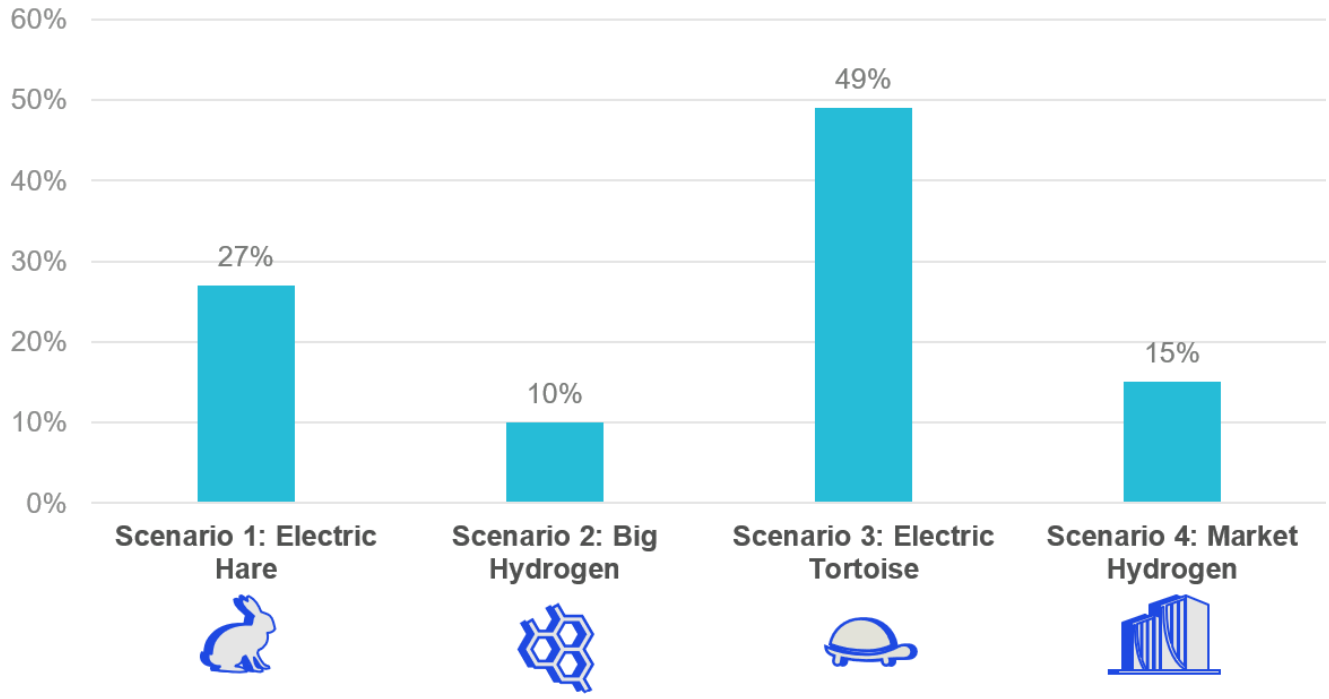
The AER must consider each element of the building block decisions on their individual merit consistent with the NGR, including being cognisant of price outcomes for customers in a consistent manner across those decisions. For example it is inconsistent to provide a $144 million lesser rate of recovery of existing investments based on a price outcome, whilst at the same time increasing prices through $66.4 million of opex socialisation to provide subsidies to disconnecting customers in clear disregard for the causer pays principle.

The short term real price path outcome is not in customers' long term interests

A short term outcome of achieving a zero real price path outcome is not likely to be in the long term interests of customers in an uncertain future. Such a constraint contributes to the socially regressive outcome of early electrifiers being subsidised by those who don't have the means to do so prior to the end of their appliance lives or due to a lack of agency to do so in Sydney's highly constrained rental market.

This inherently short term approach also ignores the long-term electrification scenarios developed by our Expert Panel and considered by them to be the most likely versions of the future that JGN should be planning to best meet our customer's long-term interests. Based on the Expert Panellists' votes, the relative likelihood of each of the four scenarios is shown below.

Figure 1–1: Relative likelihood of each scenario to 2050



Source: KPMG, Gas Networks 2050: Future scenarios summary report. Final report; January 2023, p.23.

In this long-term context, our revised proposal of $230 million of accelerated depreciation better addresses the underlying problem of demand decline compared to the AER's short-term price constraint approach. This conclusion was also reached by Houston Kemp in its report (provided at Attachment 3.1):

> *the AER appears to prioritise near or short term price stability for existing gas consumers. However, we find that maintaining price affordability over the short term will cause price volatility to be transferred into future periods, thus allocating risks away from the broader base of current customers onto a narrower base of future customers. Allocating risks in this manner will not promote the long term interests of gas consumers.*[6]

Profiling remaining depreciation to reflect declining gas demand out to 2050 is in customers' long term interests and better avoids socially regressive subsidies

Falling gas demand means that negative growth in the market for reference services is efficient under the depreciation criteria in rule 89 of the NGR. This is because it reflects the changing preferences of consumers and availability of competing technologies. The key task is now ensuring that the pace of capital recovery does not prematurely accelerate the pace of demand reduction. While being a requirement of rule 89, it is also important for achieving our NSW emissions reduction interim goals because accelerating electrification prior to having sufficient renewable energy supply will be counterproductive to those targets and potentially to electricity system reliability.

Adopting our proposed pace of depreciation promotes a more efficient pace of negative growth than the AER's draft decision by:

- as the AER explains, reprofiling more depreciation now would mitigate potential price increases in the future beyond 2030, in turn encouraging fewer customers to leave gas networks prematurely, and
- reprofiling more depreciation now enables our gas network to remain financially viable and competitive on price with other energy sources for a longer period, thereby facilitating:

[6] *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250107 – Public*, p.iv.

— a more orderly energy transition without accelerating gas price increases in future

— a more equitable energy transition allowing more customers to benefit from the use of the remaining lives of their gas appliances.

Our proposal is more consistent with the rule 89 depreciation criteria

In its report (provided at *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250107 - Public*), Houston Kemp has compared how our initial proposal of $300 million and its reasoning compare with the AER's draft decision against the rule 89 depreciation criteria. Its findings are replicated in Figure 1-2:

Figure 1–2: Relative consistency of JGN's and the AER's proposed depreciation adjustments to the depreciation criteria

Criteria	Relative consistency	Reasoning
(1) The depreciation schedule should be designed:		
(a) so that reference tariffs will vary, over time, in a way that promotes efficient growth in the market for reference services	**JGN more consistent**	JGN's proposed depreciation adjustment better promotes efficient (negative) growth in the market by bringing forward depreciation.
(b) so that each asset or group of assets is depreciated over the economic life of that asset or group of assets	**JGN more consistent**	JGN's higher proposed depreciation amount brings it closer to depreciating the value of its assets over their economic lives, relative to the amount proposed by the AER, given use of its assets will likely cease before they reach the end of their design lives.
(c) so as to allow, as far as reasonably practicable, for adjustment reflecting changes in the expected economic life of a particular asset, or a particular group of assets	**JGN more consistent**	JGN's proposed depreciation amount better adjusts the depreciation schedule to reflect changes in the expected economic life of its assets, which will likely cease by 2050.
(d) so that (subject to the rules about capital redundancy), an asset is depreciated only once (ie that the amount by which the asset is depreciated over its economic life does not exceed the value of the asset at the time of its inclusion in the capital base (adjusted, if the accounting method approved by the AER permits, for inflation))	**JGN and AER similarly consistent**	Both JGN and the AER depreciate assets once.
(e) so as to allow for the service provider's reasonable needs for cash flow to meet financing, non-capital and other costs	**JGN likely more consistent**	JGN's proposed depreciation adjustment provides a greater amount of cash flow relative to the AER in the near term, which is more likely to meet JGN's reasonable needs for cash flow to cover financing, non-capital and other costs.
(2) Compliance with subrule (1)(a) may involve deferral of a substantial proportion of the depreciation, particularly where:		

Criteria	Relative consistency	Reasoning
(a) the present market for pipeline services is relatively immature (b) the reference tariffs have been calculated on the assumption of significant market growth (c) the pipeline has been designed and constructed so as to accommodate future growth in demand	**JGN more consistent**	JGN's proposed depreciation adjustment better promotes efficient (negative) growth in the market by bringing forward depreciation.

Source: *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110 – Public,* table E-1.

This conclusion about the relative inconsistency of the AER's draft decision approach compared to JGN's proposal is unsurprising given:

1. the draft decision approach focusses on short term price outcomes and short term net zero enabling policy settings in NSW
2. whereas the criteria and JGN's proposal both focus on the market for gas services, the trajectory of demand for services over the assets' life and how the depreciation schedule can best support an efficient rate of change in the demand for gas services.

The short term zero real price path approach as applied in the draft decision will exaggerate price shocks

The short term zero real price path approach as applied in the draft decision uses a launch point and capped rate of change that both exacerbate future price shock, for: 1) building block cost realignment, and 2) AA changes if short term NSW gas policies transpire.

If a capped price growth rate approach is applied in a final decision, it must avoid these price shock outcomes by accounting for:

A cost reflective launch point | The price path constraint cannot be applied to an unsustainably low launch point[7] having regard to our actual efficient cost of supply. The draft decision fails to recognise that our current prices are not reflective of the efficient building block levels. This is due to the large 2015-20 over-recovery handback during the 2020-25 period that materially reduced them below sustainable costs. It also fails to recognise that JGN's WACC is rising from the current period to the next period by more than 1.26% when the equivalent Victorian increase was only 0.15%.

Not creating future price shock | The combination of a deflated launch point and zero real price path is that the AER's draft decision would result in the AER's price path necessarily triggering a price rise of at least 4.2%[8] moving into the subsequent (2030-35) AA period to realign our revenues with our cost of supply (as required in the electricity rules[9] and has been the AER's standard practice for price paths in gas AAs[10]) – an outcome which would clearly be counterproductive to the AER's price path outcome logic.

A net zero policy reflective real price path | The zero real price path target is inconsistent with the AER's average 1.5% real price path approach for the Victorian gas distribution networks' 2023-28 AAs. We note that this approach was decided in June 2023 *before* the Victorian connections ban was announced making the circumstances of that decision not materially different to JGN's from a short term jurisdictional gas policy perspective. Moreover, when Victorian gas policy measures did subsequently transpire, Ausnet's reopener

7 Launch point here refers to the 2024-25 prices and revenue used to calculate the price change into the 2025-30 period.

8 The 4.2% is taken from cell R44 of the *X-factors* sheet of the step 2 Post Tax Revenue Model (**PTRM**) included with the AER's draft decision. It is calculated as the relative difference between the smoothed and building block revenues in the 2029-30 year. We say 'at least' because the 4.2% is a comparison of revenue. If – consistent with the trend reflected in the demand forecast for the 2025-30 period adopted in the draft decision – demand were to reduce from 2029-30 to 2030-31, then the price impact would be even greater than a 4.2% price increase.

9 NER rule 6.5.9(b)(2).

10 AER, Draft decision Jemena Gas Networks (NSW) access arrangement 2025 to 2030 Overview, November 2024, p.13.

application now seeks a real price path of 6.47% above the AER's decision for the remaining 3 years of its AA period.

Houston Kemp similarly find that the draft decision's short term zero real price path approach has no sound basis. Houston Kemp state:

> *we find there is no sound basis for the AER's draft decision to set a zero real price path constraint for JGN, being less than the 1.5 per cent constraint applied to gas distribution businesses in Victoria. Our reasons are three-fold. Firstly, AEMO's projections suggest that the rate of future decline in residential and commercial gas consumption will be broadly similar across NSW and Victoria. This contradicts the AER's conclusion that the policy settings in NSW are less indicative of the reduced role for gas networks in the state. Further, the AER's assessment does not take into account the magnifying effect on the risks faced by JGN as derived from its obligation to incur capital expenditure on new gas connections for requesting customers who, thereafter, may disconnect from the network before JGN has recovered the costs of these connections.*
>
> *In addition, the AER's real price growth constraint affects JGN more adversely than it does the Victorian gas distributors, because:*
>
> - *JGN's rate of return on capital for the 2020-25 regulatory period is materially lower than that applied to the Victorian gas distributors, while its rate of return on capital for the 2025-30 regulatory period is materially higher than that applied to the Victorian gas distributors; and*
> - *the AER's draft decision includes a one-off revenue adjustment that increases JGN's revenues for the 2025-30 regulatory period.*
>
> *Accordingly, there is no sound basis by which the AER would set a real price growth constraint for JGN that is less than the 1.5 per cent constraint applied to gas distribution businesses in Victoria. Rather, JGN is likely to require at least a 1.5 per cent per annum real price increase in order to provide it a reasonable opportunity for cost recovery.*[11]

Our initial proposal was a prudent multi-limbed approach to the energy transition

Our Initial 2025 Plan included a number of carefully balanced, complementary measures to respond to the changes we are facing into as a result of the energy transition. These include: renewable gas connection projects; changing our Model Standing Offer to require more customers to make an up-front contribution when connecting to the network; proposing expenditure targeted to reduce emissions (such as Picarro), revenue rebalancing to industrial users, and accelerated depreciation. We have had to do this in an environment where the outlook for energy policy in NSW is uncertain, including in terms of timing of electrification and the eventual energy mix. We consider that the measures that we have proposed are consistent with that of a prudent service provider acting to promote efficient investment in, and efficient operation and use of, gas services for the long term interests of consumers of gas as required by the by the NGO.

In preparing our Draft 2025 Plan and Initial 2025 Plan, we did so with customers in the forefront of our mind to ensure that we were considering their long term interests as required NGO and that our forecast costs and charges reflected the revenue and pricing principles (RPP).

We note that contrary to stakeholder submissions, our Initial 2025 Plan to increase depreciation by $300 million relative to the historical depreciation pace does not represent any form of windfall payment. It is an NPV neutral repayment of our investments that reflects a depreciation profile that better promotes an efficient pace of gas demand decline in the market for reference services.

We have lessened our accelerated depreciation request to the average amount approved in Victoria prior to their short term gas transition policy measures.

In preparing our Revised 2025 Plan, we have carefully considered the AER's reasoning for its $156 million draft decision for accelerated depreciation. Given the current NSW energy transition by 2050 we consider that a $230

[11] *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110 – Public*, pp.iv-v.

million future of gas depreciation allowance is the bare minimum amount required as it affords JGN an equivalent opening RAB share to what was approved for the Victorian gas distributors—see Table 1-1. This minimum amount must be coupled with the AER providing us the opportunity to undertake complementary renewable gas projects, and innovate in how we optimise costs through programs like Picarro.

Our $230 million proposal is supported by the results of a statistically representative quantitative survey of our customers, in which 72% of respondents ranked the two highest levels of accelerated depreciation—which correspond to $400 million and $300 million—as their first preference.[12]

Our lower revised accelerated depreciation proposal is also consistent with the amount that can be recovered under an appropriately adjusted real price path approach, as discussed below and explained in section 3.3.

Our revised proposal is a modest yet necessary response to better support an efficient energy transition. Table 1-1 shows JGN's revised proposal is only recovering 6% of its opening RAB in its accelerated depreciation proposal which is:

- less than the amount of at least 20% needed for each of the next five AA periods to support full RAB recovery by 2050, and
- in line with the average RAB share accelerated for Victorian gas distribution networks' decisions, noting Ausnet's reopener proposal is even higher.

Table 1-1: Comparison of adjusted RAB recoveries

Gas distribution network	AD as % of Opening RAB
JGN – Initial 2025 Plan	7.8%
JGN – AER Draft Decision	4.0%
JGN – Revised 2025 Plan (proposed)	**6.0%**
Average Vic gas distribution networks	6.1%
Ausnet – Reopener (proposed)	9.4%

If the AER retains its draft decision approach, it must address the launch point and price change issues

If the AER does not accept our revised proposal of $230 million accelerate depreciation, and chooses to maintain its capped real price path approach, then it needs to adjust it to account for:

1. The 2024-25 prices it is launching from as these:
    a) are artificially deflated below our cost of supply due to the $203 million revenue handback for previous period over-recovery and the unprecedently low interest rate environment in 2020
    b) would result in the AER's price path necessarily triggering a price rise of at least 4.2%[13] moving into the subsequent (2030-35) AA period to realign our revenues with our cost of supply (as required in the electricity rules and has been the AER's standard practice for price paths in gas AAs[14]) – an outcome which would clearly offend the AER's pricing outcome logic.
2. An equivalent price path (i.e. up to 1.5% p.a. real) as it afforded Victorian gas networks recognising that:
    a) the policy information available at the time of that determination was not the more certain gas connections ban and full connection contribution policy that was subsequently implemented

12 JGN - Sagacity - RP - Att 2.1 - Accelerated Depreciation Research Report - 20241206 - Public

13 The 4.2% is taken from cell R44 of the *X-factors* sheet of the step 2 PTRM included with the AER's draft decision. It is calculated as the relative difference between the smoothed and building block revenues in the 2029-30 year. We say 'at least' because the 4.2% is a comparison of revenue. If – consistent with the trend reflected in the demand forecast for the 2025-30 period adopted in the draft decision – demand were to reduce from 2029-30 to 2030-31, then the price impact would be even greater than 4.2%.

14 AER, Draft decision Jemena Gas Networks (NSW) access arrangement 2025 to 2030 Overview, November 2024, p.13.

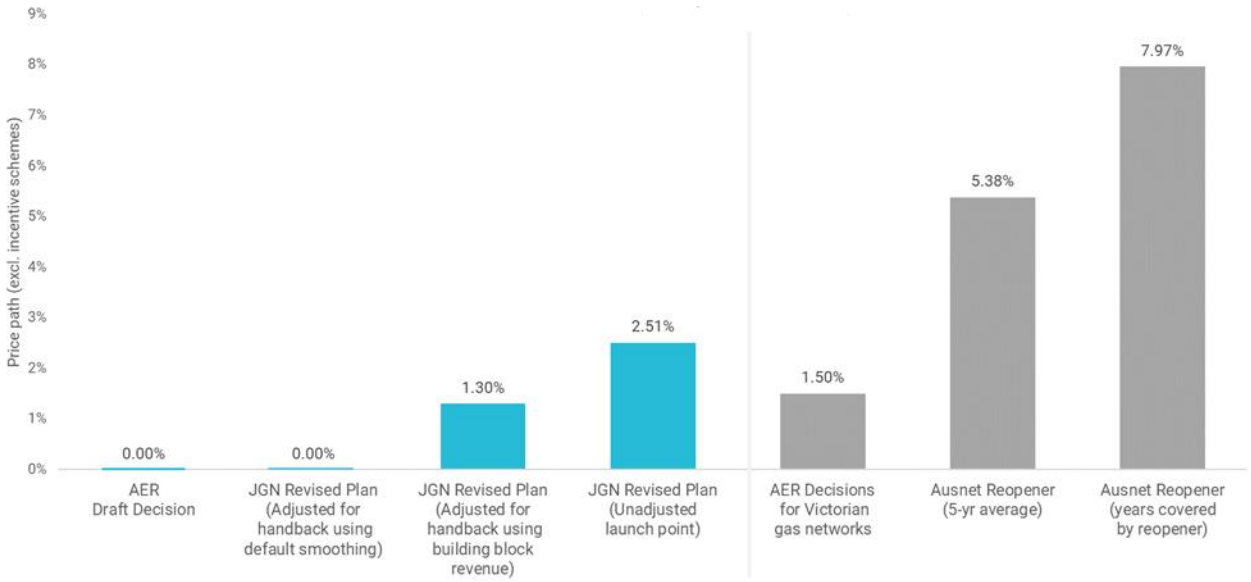
b) setting of that policy since the determination has driven an even high required price outcome in the reopener application made by Ausnet which needs an additional 6.47% real increase per year for the final 3 years of its AA period

c) JGN's $300 million proposal was calibrated down for the NSW policy status and did not target full RAB recovery by the binding NSW 2050 net zero target date as shown in Table 1-1 above

d) if policy certainty did transpire in NSW, JGN would be seeking higher 2025-30 depreciation to achieve cost recovery amid that policy (e.g. recovery of JGN's existing investment by 2050 would require depreciation in each AA period from now until then of at least $773 million in real 2025 terms per 5 year period *on average*[15]).

Adjusting for the above launch point issue on revenue handback shows that, when the handback is properly accounted for, our revised proposal of $230 million is consistent with a zero real price path. Our proposal also better aligns our 2030 smoothed revenues to within 1.13% of the building blocks for that year, thereby avoiding the 4.2% future price shock inherent in the AER's draft decision approach. We discuss this in more detail in section 3.3.

Figure 1–3: Price path comparisons (Real, % per annum over 2025-30, excluding incentive schemes)



We would welcome the opportunity to discuss any aspects of our revised proposal with the AER.

1.2 Our response to the AER's characterisation of its depreciation task

The AER must apply the rules as made and not wait for unannounced changes to the regulatory framework

In the AER's draft decision, the AER did not wholly accept JGN's proposal in respect of accelerated depreciation. It noted that it is not appropriate for the AER to allow the full amount of accelerated depreciation sought by JGN to address the stranding risk because:

15 The $773 million was calculated by taking the opening RAB (as at 30 June 2025) of $3.9 billion (from cell J57 of the *PTRM input* sheet of the step 2 PTRM included with the draft decision) and dividing it by the five 5-year regulatory periods up to 2050 (i.e., 2025–30, 2030–35, 2035–40, 2040–45, and 2045–50). In reality, this value is likely to understate the amount of real depreciation required in the earlier periods because it does not seek to smooth out recovery over those periods to reflect the decline in demand. Nor does it recognise that real depreciation will need to increase over time to recover new capex incurred.

> *accelerated depreciation will not remove the need to resolve the broader policy question involving consumers, network businesses and governments on who should pay for the costs of stranding risk associated with past capital investments, or when, and how this will occur*[16]
>
> and
>
> *We therefore consider adjusting the amount of accelerated depreciation to target a 'base' real price increase limit to ensure stable price increases for the 2025–30 period to be the most appropriate approach until a more permanent solution is developed to reduce the uncertainty associated with stranded asset risk.*[17]

We consider this an erroneous basis for the AER to reject JGN's proposal. Rather, in making its decision, the AER should be applying the NGR currently in place. The AER must provide JGN reasonable opportunity to recover its efficient costs. It should not leave this to future policy settings around treatment of stranding risk, in fact it should facilitate recovery of efficient investment that JGN has incurred to meet the needs of its customers while there is opportunity to do so. This will provide the regulatory stability required to attract continued investment to service the 1.5 million customer base JGN currently has.

As noted in the AER's Information paper on regulating gas pipelines under uncertainty of November 2021, accelerated depreciation in rule 89 is the most appropriate mechanism in the NGR to reduce asset stranding risk arising from demand uncertainty in the gas sector. The AER also recognises this in its draft decision.[18] Rule 88 requires the depreciation schedule for an access arrangement proposal to set out the basis on which the pipeline assets constituting the capital base are to be depreciated for the purpose of determining a reference tariff. Rule 89 requires the depreciation schedule to be designed so as to allow, as far as reasonably practicable, for adjustment reflecting changes in the expected economic life of a particular asset or group of assets (rule 89(1)(c)).

The AER is required by rule 89(1)(c) to allow the amount of $583 million of depreciation proposed by JGN. JGN's proposal was formulated in accordance with rule 89(1)(c) having regard to the expected economic lives of JGN's assets given the net zero emission targets set by the NSW Government. Rule 89(1)(c) requires the depreciation schedules to allow for adjustments to asset values to reflect changes in the expected economic life of assets, subject only to the qualification of the requirement by the words 'as far as reasonably practicable'.

In its draft decision, the AER has not determined on a depreciation profile that reflects the reduction in the life of JGN's assets as far as reasonably practicable. JGN accepts that it would not be practicable to adjust depreciation to the extent required to fully reflect the shortening of the life of JGN's assets, and so ensure JGN is able to recover the cost of those assets in full, including because such an adjustment would involve a real increase in prices of such magnitude as would result in a contraction in demand that would render the recovery of allowed revenues impossible. However, this is not what is proposed by JGN in its accelerated depreciation proposal. Rather, JGN's proposed accelerated depreciation represents a reasonable real price increase for consumers as evidenced by our consumers support for the level of price increase associated with either $300 or $400 million of accelerated depreciation.[19] The AER's draft decision to set depreciation at a base real price increase of 0% is non-compliant with rule 89(1)(c) because it is practicable for the depreciation schedules to be adjusted to the level proposed by JGN.

The draft decision has not had adequate regard to the emission targets set by the NSW Government

In addition, as the AER recognises in its draft decision, in making its decision on JGN's AA proposal, the AER is required to make a decision that will contribute, or will be likely to contribute to the achievement of the NGO (NGL, section 28(1)(a)). Further, the provisions of an AA proposal must be consistent with the NGO (NGR, rule 68B). The AER's decision on JGN's accelerated depreciation is inconsistent with the NGO – in particular, the objective of promoting efficient investment in, and efficient operation and use of, covered gas services for the long term interests of consumers of covered gas with respect to the achievement of targets set by a participating jurisdiction for reducing Australia's greenhouse gas emissions. The AER's decision on JGN's accelerated depreciation does not go far enough to promote efficient investment in and efficient operation of JGN's gas network having regard

16 AER, depreciation draft decision, November 2024, p.11.

17 AER, depreciation draft decision, November 2024, p.18.

18 AER, depreciation draft decision, November 2024, pp.13-14, 16.

19 JGN - Sagacity - RP - Att 2.1 - Accelerated Depreciation Research Report - 20241206 - Public

to the emission targets set by the NSW Government. Given those emission targets, the AER's decision leaves JGN with investment risk because of the risk that JGN will not be compensated for its investment in its gas network. It is also contrary to the revenue and pricing principles in section 24 of the NGL, which disclose an intent that JGN be provided with an opportunity to recover its efficient costs, or with compensation for bearing the risk of not doing so, and also be compensated for risks they bear.

The draft decision places undue weight on short term NSW policy settings, which is not the right time horizon for considering either depreciation or the effects of the legislated NSW emissions reduction targets. As Houston Kemp observe:

> *The fact that JGN has incurred capital expenditure on assets with a design life of up to 80 years, while legislated targets will necessitate a substantial reduction or cessation in the use of gas assets within the next 25 years, is more relevant to this assessment than the presence or extent of policy measures in place at the beginning of, or over the course of, the next access arrangement period. These legislated targets effectively reduce the economic life of JGN's gas assets, so that JGN's proposed depreciation adjustment, rather than the AER's proposed depreciation allowance, provides a more reasonable opportunity for cost recovery.*[20]

[20] *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110 – Public*, p.iv.

2. Our forecast of depreciation and its basis

This section explains our revised proposal amount of 2025-30 depreciation, the depreciation methods and asset life assumptions underpinning it.

2.1 Our forecast depreciation amount

Our revised proposal for regulatory and straight-line depreciation amounts for the 2025–30 period are set out in Table 2-1. We have separately identified the additional straight-line depreciation that results from our accelerated depreciation proposal discussed further in section 3.

Table 2-1: Revised forecast depreciation ($2025, millions)

	2025-26	2026-27	2027-28	2028-29	2029-30	Total
Straight-line depreciation						
Standard	164	169	175	180	184	872
Accelerated depreciation	46	46	46	46	46	230
Total	**210**	**215**	**221**	**226**	**230**	**1,102**
Less indexation	(105)	(105)	(105)	(103)	(101)	(519)
Regulatory depreciation	**105**	**110**	**116**	**122**	**129**	**583**

2.2 Our depreciation approach

Our revised proposal retains the depreciation methodological specifications approved in the AER's draft decision. These include:

- Use of straight-line depreciation using the year-on-year tracking method
- Our current standard asset lives for existing asset classes
- A new Future of Gas asset class for accelerated depreciation
- The use of forecast depreciation for the subsequent roll forward of our RAB in 2030.

Table 2-2 provides a summary of asset classes and asset lives that will apply for the 2025–30 period.

Table 2-2: Asset lives for existing and new asset classes

Asset Class Name	Closing RAB as at June 2025 ($M Real 2025)	Effective existing asset life as at June 2025 (years)	Standard life (years)
Trunk Wilton-Sydney	52.1	29.0	80.0
Trunk Sydney-Newcastle	82.4	37.6	80.0
Trunk Wilton-Wollongong	8.8	32.4	80.0
Contract Meters	11.3	13.4	15.0
Fixed Plant - Distribution	205.3	42.5	50.0
HP Mains	549.3	54.2	80.0
HP Services	20.5	43.4	50.0
MP Mains	1,192.2	23.9	50.0
MP Services	1,029.8	35.4	50.0
Meter Reading Devices	58.4	11.5	15.0
Country POTS	13.1	23.1	50.0
Tariff Meters	256.0	13.2	15.0
Computers - IT Infrastructure	0.6	3.3	5.0
Fixed Plant	1.6	5.7	10.0
Furniture	-0.7	0	10.0
Land	8.5	n/a	n/a
Low value assets	0.0	0	10.0
Mobile Plant	6.4	7.0	10.0
Vehicles	3.9	4.3	6.0
Future of Gas MP Services	267.9	5.0	n/a
Leasehold Improvements (SL)	7.4	5.4	10.0
Buildings (SL)	40.6	40.3	48.0
Software - Inhouse (SL)	35.3	3.8	5.0
Equity raising costs	2.3	39.9	42.5

3. How much accelerated depreciation we are now proposing

This section explains how we are proposing to accelerate recovery of $230 million of our existing RAB assets. This is lower than the $300 million we proposed in our 2025 Plan.

3.1 What we are now proposing

Our Revised 2025 Plan now proposes to accelerate depreciation of $230 million (6.0%) of our existing RAB over the 2025–30 period compared to what these assets' technical design lives (i.e. our standard asset lives) would provide. This is $70 million less than our Initial 2025 Plan.

3.2 How is our proposal preferable to the AER's zero price path outcome

What is the right horizon to assess depreciation recovery and customers' long-term interests?

The horizon for assessing JGN's proposed depreciation schedule under rule 89 and in alignment with the revenue and pricing principles for a reasonable opportunity to recover JGN's efficient costs has to be informed by:

- The weighted average effective remaining life of our assets which is 33 years[21] with $1.8 billion unrecovered assets by 2050[22]
- The 25 year period to NSW's 2050 emissions reduction target, noting the effects of the 2030 50% reduction interim target and the 2035 70% reduction interim target
- The average remaining life of our customers' gas appliances and plant investments and the resulting likely timeline of their replacement or electrification.

The fact that NSW customers' gas demand over these horizons will reduce is commonly held by JGN, AEMO, our Export Panel, various submissions[23], and even acknowledged by the AER which states:

> *We recognise that there is currently evidence indicating that demand for natural gas is likely to gradually decline in the long-term as NSW transitions to meet its net zero emissions goals. The impact of declining demand will lead to higher network costs per customer due to fewer customers to share the fixed costs, and therefore increasing stranded asset risk.*[24]

This is why our Expert Panel developed four scenarios out to 2050. All of which forecast NSW's total gas demand throughput to decline in the medium to long term, which the AER's draft decision rightly observes as is AEMO's 2024 Gas Statement of Opportunities (GSOO).[25]

JGN submits that a proper assessment of the need for and consequences of reprofiling our capital recovery as provided for in rule 89 requires looking at the full period price outcomes to 2050, not the outcomes for the first five years of that period.

This is a conclusion also reached by Houston Kemp, who states:

21 This is calculated using the opening values and remaining lives for the assets shown in Table 2-2 for depreciating asset classes (i.e., excluding land and low value assets) and setting the remaining life for the future of gas assets to that for the MP services. If new assets are included, then the weighted average remaining life will be higher.

22 Under the Electric Tortoise future scenario as presented in JGN's future of gas model submitted in the Initial 2025 Plan (*JGN - Att 7.8M - Future of gas model – 20240628*)

23 As noted in submissions made to the AER including by Ausgrid, Institute for Energy Economics and Financial Analysis, Justice and Equity Centre, Energy Consumers Australia, CCP31 and Rewiring Australia.

24 AER, depreciation draft decision, November 2024, p.11.

25 Ibid.

> *Crucially, JGN has incurred capital expenditure on assets with a design life of up to 80 years, while legislated targets will necessitate a substantial reduction or cessation in the use of gas assets within the 25 years though to 2050. Put another way, the NSW and Australian governments' legislated targets, regardless of short term policy settings, effectively reduce the economic life of JGN's gas assets. Consequently, long term policy objectives are more relevant to the AER's assessment than the presence or extent of policy measures in place over the next access arrangement period.*[26]

The issue being addressed is demand decline (or negative demand) not demand uncertainty

When looking at this horizon, demand decline is indisputable. Policy outcomes are legislated, and they will not be met without gas demand decline.

This means that whether NSW, Victoria or ACT have harmonised *interim* policy measures or not is irrelevant to the amount of depreciation reprofiling required because:

1. The demand trajectory is to decline from here – as commonly agreed per above
2. This AA period will have the largest customer base and greatest customer demand over which to equitably share the capital recovery costs. This period is the most beneficial time to use this important regulatory lever – as also acknowledged by the AER in its draft decision:

> *We consider the benefit of accelerated depreciation in terms of reducing stranded asset risk is greatest while there is still a large customer base to share the cost recovery of the capital base.*[27]

Our customers recognise this, and the socially regressive and intergenerational inequitable outcomes of delaying action. That is why they overwhelmingly supported our 2025-30 depreciation options and corresponding price increases that aligned with either $400 million or $300 million in our representative sample survey.[28]

Waiting for more specific NSW interim gas policy measures is not needed, and as the Victorian experience of Ausnet shows, will only exacerbate customer bill impacts both within and after the 2025-30 period. Our proposal better addresses the underlying problem of demand decline compared to the AER's short-term price constraint approach. This conclusion was also reached by Houston Kemp:

> *Finally, the AER proposes a constant real price path, starting from the final prices in the current regulatory period. It has done so to be 'prudent' and allow 'a measured start to accelerated depreciation while maintaining price affordability for consumers'. By its approach, the AER appears to prioritise near or short term price stability for existing gas consumers. However, we find that maintaining price affordability over the short term will cause price volatility to be transferred into future periods, thus allocating risks away from the broader base of current customers onto a narrower base of future customers. Allocating risks in this manner will not promote the long term interests of gas consumers.*[29]

Our approach better avoids stranding our customers' gas appliances and gas plant and equipment

An orderly transition to renewable energy out to 2050 should not strand customers' gas appliances. But the draft decision would necessarily increase future prices, accelerate gas defections, and increase the likelihood of JGN's shutdown before some customers are ready to replace their gas appliances thereby prematurely stranding customers' gas appliances. That outcome cannot be in customers' long-term interests and will raise customers' costs of energy transition relative to the orderly lifecycle replacement transition case.

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26 *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110 – Public*, p.32.

27 AER, depreciation draft decision, November 2024, p.15.

28 JGN - Sagacity - RP - Att 2.1 - Accelerated Depreciation Research Report - 20241206 - Public

29 *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110 – Public*, p.iv.

Prematurely stranding customers' gas appliances was a key concern of our Advisory Board when considering options for addressing declining gas demand as reflected in the problem statement it developed.[30]

JGN considers the AER's draft decision fails to adequately account for the heighted risk of customer gas appliance stranding that results from its lower substituted level of depreciation. This must be accounted for when considering gas users' long-term interests. Prematurely stranding their appliances cannot be in their interests and raises the cost of our energy transition.

3.3 AER's draft decision approach does not consider JGN's unique situation of handback in the current period

The AER's draft decision of 0% real price path is derived from JGN's actual 2024-25 prices. These prices are artificially suppressed due to the revenue handback in the 2020-25 AA period for an over-recovery in the 2015-20 period. Consequently, the smoothed revenue for 2024-25, as determined in the AER's 2020-25 final decision, falls below JGN's actual building block cost of supply.

This places JGN at a disadvantage when applying the price path targeting approach the AER applied for Victorian gas distributors, and would result in the AER's price path necessarily triggering a price rise of at least 4.2%[31] moving into the 2030-35 period to realign our revenues with our efficient cost of supply.

Figure 3–1 below illustrates the effects of this issue as follows:

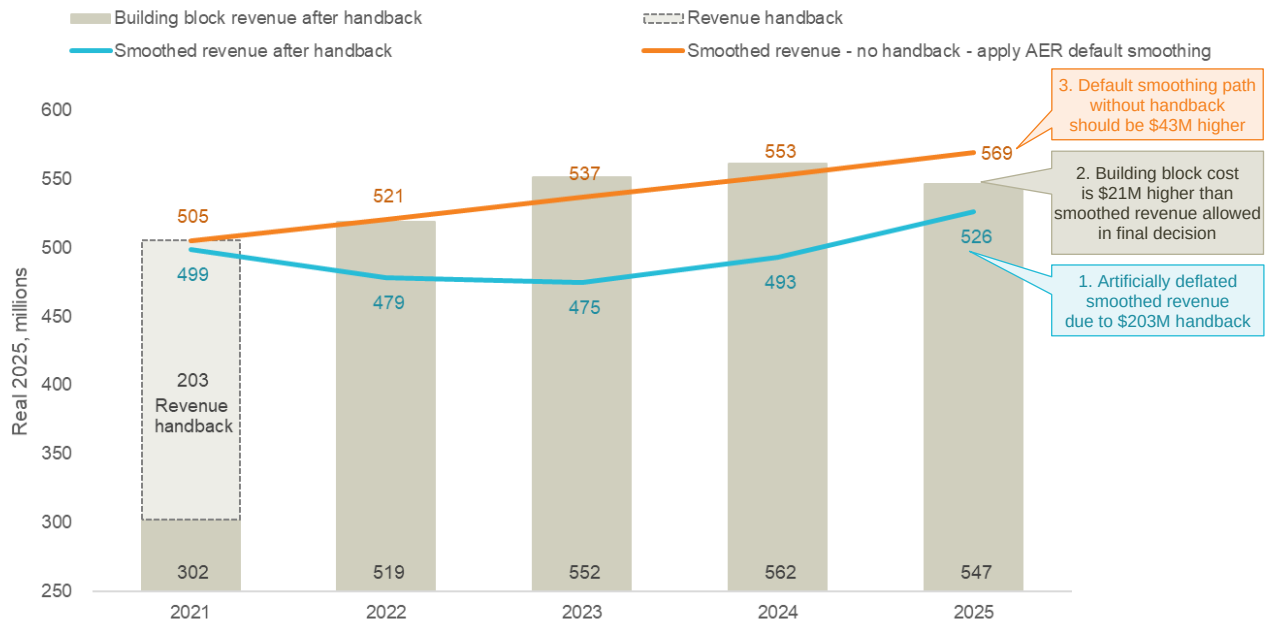
1. The blue line shows the AER's 2020-25 smoothed revenue decision which was deflated by $203 million for an over-recovery in the 2015-20 period
2. The beige bars show JGN's building block costs over the period as approved in the 2020-25 final decision
3. The orange line shows that when the revenue handback of $203 million is excluded and the 2020-25 period revenue is resmoothed using the AER's default smoothing method in the PTRM, the smoothed revenue for 2024-25 would increase by $43 million.

This highlights that JGN's actual 2024-25 prices which reflect the AER's 2020-25 final decision smoothed revenue will underrepresent JGN's true cost-reflective revenue baseline.

Figure 3–1: Accounting for the revenue handback in the price path launch point

30 Initial proposal JGN - KPMG - Att 2.4 – Advisory Board Report – 20230531 - Public

31 The 4.2% is taken from cell R44 of the *X-factors* sheet of the step 2 PTRM included with the AER's draft decision. It is calculated as the relative difference between the smoothed and building block revenues in the 2029-30 year. We say 'at least' because the 4.2% is a comparison of revenue. If – consistent with the trend reflected in the demand forecast for the 2025-30 period adopted in the draft decision – demand were to reduce from 2029-30 to 2030-31, then the price impact would be even greater than 4.2%.

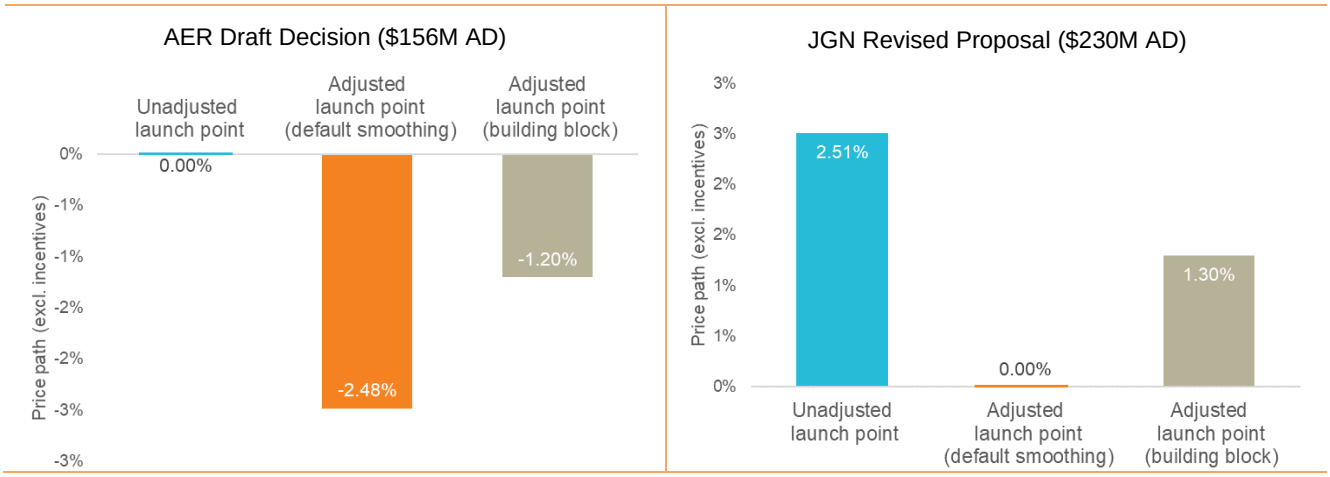


The AER's draft decision of 0% real price increase is derived from JGN's 2024-25 prices, which are artificially suppressed due to the revenue handback. Consequently, the smoothed revenue for 2024-25, as determined in the AER's 2020-25 final decision, falls below the building block cost. This means that as a launch point it does not provide a revenue amount sufficient to recover JGN's efficient cost of supply.

When the revenue handback of $203 million is excluded, with the revenue resmoothed using the AER's default smoothing method in the PTRM, the smoothed revenue for 2024-25 would increase by $43 million. Even just to realign with the building block for that year, JGN's revenue would need to be $21 million higher.

Figure 3–2 below illustrates the impact of adjusting the launch point to the price path. It compares the effective price path from the unadjusted launch point (i.e. actual 2024-25 prices) (blue bars) with the adjusted launch points (with default smoothing in orange and matching building block cost in beige) showing the resulting price path when this is accounted for. It shows that when the handback is properly accounted for, our revised proposal of $230 million is consistent with a zero real price path. Our proposal also better aligns our 2030 smoothed revenues to within 1.13% of the building blocks for that year, thereby avoiding the 4.2% future price shock inherent in the AER's draft decision approach.

Figure 3–2: Price path outcomes after accounting for the revenue handback in the price path launch point



If the AER retains its draft decision approach, it must address the launch point and price change issues

If the AER does not accept our revised proposal, and chooses to use its real price constrain approach, then the AER needs to adjust its approach for:

1. The prices it is launching from as these:
    a) are artificially deflated below our cost of supply due to the due to the $203 million revenue handback for previous period over-recovery and the unprecedently low interest rate environment in 2020
    b) would result in the AER's price path necessarily triggering a price rise of at least 4.2%[32] moving into the 2030-35 period to realign our revenues with our cost of supply (as required in the electricity rules[33] and has been the AER's standard practice for price paths in gas AAs[34]) – an outcome which would clearly offend the AER's pricing outcome logic.
2. An equivalent price path change (i.e. up to 1.5%) as it afforded Victorian gas networks recognising that:
    a) the policy information available at the time of that determination was not the more certain gas connections ban and full connection contribution policy that was subsequently implemented
    b) the setting of that policy since the determination has driven an even higher required price outcome in the reopener application made by Ausnet which needs an additional 6.46% real increase per year for the final 3 years of its AA period
    c) JGN's $300 million proposal was calibrated down for the NSW policy status and did not target full RAB recovery by the binding NSW 2050 net zero target date
    d) if policy certainty did transpire in NSW, JGN would be seeking higher 2025-30 depreciation to achieve cost recovery amid that policy (e.g. recovery of JGN's existing investment by 2050 would require depreciation in each AA period from now until then of at least $773 million in real 2025 terms per 5 year period *on average*[35]).

We consider each of these issues below.

3.3.1 A cost reflective revenue launch point is needed

Our 2024-25 revenues are $43 million below the efficient building block costs

Without adjustment, 2024-25 is not a cost reflective launch point.

The price path constraint cannot be applied to an unsustainably low launch point having regard to our actual efficient cost of supply. The draft decision fails to recognise that our current prices are not reflective of the efficient building block levels.

JGN's 2020–25 period revenues includes a reduction of $169.1 million ($2019–20) or $203 million in $2024-25 for the AER's remade final decision for JGN for the 2015–20 period (the 'remittal'). This downward adjustment

[32] The 4.2% is taken from cell R44 of the *X-factors* sheet of the step 2 PTRM included with the AER's draft decision. It is calculated as the relative difference between the smoothed and building block revenues in the 2029-30 year. We say 'at least' because the 4.2% is a comparison of revenue. If – consistent with the trend reflected in the demand forecast for the 2025-30 period adopted in the draft decision – demand were to reduce from 2029-30 to 2030-31, then the price impact would be even greater than 4.2%.

[33] National Electricity Rules rule 6.5.9.

[34] AER, Draft decision Jemena Gas Networks (NSW) access arrangement 2025 to 2030 Overview, November 2024, p.13.

[35] The $773 million was calculated by taking the opening RAB (as at 30 June 2025) of $3.9 billion (from cell J57 of the *PTRM input* sheet of the step 2 PTRM included with the draft decision) and dividing it by the five 5-year regulatory periods up to 2050 (i.e., 2025–30, 2030–35, 2035–40, 2040–45, and 2045–50). In reality, this value is likely to understate the amount of real depreciation required in the earlier periods because it does not seek to smooth out recovery over those periods to reflect the decline in demand. Nor does it recognise that real depreciation will need to increase over time to recover new capex incurred.

relative to our efficient building block costs reflected the difference between what JGN recovered over the 2015–20 period under interim tariff undertakings and the revenue the AER approved in its remade decision.[36]

Box 1: Handback of over-recovery in the 2020-25 period

Following the release of the AER's Final Decision on our 2015 Plan, we appealed some aspects of the AER's decision. As a result of these proceedings, the AER's decision was set aside. Following a subsequent appeal by the AER the decision was remitted back to the AER to be remade.

Throughout 2017-18, we worked closely with the AER, the AER's Consumer Challenge Panel, and customer advocates to develop a proposal to resolve all outstanding matters on the remittal as quickly as possible, to deliver an outcome in the long-term interests of consumers. On 28 February 2019, the AER remade its Final Decision on our 2015 Plan.

In the absence of a Final Decision on our 2015 Plan, for the years 2016-17, 2017-18 and 2018-19, our prices were set using interim arrangements, with imperfect knowledge of the eventual outcome of the appeals and remittal process. A consequence of these interim arrangements was that our network charges for these years were higher than the AER's remade decision of 28 February 2019. This meant that we collected revenue above what would have occurred had the remade decision been in place from the outset of the 2015-20 period.

Noting that the remittal was only finalised in February 2019, there would only have been one year remaining in our 2015 Plan period in which to make the revenue adjustment. In order to avoid the significant price volatility this adjustment would cause, we worked closely with the Australian Energy Market Commission, the AER and consumer groups to develop a new rule in the National Gas Rules which allowed the AER to smooth the return of revenue to customers into our 2020 Plan period.

The new rule enabled the AER to make an adjustment determination to our 2015 Plan building-block revenues and offset them against those in our 2020 Plan. On 28 February 2019, the AER made an adjustment determination. The adjustment determination lowered our 2020 Plan building block revenues by $203 million ($169 million in $2019-20)[37]—we refer to this revenue adjustment as 'the handback' throughout this document.

The handback resulted in price path set by the AER for the current period that was lower than the price path to recover our actual efficient cost of supply.

The AER in its 2022 Gas network performance report notes that:

> *JGN's revenue reduction is materially influenced by a downward adjustment of $169 million ($ Jun 2020) over its 2020–25 access arrangement period to correct for an overcompensation provided to it previously.* [38]

Therefore to apply any real price path targeting approach requires setting the starting point to an efficient level by removing the downward adjustment to our cost of supply included over 2020-25 period.

Figure 3–1 above shows how this prior AA period adjustment materially reduced our allowed revenues below efficient costs. By 2024-25 this difference was projected to be $43 million if we applied the AER's default PTRM smoothing to the JGN's 2020-25 PTRM without the handback. We have provided an illustrative 2020-25 PTRM[39] that shows how the 2024-25 revenue needs to be adjusted to apply the real price path approach to improve comparability with the Victorian gas businesses (that did not have the handback in their starting point for measuring price path).

36 See AER, Overview | Draft decision – Jemena Gas Networks (NSW) Ltd Access Arrangement 2020-25, Nov 2019, section 4.6.1.

37 AER, Final decision - Jemena Gas Networks adjustment determination, February 2019.

38 AER, Gas network performance report, December 2021, pp. 38–40

39 The illustrative PTRM is provided in the appendix *JGN – Att 7.2A – Illustrative 2020-25 PTRM excluding revenue handback – 20250115*

Applying the zero real price path to an unadjusted 2024-25 revenue would create a price rise of at least 4.2% moving into the 2030-35 period

Not creating future price shock should be an aim of the AER's price path decision. Indeed it is an obligation in the NER rule 6.5.9(b)(2) which requires that the X-factor (i.e. smoothed price path):

> *must be such as to minimise, as far as reasonably possible, variance between expected revenue for the last regulatory year of the regulatory control period and the annual revenue requirement for that last regulatory year*

The AER acknowledges that this is also its aim in gas decisions with a target building block to smoothed revenue variance of +/–3%. The AER's draft decision relevantly states that:

> *By smoothing revenue we also aim to minimise price volatility between and within access arrangement periods by keeping the difference between smoothed and unsmoothed revenue in the final year of each period as close as possible, and to provide price signals across tariffs that reflect JGN's underlying, efficient costs of providing services. Our standard approach has been to keep a divergence of up to +/–3% between the smoothed and unsmoothed revenues for the last year of the period if this can achieve smoother price changes across the access arrangement periods.*
>
> *For this draft decision, we approved lower revenues than JGN's proposal. This is mainly driven by our reduction to JGN's proposed accelerated depreciation. However, our draft decision allows for higher revenues than those determined in the 2020–25 period. The rising revenues and declining demand mean that prices are increasing over the 2025–30 period.*
>
> *We have smoothed the increase in forecast revenues to achieve a more stable price path for the 2025–30 period. Consequently, we have relaxed our standard approach to the final year difference between the smoothed and unsmoothed revenues. In the present circumstances, we have determined that the final year revenue difference is about –4.2%. We are satisfied that the draft decision tariff path effectively balances the aims of price path stability within the 2025–30 period and across periods.*[40]

The combination of a deflated launch point and zero real price path is that the AER's draft decision would result in the AER's draft decision price path necessarily triggering a price rise of at least 4.2% moving into the 2030-35 period to realign our revenues with our cost of supply – an outcome which would clearly be counterproductive to the AER's pricing outcome logic.

The AER acknowledges that future demand will be lower and, other things being equal, just resetting our costs to demand will place upward pressure on JGN's prices in 2030-31. The AER should therefore not exacerbate those known future price rises by setting up a compounding 4.2% price rise into the next period.

Departing from its standard tolerance range to an argument of more stable price outcomes contradicts each other in this context and is not in the long term interest of customers. It does not support the AER's claim that it is '*satisfied that the draft decision tariff path effectively balances the aims of price path stability within the 2025–30 period and across periods*' when its decision has effectively compounded future price rises in subsequent periods.

If a real price path approach is retained, the AER must adopt a policy reflective real price path.

3.3.2 A policy reflective price path is needed

The policy information available for the Victoria determination was not more certain than NSW is

The real zero price path is inconsistent with the AER's average real 1.5% price path approach for the Victorian gas distribution networks' 2023-28 AAs based on the policy at the time of those decisions which were made on 2 June 2023.

[40] AER, Overview | Draft decision – Jemena Gas Networks (NSW) 2025–30, Nov 2024, p.13.

We note, contrary to the characterisation in the draft decision, the AER's 1.5% real price path approach was done in 2023 *before* announcement of the following 2024 Victorian policies:

- from 1 January 2024, the Victorian Government has banned new gas connections for new dwellings, apartment buildings, and residential subdivisions requiring planning permits[41]
- from 1 January 2025, the Essential Services Commission's Gas Distribution Code of Practice (updated 1 October 2024) requires gas distributors to impose full upfront charging on customers for new gas connections
- during 2024, the Victorian Government is consulting on a Regulatory Impact Statement (**RIS**) on an appliance ban for rental properties
- in late 2024, the Victorian Government will be consulting on a RIS that would look at electrifying commercial buildings and introducing an end-of-life appliance replacement ban for residential customers.

This makes the policy circumstances of that June 2023 decision not materially different to JGN's from a jurisdictional short-term gas policy perspective. While the legislated net zero emissions targets were likewise set for both jurisdictions.

The lack of a gas connections ban in NSW increases JGN's stranding risk relative to Vic or ACT networks

The current NSW policy settings, together with JGN's NGR connection obligations, mean our asset stranding risk is worse than in jurisdictions that have enacted connection bans. Houston Kemp explains this in Attachment 3.1:

> *The AER considers that jurisdiction-wide bans on new gas connections in Victoria and Australian Capital Territory constitute strong policy signals that likely indicate a limited role for gas networks in those jurisdictions beyond 2050. The AER appears to reason that the absence of such a policy in NSW implies a weaker policy signal regarding the reduced role for gas networks in the state, with governments in Victoria and Australian Capital Territory targeting earlier net zero target dates and stronger interim targets compared to that of the NSW government.*
>
> *In our view, the AER's reasoning has two key shortcomings. First, AEMO's projections suggest that the rate of future declines in residential and commercial gas consumption will be broadly similar across NSW and Victoria. This sits uneasily alongside the AER's conclusion that policy settings in NSW are less indicative of the reduced role for gas networks in the state, on which the AER relies to justify a lower real price growth constraint for JGN relative to Victorian gas distribution businesses.*
>
> *Second, the AER has not closely considered how the requirement for JGN to connect new customers may impact on the likelihood and magnitude of asset stranding risks, as compared to gas distribution businesses in Victoria and the Australian Capital Territory. We find that this obligation magnifies JGN's asset stranding risks relative to those of gas distributors in Victoria.*
>
> *In addition, we find that the AER's zero real price growth constraint does not account for JGN's unique circumstances.*
>
> *Consistent with these observations, there is no sound basis by which the AER would set a real price growth constraint for JGN that is less than the 1.5 per cent constraint applied to gas distribution businesses in Victoria.*[42]

Stronger interim NSW policies would require even more price rises as Ausnet's reopener shows

When the Victorian gas demand reducing policy measures did subsequently transpire, the 1.5% real price path proved to be insufficient as evidenced by:

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41 Amendment VC250 was gazetted on 1 January 2024 and introduces new requirements for the construction of new dwellings, apartments and residential subdivisions that require a planning permit through a new particular provision at clause 53.03.

42 *JGN - Houston Kemp - RP - Att 3.1 - Smoothing cost recovery when gas demand is declining - 20250110 – Public*, p.33.

- Ausnet's reopener application now seeks a real price path of 8.87% per year for the remaining 3 years of the period, which is 6.47% per year (real) higher than the AER had approved before those policies[43]
- The AER's decision that this variation application is not non-material under NGR cl.66(1) which it states was because:

> *We consider that the variation proposal is likely to financially impact the operation of AusNet's gas access arrangement for the 2023−28 access arrangement period.*[44]

JGN's revised proposal of $230 million is aligned with zero real price path and is therefore conservative

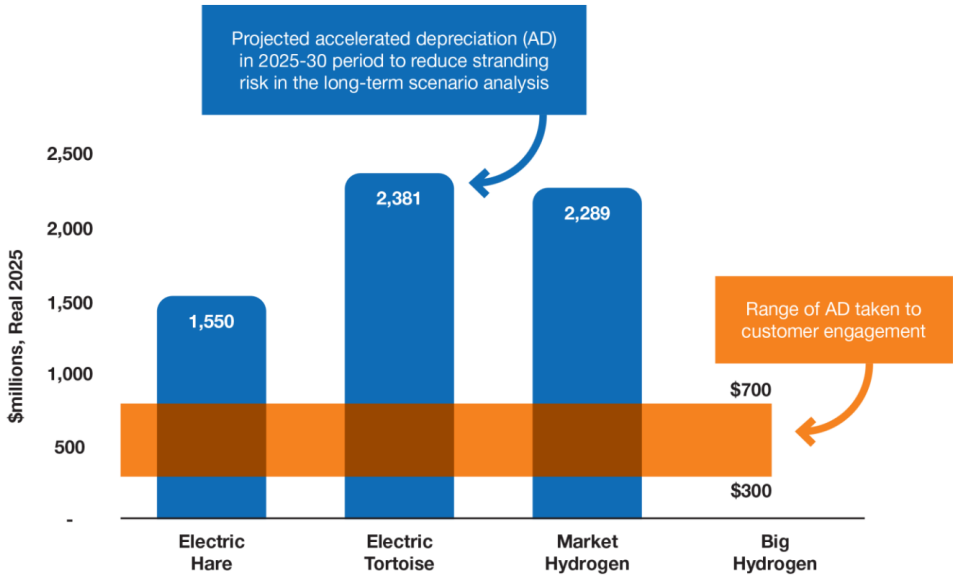
JGN's initial $300m proposal was already calibrated down for the NSW short-term policy status

The draft decision does not account for the fact that JGN's $300 million initial proposal was:

- already calibrated down for the NSW policy status, and
- did not target full RAB recovery by the binding NSW 2050 net zero target date.

As shown in Figure 3-3 we narrowed our accelerated depreciation options (in orange) down from what is needed to keep gas competitive (in blue) across the four Expert Panel scenarios, and were asking significantly less than was needed to recover our investments before 2050. This lower amount is also attributable to our proposed investments in renewable gas connections which complement our proposal to accelerate depreciation, with both initiatives reducing future asset stranding risk, and extending the life of the gas network for our customers.

Figure 3-3: Narrowing our accelerated depreciation options



If greater short-term NSW gas policy certainty did transpire, JGN would be seeking higher 2025-30 depreciation to achieve cost recovery amid that policy (e.g. recovery of JGN's existing investment by 2050 would require depreciation in each AA period from now until then of at least $773 million in real 2025 terms per 5 year period *on average*[45]).

[43] Ausnet, Access Arrangement Information 2024-28 Variation Proposal, 30 Sep 2024, p.4.

[44] AER, Notice of the AER's decision on the materiality of AusNet Gas Services' (AusNet) 2023−28 access arrangement variation proposal, 25 Oct 2024, p.1.

[45] The $773 million was calculated by taking the opening RAB (as at 30 June 2025) of $3.9 billion (from cell J57 of the *PTRM input* sheet of the step 2 PTRM included with the draft decision) and dividing it by the five 5-year regulatory periods up to 2050 (i.e., 2025–30, 2030–

Under AER's price path targeting approach, it is imperative to first adjust the 2024-25 starting point to the cost-reflective level. Following this adjustment, targeting a 1.5% real price path would correspond to an accelerated depreciation of $350 million. In contrast, As **Figure 3–2** shows, JGN's proposal of $230 million aligns with the AER's target of a zero price path if adjusted for the resmoothed 2020-25 revenues or a 1.3% price path if adjusted to our building block cost for that year.

This proposal is therefore conservative compared to AER's decision for Victorian gas businesses. It reflects an acceleration of only 6% of JGN's RAB, compared to 6.1% for the average RAB of Victorian gas businesses, noting that Ausnet is seeking to further accelerate RAB recovery of 9% of its RAB.

35, 2035–40, 2040–45, and 2045–50). In reality, this value is likely to understate the amount of real depreciation required in the earlier periods because it does not seek to smooth out recovery over those periods to reflect the decline in demand. Nor does it recognise that real depreciation will need to increase over time to recover new capex incurred.

4. Other complementary measures

Consistent with our initial AA proposal, we are proposing a suite of complementary measures

A key aspect to our 2025 Plan has been to manage the challenges presented by the energy transition through risk management and innovation. Our revised proposal retains modified versions of the following proposals to complement our capital recovery risk management:

- The proposal for an allowance for renewable gas connections capex has been supported with a fixed principle to make a revenue adjustment to the building block revenue of the next access arrangement period (2030-35) to hand back the 2025-30 revenue the extent that actual capital expenditure for renewable gas connections is less than the amount allowed by the AER (discussed in *JGN - RP - Att 4.2 - Renewable gas expenditure – 20250115*).

- Innovating how we minimise costs through programs like Picarro leak detection services (discussed in *JGN - RP - Att 5.3 - Picarro – 20250115*).