

30 April 2026

Ms. Anna Collyer,
Chair, Australian Energy Markets Commission
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Dear Anna,

AusNet welcomes the opportunity to provide a submission in response to the Australian Energy Market Commission's (AEMC) *Gas Networks in Transition* Directions Paper. We appreciate the Commission's careful consideration of the challenges faced by gas networks and the gas regulatory framework in the context of declining demand, and the importance of the integrity of the fundamental regulatory mechanisms which support investment into essential services in the energy sector.

We support the AEMC's assessment that the rule change proposals on depreciation and capital redundancy would be inconsistent with the revenue and pricing principles (RRP) and could foreclose networks' ability to recover their efficient costs. Further, we welcome the AEMC's confirmation that accelerated depreciation does not constitute a transfer of risk from networks to customers and is an important tool to manage long-term customer interests and promote the National Gas Objective (NGO).

The proposed package of reforms carefully balances adjustments to the existing framework and we support the policy direction outlined. We support the AEMC's proposals to amend the existing capital cost provisions to manage shared risks between consumers and service providers to enable an orderly energy transition. We consider the improved capital cost recovery tools and longer-term planning can better achieve the NGO.

When drafting rules to achieve these reforms, we encourage the AEMC to consider the following key areas:

- Clear guidance on depreciation rules so that networks have reasonable opportunity to recover efficient costs. Without this, incentives to continue to invest where needed and provide pipeline services are impacted, which is not aligned with customers' long-term interests.
- The decision-making models for capital recovery and capital redundancy should have limited regulator discretion, Options B or C(i) described in the Directions Paper, aligned with the conclusion that networks are best placed and incentivised to set depreciation schedules and prices below demand-destructive levels.
- Guidance for the 20-year outlook should be clearly aligned with an outcomes-driven purpose to improve transparency on decision-making by service providers and regulators within access arrangements, in the context a longer outlook. This should not be seen as a 20-year forecast, especially in areas outside of networks' control.
- The tariff reforms proposed are not needed and the proposed position on standalone costs risks undermining the intention of the capital recovery and redundancy reforms.

Recognising that AusNet will be amongst the Victorian gas distribution networks first to apply any new rules from this review, our view is that the direction of the reforms is implementable. The proposed direction is likely to benefit the long-term interests of Victorian customers and should not be delayed.

We appreciate the thorough consultation of the AEMC and are keen to continue engagement through the remainder of the process to apply these reforms in practice for our Gas Access Arrangement Review (GAAR) Proposal for submission to the Australian Energy Regulator (AER) by 1 June 2027. If you have any questions on this submission, please do not hesitate to contact Eliza Cochrane (eliza.cochrane@ausnetservices.com.au).

Sincerely,



Moyo Tian
General Manager, Strategy and Regulation (Gas)
AusNet

Overall direction

Question 1: Our Proposed Package of reforms

What are stakeholder views on our assessment of the proposed direction and how it better promotes the NGO and is consistent with the RPP, in comparison to the status quo and the ECA and JEC rule change proposals?

Question 2: Implementation considerations

1. Do stakeholders consider that there are any barriers to implementing our proposed package of reforms considering the planned publication of the final determination in December 2026? Do you consider some form of transitional arrangements are required for any element?
2. Do stakeholders consider there are any significant implementation costs associated with our proposed package of reforms that the Commission should consider?

The direction of the balanced reform package promotes the long-term interests of gas consumers.

We support the AEMC's approach to make targeted amendments to the rules instead of wholesale changes. Consistent with our response to the consultation paper, we also support the AEMC's intent to ensure more consistent regulatory interpretation and application of existing tools and greater transparency for stakeholders. The AEMC has broadly identified priority areas where regulatory clarification and/or targeted changes to the existing framework would better promote the long-term interest of customers.

We anticipate the implementation of the reform package is feasible for the upcoming Victorian GAAR.

We consider the AEMC has sufficient time to determine a final rule and that this should apply to the next set of Access Arrangement Reviews, the Victorian 2028-33 GAAR. Transitional arrangements are not appropriate given the AEMC's conclusion of the reforms points to early action to manage gas networks under uncertainty, including in the Victorian context, and it would not be in the long-term interest of customers to delay.

While many new requirements would involve greater resourcing from the Victorian networks, they are likely to deliver significant benefit and we intend to include the new directions in our GAAR where practical. If the final rules require larger changes or associated step change in costs, then it may be appropriate to apply these from the Revised Proposal stage in Victoria (i.e. if there are specific details in the 20-year plans that do not materially inform access arrangement decisions) but we consider the AER's assessment on capital recovery and expenditure should align with the new rules.

Longer-term outlook

Question 4: Our proposed direction on a longer-term outlook

1. What are your views on our proposed direction to require service providers and the regulator to consider a longer-term outlook and longer-term consequences?
2. Do you have any views on information or analysis that should be included in a service provider's 20-year

Recognising the intent to provide transparency, we support a long-term outlook with a clear purpose linked to access arrangement decisions.

We support the intent and recognise the benefits of greater transparency on long-term outlook, provided it has a clear purpose and scope. A clearly articulated purpose will be critical to ensure the outlook meaningfully informs regulatory assessment, rather than becoming an imposing regulatory burden with limited value for decision-making or transparency.

- The primary purpose of the 20-year outlook should be to inform why decisions made for a five-year access arrangement are prudent and efficient in context of the longer-term outlook.
- The purpose should not be to specify detailed plans or forecasts over the 20-year horizon for the network.

Clear guidance, aligned with the AEMC's intended purpose, will be required to outline how the 20-year outlook is used within the access arrangement process, including the specific role and expectations of the AER. We encourage the AEMC to consider in the guidance:

- While there should be a degree of consistency across networks, overprescription in the rules risks the scope not remaining fit for purpose over time and could lead to unnecessary regulatory burden.
- A clear, principles-based specification in the rules would best allow service providers appropriate discretion to develop an outlook which supports decisions relevant for their jurisdiction and network.
- The long-term outlook should limit inappropriate reliance on assumptions about factors beyond a service provider's control, such as wholesale prices and government policy settings.

There is clear decision-making value in long-term demand scenarios to inform depreciation schedules and expenditure plans over the 5-year access arrangement. We note many of these outputs have been considered and provided by networks in recent access arrangements (including AusNet's 2023-28 Proposal). Nonetheless we see the value of specifying transparency in the rules to support stakeholders being better informed to engage with and interpret information across the access arrangement process. Specifically, we support improved transparency around how both service providers and regulators have:

- Determined capital recovery decisions given the uncertainty across long-term outlooks, and how this decision impacts the ability and incentive for service providers to efficiently provide and invest in pipeline services over the outlook period.
- Assessed expenditure is prudent and efficient within the context of a longer-term outlook.
- Outlined longer-term risks facing networks and customers and how these have been addressed across the access arrangement, including identifying limitations of the regulatory framework which may need to be addressed to resolve the risks.

On long-term demand forecasts, the AEMC must consider that demand is reactive to network pricing. As such, demand forecasts used for the purposes of informing depreciation schedule decisions should be endogenously linked to resulting network prices. Using exogenous demand forecasts to describe long-term demand scenarios that inform depreciation schedules – and resulting network prices – could trigger customer price reactions counter to the long-term outlook.

Notwithstanding this point, we see a role for qualitative alignment with externally available forecasts such as AEMO's ISP or GSOO to support stakeholders' understanding of the high-level context of a long-term scenario (e.g. 'high electrification' or 'slow electrification'). We are keen to engage with the AEMC on how to balance these two considerations in practice.

The long-term outlook should not be considered a forecast.

It is also important that the 20-year outlook is not treated as a prediction of the future. Given the inherent degree of uncertainty over longer horizons for technology, policy and demand trends, the outlook should instead present plausible scenarios which help inform current regulatory decisions. This supports the purpose by showing how service providers have considered the potential long-term consequences of choices made in the upcoming period, rather than using the long-term outlook to forecast outcomes that are highly uncertain and largely outside the control of service providers.

However, we reiterate that forecasts over an access arrangement period contain considerable uncertainty and therefore there is diminishing value in providing detailed building block, expenditure or tariff forecasts for a longer 20-year period. While service providers can indicate a directional view under plausible scenarios, detailed modelling to support decisions outside of the access arrangement period should be out of scope. For example, if decommissioning planning is not within the scope of the framework, we consider any detailed analysis or modelling should be considered through alternative processes (e.g. jurisdictional requirements).

Without expanding the scope or purpose, we consider the 20-year outlook can also act as a useful input for other stakeholder processes, including government and electricity network planning. We support broad alignment with longer-term planning requirements for electricity network, where practical. In principle, a longer-term outlook will help ensure that regulatory determinations made for a five-year period are consistent with outcomes that promote efficiency and the long-term interests of consumers, and improve coordination between gas and electricity planning, and inform government policy.

Capital cost recovery & redundancy

Question 5: Our proposed direction on capital cost recovery

1. What are your views on our proposed direction for capital cost recovery tools in the NGR?
2. Do you have any views on the decision-making model options explored for:
 - a. depreciation and treatment of inflation?
 - b. redundant capital provisions?
3. In relation to our proposed direction for redundant capital, do you have any views on:
 - a. the materiality threshold that should apply to partial redundancy?
 - b. the constraints that could apply to the regulator's use of partial redundancy?

We support the AEMC's direction on capital cost recovery rules to provide opportunity for service providers to recover efficient costs.

We support the AEMC's proposed direction on capital cost recovery tools and consider the AEMC has substantively considered the risks within the current framework as gas networks transition. The AEMC recognises that use of accelerated depreciation is key tool which can enable efficient capital recovery, particularly where networks are facing stranding risk but have significant customer numbers today.

We echo the AEMC's characterisation of the current challenges around applying efficient accelerated depreciation and support the AEMC's recognition that limited flexibility in short-term price changes prioritises short-term interests of current customers at the expense of customers' long-term interests. We therefore support the AEMC's rejection of the ECA and JEC's characterisation of accelerated depreciation as a transfer of risk to customers when it is instead represents a tool to better balance customers' long-term interests, and the AEMC's conclusion that these alternatives are inconsistent with the RRP.

Guidance on the depreciation rules should create clear objectives which protect the long-term interest of consumers.

We support the AEMC's direction to provide further guidance on depreciation which recognises that the current application would likely, in the long-term, not provide service providers sufficient opportunity to recover our costs nor balance short- and long-term customer interest aligned with the NGO and RPP.

The AEMC should explicitly clarify in the rules that depreciation schedules are to be designed to:

- **Maintain reasonable opportunity for networks to recover costs.** New and previous capital investment which is deemed prudent and efficient must be given reasonable opportunity to be recovered.
- **Maintain incentives for network investment necessary to provide ongoing service.** If decisions around depreciation schedules do not reflect reasonable opportunity to recover costs, service providers will face perverse incentives discouraging service providers to continue to invest where needed, and ultimately to continue to provide the network service even if demand remains.
- **Subject to the above, enable price stability over time given demand over the remaining life of the pipeline.** Where networks face declining demand, it is becoming increasingly important to consider impacts of longer outlooks for demand when determining how particular depreciation schedules will impact price volatility over time.

As noted by the AEMC, service providers are well-placed to design a depreciation schedule which promotes the long-term interests of consumers. There is a strong incentive for service providers to balance long-term risk reduction with short-term price increases, as the latter sends price signals which could trigger an early exit of our customers and increase economic asset stranding risk. Based on these incentives and the conclusion that service providers are in the best position to make decisions on balancing risks, we therefore encourage the AEMC to also consider Option B as the decision-making model for depreciation. If Option B is not preferred by the AEMC, we support Option C(i), where the regulator can only reject a depreciation if it is inconsistent with NGO and RPP. Option B or C(i) would require a strong burden of proof and greater transparency how depreciation has been designed to enable network services over the outlook.

In addition, we support the proposal that service providers should have flexibility in treatment of inflation, specifically whether they elect an indexed or un-indexed regulated asset base (RAB). As recognised by the AEMC, service providers are well-placed and have a strong incentive to appropriately balance the risks and

trade-offs of indexation and both options are equivalent in net present value terms. We support limited regulator discretion for determining when a service provider can recover compensation for inflation (Option B).

While we appreciate the AEMC's recognition that upholding the recovery of efficient costs is a key component of the framework and are supportive of the direction on capital recovery, we note that these amendments will not eliminate all risks to capital recovery. Risk remains both due to the historic application of the rules and may not be fully mitigated by future application of depreciation schedules, particularly if demand declines faster than forecast. This risk is heightened in jurisdictions where governments further determine the speed and long-term future of reticulated gas through policy.

The capital redundancy mechanism should be a tool of last resort.

We support the AEMC's characterisation of the capital redundancy mechanism as a tool of last resort. While we note that the current challenges faced by gas networks are not what the mechanism was intended to manage, we recognise AEMC's intention for the redundant capital provisions to be amended to capture a scenario of economic redundancy, where full capital costs cannot be recovered from a remaining customer base. This scenario is distinct from physical redundancy.

We disagree with the AEMC's position that service providers do not have an incentive to identify the level of asset value which is redundant, and the AEMC's position this may be a reason for more discretion for the regulator. Similarly to depreciation schedules, service providers have a strong incentive to set prices to increase the likelihood of the customer staying connected to the network and hence provide greater opportunity to recover some of our costs.

AusNet understands the AEMC's intention is to provide an additional last resort customer protection measure for the regulator to make capital redundant where the regulator determines a service provider has not already reduced their prices accordingly, which would be contrary to our incentive to retain customers. If the rules are drafted this way, we consider a higher level of regulator discretion is unlikely to have material impact on the amount of capital which could be recovered.

However, if the rules do not explicitly recognise this limited application which we believe is the intent, then we strongly do not support broad discretion for the regulator on capital redundancy proposals. Higher levels of discretion may lead to a scenario which prematurely determines a price different to the service provider's view of the prices required to avoid inefficient price-driven customer exits from the network.

The mechanism to re-add redundant capital into the RAB provides little comfort in this scenario. We consider the scenario where networks see demand fall steeply enough to warrant value removed from the RAB, but later experience sufficient demand to re-add value is relatively unlikely. While the mechanism to re-add capital should exist, its inclusion does not mitigate the threat a capital redundancy provision with significant regulatory discretion poses to the regulatory compact.

We therefore support a decision model with limited regulatory discretion (Option B or C(i)), where the regulator has a strong burden of proof to deviate from a service provider's position.

Practically, we propose the below guidelines for the draft rules to achieve the AEMC's intention:

- **The rules should be drafted to reflect economic redundancy.** While the original intent of rule 85 was not to address the economic asset stranding challenges faced by gas networks today, given the AEMC's direction on reforming the rules we question whether it is useful to refer to "partial redundancy". The definition should relate to the value which is economic redundant, rather than be linked to utilisation or demand metrics.
- **The rules should define the objective of the redundancy provision and include clear, simple criteria** of when capital should be removed or added back. This will limit the application to adjustments which are necessary as a last resort when capital is unrecoverable. As we consider service provider's incentives will be aligned with the objective of the redundancy provision, sufficient clarity is essential to avoid ambiguity when the rules are applied by regulators.
- **Redundancy should be ex-post only** and reflect the revealed value which has become redundant. There is no clear benefit but clear risk in ex-ante capital redundancy. Provided that the direction of the AEMC is to effect, through capital redundancy, what a prudent service provider would do (i.e., charge below the regulated price cap), ex-post redundancy is the best way to achieve this purpose.

These proposals are in line with the conclusions in Section 3 and 5 of Incenta report: *Analysis of the AEMC's Proposals for Capital Recovery*¹

¹ Attachment B to ENA submission to the Directions Paper
AusNet Gas Services Pty Ltd (ABN 43 086 015 036)

Expenditure

Question 6: Our proposed direction on expenditure

1. What are your views on our proposed direction to amend the NGR capex provisions? For example:
 - a. Clarifying that service providers must justify all capex through a quantitative assessment of all credible options that support the provision of regulated pipeline services.
 - b. Amending the justification for safety-related capex to be necessary for the safe operation of pipelines and use of services in NGR rule 79(2)(c)(i).
 - c. Amending the justification for capex to maintain capacity to meet forecast (instead of existing) demand for services under NGR 79(2)(c)(iv).
2. What are your views on the need for the NPV test in rule 79(2)(b)?
3. What are your views on our proposed direction to amend the NGR opex definition?

The proposed changes to tighten existing expenditure criteria are in line with best practice under the existing rules.

We generally support the approach outlined by the AEMC on reforms to the expenditure criteria. We recognise in the context of declining demand it is more important to minimise expenditure to what is necessary for safe and reliable network. While service providers already have incentives to minimise expenditure to reduce economic asset stranding risk, improving transparency for stakeholders of network's expenditure proposals and AER assessments will help their understanding of the proposals.

While we maintain that the proposed changes broadly reflect best practice under the existing rules, we consider the following changes appropriate:

- Requiring networks to provide a quantitative assessment of all new capex. We note current expectations and the uncertain demand outlook implicitly requires a high threshold of evidence and is likely this change would largely replicate the application of current rules, but we understand the intention of the AEMC providing additional clarity in the rules, provided these remain practical and proportionate to the materiality of the expenditure.
- Given the connection charges are now charged upfront in Victoria and across jurisdictions, we consider the NPV test in rule 79(2)(b) has limited practical value. At the same time, we do not expect material benefits for consumers from its removal.
- Removing references in the opex criteria to increasing long-term demand. We consider there is no benefit in expenditure criteria in the rules specifying if demand is increasing or decreasing, as expenditure should align with meeting forecast demand for reference services.
- Requiring explicit links between proposals and expenditure drivers in the Rules.

Considering their practical implementation in our access arrangements, the following changes have limited benefit for stakeholders and we do not support them:

- The amendment to the criteria for safety expenditure provides limited practical value and is not required. There is sufficient flexibility under either the current or AEMC's proposed drafting to ensure expenditure is minimised to only what is necessary. As the AEMC noted in its response to Q&A in its public forum on the Directions Paper, this requirement would also be superseded by jurisdictional safety requirements which often cite "as low as reasonably practicable" measures.
- We understand the intent of the AEMCs change to rule 79(2)(c)(i) from meeting existing levels to meeting forecast demand is to ensure networks do not incur unnecessary expenditure or overbuild capacity in the network given long-term demand uncertainty. We consider changes to this rule will have limited practical value as capacity-driven augmentation of the network would be justified under rule 79(2)(a) and forecast demand will likely be a key input for quantitative assessments justifying expenditure to meet levels of demand regardless (e.g. reliability expenditure would consider demand over the period).

We appreciate the clarity from the AEMC that the proposed rule changes related to non-pipeline alternatives would be out of scope of the NGR. However, we note that changes to the NGL required would be in the long-term interests of gas customers if through the transition non-pipeline alternatives (in a given location) are lower cost to the service provider than providing pipeline services.

Similarly, while we recognise and support the AEMC's commitment to the timeline for this reform package and the limited time to review a decommissioning framework within that period, further work on decommissioning will be required across some jurisdictions. Both non-pipeline alternatives and decommissioning should be considered in future reviews, in conjunction with any decisions on the long-term policy direction for gas networks which rightly sit with governments.

Tariff arrangements and incentives

Question 7: Our proposed direction on tariff arrangements

1. What are your views on our proposed direction for amending the reference tariff arrangements?
2. What are your views on our proposal to provide guidance on applying the concepts of long run marginal cost, standalone and avoidable costs?
3. What are your views on our proposal to require service provider and the regulator to give greater consideration to customer impacts in setting tariffs and tariff variation mechanisms?

Question 8: Incentive mechanisms

1. Having regard to our proposed direction, do you consider there is a need for additional or modified incentive mechanisms for service providers?

We do not support the direction of the AEMC's proposed changes to reference tariffs, particularly in relation to stand alone costs.

We are broadly supportive of the AEMC's intention to require greater consideration and transparency on tariff arrangements. However, we consider any specific requirements which may increase regulatory burden on service providers should be carefully weigh up the benefits and regulatory costs. Taking into account the variability in networks customer bases and long-term outlooks, we consider any new rules should be principles-based to avoid regulatory burden which may not be fit for purpose over time.

The lower and upper bound constraints in Rule 94 under which total revenue is allocated across tariff classes serve a clear and narrow purpose: to prevent unreasonable cross-subsidisation between customer classes by ensuring that no class contributes materially less than its avoidable cost, or more than its stand-alone cost of provision. We agree with the AEMC's position that long run marginal cost should only be considered where relevant, which may be less valuable for certain networks, especially those in decline.

The AEMC's proposal to reinterpret upper bound stand-alone costs as a switching price tied to alternative energy sources departs from the intent of the framework. In practice, this interpretation would mandate a cap on reference tariffs without a link to costs of providing the service. First, this would remove the essential link between the cost-based total revenue determination and tariff-setting. It would require determining hypothetical switching prices for customer classes despite wide variation in appliances, usage profiles and technical constraints and without any clear relationship to the service provider's efficient costs. We also do not consider it possible to implement this in a robust, evidenced way.

Second, it would materially increase stranded asset risk by limiting recovery of tariffs aligned with the use of capital recovery tools to bring forward depreciation to match the expected economic lives of assets. This would likely result in systematic under-recovery of revenue, particularly under scenarios where assumptions in the switching cost calculation change rapidly and are outside of the service provider's control (for example, gas and electricity wholesale price shocks). This would undermine service providers' long-term ability to provide pipeline services and we consider the proposed direction is inconsistent with the National Gas Objective and the Revenue and Pricing Principles.

This position is in line with the conclusions in Section 6 of Incenta report: *Analysis of the AEMC's Proposals for Capital Recovery*¹.

We support improved transparency around decisions within the current tariff variation mechanism framework.

We support the AEMC's position that no changes or additional prescription in the Rules is required to design and approve tariff variation mechanisms. We consider the current framework provides sufficient flexibility to remain fit for purpose to accommodate different network characteristics over time, provided the need for consistency between networks is loosened to allow the decision to reflect jurisdictional circumstances. We support improved

transparency around the short- and long-term customer and network impacts of changes to the tariff variation mechanism. While this has been sufficiently considered to date it is likely to become increasingly important through the transition.

Existing incentive mechanisms are fit for purpose.

We do not consider there is need for additional incentives. The current incentive schemes provide sufficient coverage and flexibility for networks and the regulator to adapt parameters as needed to return efficiencies for gas network customers. In addition, we consider implicit incentives to minimise expenditure due to economic asset stranding risk add additional sufficient incentive beyond the expenditure schemes.