ENERGY CONSUMERS AUSTRALIA

Directions paper

Gas Networks in Transition

Energy Consumers Australia's submission to the Australian Energy Market Commission

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Energy Consumers Australia is the national voice for household and small business energy consumers. We advocate for a fair, affordable, and reliable energy system that meets everyone's needs and leaves no one behind on the journey to net zero.

Feedback on *Gas Networks in Transition* directions paper

Energy Consumers Australia (ECA) welcomes the opportunity to respond to the Australian Energy Market Commission's (AEMC) directions paper regarding the proposed rule change requests by ECA and the Justice and Equity Centre (JEC).

To genuinely protect the long-term interests of Australian households and small businesses, the regulatory framework must evolve. The energy transition is fundamentally challenging the ability of the current framework to address the risks that consumers face as gas demand declines. The rules governing gas networks must reflect this shift.

The regulatory framework was designed for a growing network. This no longer reflects reality, as residential and commercial gas use is falling. The Australian Energy Market Operator has forecast a 79% demand reduction by 2045.[1] Consumers are exposed to growing costs, risks and inequities as demand declines and networks seek to recover costs from a shrinking pool of gas consumers. Cost recovery and network investment rules need to protect consumers in the transition rather than assume consumers should continue to bear the overwhelming share of costs and risks. Planning and transparency are also essential to avoid a disorderly transition.

We welcome the AEMC's recognition that the current regulatory framework may no longer be fit for purpose where demand is declining. We also welcome some aspects of the directions paper, like tightening capital expenditure rules, as a step in the right direction.

However, ECA is deeply concerned with the proposed direction on some of the rule changes, particularly on capital cost recovery, and considers that the directions paper misses the intent of some our original rule change proposals.

The proposed direction would move the dial further towards guaranteeing network cost recovery, rather than prioritising the long-term interests of consumers. It would fail to ensure a fair allocation of costs and risks as demand declines. Indeed, the AEMC says its changes "would mean that today's gas consumers face higher prices".[2] Ostensibly this is to protect future generations from even higher prices. Yet framing this issue as being only about balancing costs between different generations of consumers – rather than about fairly sharing costs and risks between consumers and networks and their investors – misses the point entirely.

In our view the AEMC's assessment and proposed direction depends on a number of assumptions that, as we discuss in this submission, we believe are incorrect and we urge the AEMC to reconsider. These include:

[1] Gas Statement of Opportunities 2026 Gas Forecasting Data Portal, Step Change scenario (Residential and Commercial).
[2] AEMC, Directions paper, 23.

- *The interpretation of the 'regulatory compact'*. In practice, consumers have not made an explicit commitment to fund the future costs of the network to which they are currently connected, only the current costs of being connected, while they remain connected.
- *The assumption that a network's commercial incentives are aligned with the long-term interests of consumers*. The AEMC's proposed direction would effectively impose this assumption, which evidence demonstrates is incorrect, at exactly the time when network incentives and consumer interests are diverging. The draft direction on accelerated depreciation would facilitate networks shifting costs and risks to consumers.
- *Over-reliance on modelling of hypothetical networks*. We are concerned the AEMC is placing too much reliance on its modelling of hypothetical networks to develop and support its position on capital cost recovery. What is more important is to develop rules that will be fair when applied to actual networks. As the modelling we have commissioned on the Jemena and AGN (SA) gas networks demonstrates, accelerated depreciation does little to reduce stranding risks but imposes meaningful costs on consumers.

We also urge the AEMC to further consider more detailed planning and reporting requirements for networks as we have proposed in our rule change. While the proposed long-term forecast would be an improvement on the status quo, the AEMC has rejected our proposal for a Gas Annual Planning Report (GAPR), seemingly based largely on unverified claims of implementation costs. Strategic planning is a basic business requirement for a sector managing $11.8 billion in assets.[3] Without granular data, governments and regulators are unable to coordinate gas decommissioning with electricity grid upgrades, leading to a disorderly and expensive transition that consumers will ultimately be forced to fund.

While we look to the AEMC to make necessary changes to the rules to manage consumer risks in the transition, we also agree with the AEMC that jurisdictional governments have a necessary role to play in the transition and that changes are needed that sit outside the National Gas Rules (NGR). We encourage the AEMC to go further in making specific recommendations to governments on the policy clarity and legislative changes outside the rules that are needed to support the transition.

ECA has also recently released its *Power Move* report highlighting the actions ECA believes governments need to take to support fair and affordable electrification and effectively plan for the future of the gas network.[4]

Thank you for considering this submission. If you have any questions, please contact Claire Ohk at Claire.Ohk@energyconsumersaustralia.com.au.

Sincerely,

Brian Spak

Acting CEO

Energy Consumers Australia

[3] AER, State of the energy market report, 2025, 184.
[4] ECA, Power Move: Fair and affordable electrification for Australian households and small businesses | Energy Consumers Australia.

Responses to Consultation questions

General comments

Ensuring an affordable and orderly transition is the only way to meet the long-term interest of household and small business users in a declining market

The regulatory framework cannot operate under the assumption that consumers possess the financial capacity to fund a managed recovery of legacy assets through escalating prices. We are concerned that the proposed direction, which positions accelerated depreciation as the primary tool to manage asset stranding, effectively shields monopoly businesses from market shifts. This approach, in our view, is inconsistent with the long-term interests of consumers under the National Gas Objective (NGO).

In a transitioning market, delivering genuine benefit means minimising total system costs and providing a safe transition pathway, rather than artificially extending the economic life of existing infrastructure. Simply accelerating costs for consumers is not an equitable answer to how we recover the cost of that infrastructure.

While we recognise that the AEMC does not dictate jurisdictional energy policy, a lack of finalised government policy cannot be a reason for regulatory inaction. The AEMC must maximise the tools it has available right now within the NGR to build protective guardrails for consumers.

Energy affordability limits consumer capacity to absorb transition costs

The urgency of this reform is underscored by the financial pressures facing households who already pay for over 90% of gas network revenue.[5] Survey data demonstrates 50.9 per cent of respondents indicate they are "extremely or quite concerned" about the cost of gas used in their homes and businesses.[6] Furthermore, 33.4 per cent of people report finding it "quite or very difficult" to pay their gas bills in the last six months alone.[7]

Relying heavily on accelerated depreciation to manage stranding risk will likely trigger the price shocks the AEMC aims to prevent. To protect the long-term interests of Australian households and small businesses, the regulatory framework must pivot from network preservation to fairly managing gas network decline. This requires stopping unnecessary spending, sharing transition costs fairly between investors and consumers, and mandating the transparency needed for a coordinated energy transition.

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?

ECA appreciates the AEMC's attempt to take a holistic approach to these reforms. However, the AEMC should review its assessment that the proposed direction better promotes the NGO and aligns with the Revenue and Pricing Principles (RPP) more effectively than our original rule change proposals. We have outlined our views on the proposed direction in more detail in response to the specific questions later in the paper.

[5] e.g. AER, Gas Network Performance Report, 2022, 107, Figure 7-9.
[6] ECA, Consumer Energy Report Card (CERC), Dec 2025.
[7] Ibid.

In short, we consider that:

- **Long-term planning:** the proposed direction is an improvement on the status quo but falls well short of our rule change proposal, which we consider would better meet the NGO and RPPs (see response to **Q4**).
- **Capital expenditure:** the proposed direction is a significant improvement on the status quo. Including our additional proposals would further strengthen the rule change consistent with the NGO and RPPs (see response to **Q5**).
- **Capital cost recovery:** the proposed direction on accelerated depreciation is worse than the status quo. In our view it would be harmful to the long-term interests of consumers. Our rule change proposal would better meet the NGO and RPPs and improve on both the status quo and the AEMC's draft direction. The proposed direction on capital redundancy is an improvement on the status quo but would be improved by removing proposed restrictions on its use (see response to **Q6**).

We believe the AEMC's assessment is based on a flawed interpretation of the long-term interests of consumers and fails to address the structural divergence between network incentives and consumer outcomes, instead incorrectly assuming strong alignment between the incentives of gas networks and consumers' interests.

Our rule change requests were designed to address a structural disconnect in the gas market: a regulatory framework built for growth and expansion being applied to a network in decline. Genuinely promoting the NGO requires a framework that ensures the costs and risks of this transition are shared equitably, rather than shifted entirely onto households and small businesses.

Shifting costs and risks onto consumers does not promote their long-term interests

The NGO requires the regulatory framework to promote the long-term interests of consumers. The AEMC argues that its direction meets this goal by balancing current price impacts with the interests of future consumers. However, with households and small businesses already struggling to pay for their gas bills, any changes that intentionally increases prices today without requiring any conditions to protect consumers from the cost of stranding gas networks does not meet this criterion.

The AEMC disputes that accelerating capital cost recovery shifts costs and risks onto consumers. Instead, the AEMC considers its direction promotes intergenerational equity. The only costs and risks to be shared, on this view, are between different generations of consumers. This is a flawed argument that ignores the reality of declining gas demand. Because residential and small business gas demand is in decline the shift is not between generations of consumers. It is asking today's consumers to reduce the losses that network investors face in the future.

It is not feasible to guarantee full network cost recovery. In reality, a network in structural decline faces the risk that its capital base will never be fully recovered because the market for its product and services is disappearing. By allowing networks to front-load capital cost recovery now, the regulatory framework is not balancing costs between generations but using the "stickiness" of captive consumers,[8] such as those who lack the choice to electrify, to guarantee a return for investors. This effectively transfers the costs of a declining network from networks' shareholders to its current gas consumers. Rather than promoting equity, this approach creates a regulatory shield that protects the terminal value of assets at the expense of current energy affordability.

[8] AEMC, Directions paper, 124.

On planning requirements, the AEMC's proposed direction does not adequately engage with the benefits to consumers from a well-planned and managed transition, and the information and reporting that is necessary to enable one. This is despite the directions paper repeatedly warning of the risks of a 'disorderly energy transition.' The AEMC heavily weights unverified claims that better planning and reporting will impose unmanageable cost burdens on gas networks yet does not adequately consider how these requirements could support better planning that would, in our view, be clearly in the long-term interests of consumers.

The RPPs do not guarantee full cost recovery for networks

The AEMC acknowledges that the RPP does not guarantee full cost recovery but a reasonable opportunity to recover their efficient costs.[9] Yet the proposed direction on accelerated depreciation is heavily weighted towards guaranteeing network cost recovery.

The 'reasonable opportunity' to recover costs needs to be considered in the context of the energy transition and declining gas demand. It cannot simply be assumed that consumers can, or should, bear the costs and risks of asset stranding that could reasonably have been foreseen for some time.

There is some recognition of this in relation to the AEMC's proposal to amend the redundant capital provisions.[10] The AEMC asserts that its proposed direction replicates the outcomes of a "workably competitive market" as described in Box 3 of the directions paper.[11] While we support this direction, we are concerned that this principle is not being applied consistently to the assessment of the other rule change requests. We contend that the AEMC's proposed direction on depreciation achieves the exact opposite.

As the gas network declines the costs need to be shared fairly between consumers, network investors, and taxpayers. While decisions about cost sharing and the 'endgame' of household gas networks involve broader policy questions for government that may be outside the AEMC's remit, the AEMC should not presuppose the outcome by front-loading costs onto a consumer base that is already bearing the overwhelming share of costs and risks.

Genuinely promoting economic efficiency in a declining demand scenario requires that network investors bear a fair and proportionate share of transition costs. Our original rule change request aligns more closely with the RPP because it makes capital recovery contingent on robust consumer protections that aim to ensure consumers are not bearing an unfair share of these costs through the transition. This ensures that the reasonable opportunity to recover costs is balanced with an effective incentive for the business to manage its assets prudently as the market declines. This is the only approach currently on the table that provides a fair path forward for all consumers, especially those who do not have the choice to electrify their homes today.

Question 2: Implementation considerations

- 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?
- Do stakeholders consider there are any significant implementation costs associated with our proposed package of reforms that the Commission should consider?

[9] AEMC, Gas networks in transition: Directions paper, 2026, 81
[10] Ibid., 75.
[11] Ibid., 53.

Rule changes should be implemented as soon as practicable

ECA supports the AEMC's timeline for a final determination by December 2026. While we recognise that this creates a compressed timeframe for the upcoming Victorian access arrangement resets, with proposals due to the AER in June 2027, we believe the urgency of the transition justifies this approach.

Victoria represents the largest residential gas market in Australia and is already subject to clear jurisdictional policy signals through the Gas Substitution Roadmap.[12] Applying updated rules, particularly those related to operating expenditure and planning, as early as possible will deliver tangible benefits to consumers. We also recommend our proposed rule changes on accelerated depreciation are applied as soon as practicable, noting Victorian networks proposed a combined $461 million combined in accelerated depreciation in the most recent access arrangement period.[13] Delaying these reforms for another five-year cycle would leave Victorian households and small businesses exposed to inefficient investment and avoidable costs.

We do not believe extensive transitional arrangements are required for the core elements of the package. We recognise some lead time may be required to enable readiness for implementation of some elements of the reform package, e.g. for the types of new planning and reporting requirements we propose. But the urgent need to ensure the rules are fit for purpose for the energy transition should mitigate against any excessive delay.

The AEMC should monitor the consumer outcomes of the reform package

We recommend that the AEMC include plans for monitoring and review of the reform package as part of the implementation. The directions paper relies on modelling of hypothetical networks to determine how real-life networks should be regulated; how they apply in practice and whether they will ultimately be fit for purpose for the transition remains uncertain as much of the transition is uncertain. Therefore, there must be a mechanism to ensure the rules are delivering fair outcomes in practice.

At a minimum, we suggest the AEMC commit to a review of the reform package after 3 years (perhaps timed around forthcoming access arrangement cycles), including to provide a formal vehicle that allow the AER and other stakeholders to provide direct feedback to the AEMC as the rule changes take effect and the transition unfolds. This would ensure the regulatory framework remains responsive to shifting demand and consumer needs. We note the AEMC has proposed, for example, to undertake a periodic review of consumer outcomes in the retail energy market.[14] The need to monitor outcomes for consumers in the transition away from gas is similarly important.

Implementation costs are not likely to outweigh the benefits

We do not consider that the reform package we have proposed, or the AEMC's proposed directions, would impose significant implementation costs on gas networks. (As we later note though the proposed direction on capital cost recovery would impose significant costs and risks on consumers.)

We firmly reject claims that the implementation costs of any of the proposed rule changes we submitted are too burdensome or would outweigh the benefits. We recommend the AEMC carefully scrutinise any such claims from stakeholders and not simply accept assertions that the changes would impose significant costs or burdens.

[12] Victorian Government, Victoria's Gas Substitution Roadmap
[13] AEMC, Directions paper, 56.
[14] AEMC, Pricing Review draft report, 73ff.

For example, the Australian Pipelines and Gas Association (APGA) has estimated that compliance would require 25,000 staff hours annually across the entire sector.[15] As we note in response to **Q4** this figure should be considered an ambit claim. However, even taking this claim at face value, if we assume a standard 1,800-hour work year per employee, this equates to approximately 14 full time equivalent staff (FTE) across the entire Australian gas distribution sector. We do not think it is credible that a sector managing a combined $11.8 billion dollar asset base with thousands of existing staff cannot afford to allocate three staff members per business to conduct long term strategic planning, or that any such cost would not outweigh the demonstrable benefits to the transition as we have outlined in our rule change requests. Greater costs and inefficiencies will arise if the regulatory framework continues to remain out of date and does not require the information and planning that is necessary to effectively manage the transition in the long-term interests of consumers.

We encourage the AEMC to assess the costs and benefits of implementation more rigorously before the draft determination.

Question 3: Application to transmission and distribution

- What are your views on our proposed direction that reforms should apply to distribution and transmission pipelines (where relevant)?

While our rule change has focused on distribution networks, we note the AEMC's observation that declining gas demand could have implications for transmission pipelines and support the AEMC's proposed direction to apply these reforms to both gas distribution and transmission pipelines where relevant or with any necessary modifications, as they are part of a single and interconnected supply chain.

The combined value of the capital bases for scheme pipelines regulated by the AER is approximately $14 billion, which includes $2.2 billion dollars in transmission assets.[16] With the AER and ERA recognising that some transmission pipelines are facing demand risks and have allowed accelerated depreciation,[17] we see it appropriate that reform apply to both types to ensure efficiency and appropriate management of the risks facing consumers is maintained across the entire network, though noting our concerns with the direction of the proposed capital cost recovery rules.

Fragmented rules create a risk that one part of the network is managed for decline while another continues to invest based on outdated growth assumptions. Aligning the rules for both sectors ensures that investment incentives are calibrated to the actual needs of a transitioning market, reducing the risk of consumers paying for assets that are no longer required.

Question 4: Longer-term outlook

- 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?
- Do you have any views on the information or analysis that should be included in a service provider's 20-year outlook?

[15] APGA, submission to consultation, 37.
[16] AER, State of the energy market, 2025, 184.
[17] AEMC, Gas networks in transition: Directions paper, 2026, 62.

ECA is disappointed that the AEMC has not engaged more fully with our proposed rule change to require gas networks to publish an annual planning report. The directions paper underweights the benefits and overweights the costs of such an exercise.

At the same time when the AEMC says electricity network planning tools are upgrading 'from an old street directory to Google Maps',[18] the AEMC does not see fit to meaningfully improve planning requirements for gas networks that are already subject to significantly fewer requirements than electricity networks. Rejecting the proposed rule change as a whole prevents the electricity-gas network system coordination required for an orderly transition and risks forcing energy consumers to fund uncoordinated and inefficient infrastructure investment across both networks.

The AEMC should reassess the benefits and costs of the proposal

We recommend the AEMC more fully assess the benefits and costs of the proposal before proceeding to a draft determination. These have, in our view, not been adequately assessed in the report and the AEMC has too readily dismissed the proposal as being costly or lacking in benefit.

The AEMC states it has been 'unable to identify any stakeholder that would benefit from the publication of such granular information on an annual basis'.[19] As we outlined in our rule change request, such information would be valuable to many stakeholders, including state, territory, and local governments and electricity distribution networks, who could use these insights to deliver a lower cost energy transition overall. This includes to identify opportunities for strategic decommissioning, which the AEMC recognises as needing coordinated action by governments, regulators and other stakeholders.[20]

In a recent discussion, Amy Kilpatrick, CEO of CARE Financial Services, which helps low-income households qualify for electrification funding in the ACT, volunteered her organization's need for more information about which households are connected to gas so that she can help them get the government assistance they need. She was unprompted and unaware of the live rule change request, but stated, "How can we ensure no one is left behind, if we don't know who has gas?"[21]

ECA's contention that there would be material benefits from its proposed reporting requirements is supported by multiple stakeholders in their submission to the AEMC:

- "Improved reporting obligations would support efficient regulatory decisions by providing evidence on utilisation, cost recovery, and transition planning. It would also enable consumers to better understand how networks are managing transition costs and risks."[22]
- "Ensuring that regulation requires network operators to model and disclose utilisation trajectories and to plan for downsizing of network assets will lead to a more transparent and effective planning and pricing system…without planning, under-utilised networks risk stranded assets and rising per-customer costs."[23]
- "While defection from reticulated gas networks is currently occurring on a house-by-house basis, a much more efficient approach in the long term will be to consider strategically decommissioning

[18] Anna Collyer, AEMC proposes enhanced distribution network planning to support local energy solutions | AEMC.
[19] AEMC, Directions paper, 40.
[20] AEMC, Directions paper, v.
[2121] Discussion between Amy Kilpatrick and Brian Spak, 23 April 2026.
[22] Origin, submission to consultation paper, 6.
[23] Climateworks, submission to consultation paper

sections of the gas network at a time. This will require reliable information on the spatial layout of the network, and on the age of specific assets."[24]

- "Mandatory Gas Annual Planning Reports would provide the information needed for regulators, governments, and communities to plan for electrification and manage network contraction in an orderly and fair way. Such requirements would prevent inefficiencies, reduce information asymmetry, and improve accountability across the sector."[25]

These are only a sample of the benefits cited, but it's clear that a wide range of stakeholders see value in greater information reporting than currently exists, and of the type that we proposed. It's unclear why the AEMC has been so dismissive of these points. We urge the AEMC to reevaluate its assessment.

In terms of the costs, most of the claims that the GAPR will be costly are generic in nature. An exception is APGA's claim that it will require 25,000 person-hours of time to prepare.[26] Given the high-level nature of the rule proposal, this is an implausibly firm estimate, and given no supporting analysis is provided, the AEMC should treat this as an ambit claim.

Other cost issues raised by networks include the cost of developing engineering cost estimates (Ausnet) and the difficulty of assigning asset ages to individual sections of the network (AGIG).

While we acknowledge that producing granular, location data requires resourcing, we think the way to address these is to work through the information being sought and the use cases against the costs of providing information at different levels of accuracy and granularity to work out what the practical balance of cost versus quality of information should be. It is not to simply dismiss the proposition out of hand.

The directions paper's assertion that much of the information already exists is simply not the case. And it can't both be true that the information sought is already being published *and* that it would be costly to consolidate that information into an annual report.

What is actually available is some annual historical information (RINs, quarterly disconnection statistics, annual AER report analysing the previous year's outcomes) and a set of projections published every five years as part of the access arrangement process. In neither case is there the kind of locational granularity that would support two key benefits identified in our rule change proposal and by multiple submissions:

- Information about the rate of electrification and the size and location of the resultant new electric load that would inform electricity network augmentation expenditure (augex) requirements, which are locationally specific.
- Information about the most prospective areas for strategic decommissioning, whether based on local interest, rapidly declining demand and/or upcoming repex.

The rule change is necessary to enable long-term gas and electricity network planning

Determining where new demand peaks from electrification are sufficient to trigger an upgrade requires a granular, transparent understanding of activity on both gas and electricity networks. While annual planning reports and other initiatives have recently improved stakeholders' understanding of electricity

[24] IEEFA, submission to consultation paper, 6.
[25] SACOSS, submission to consultation paper, 4.
[26] APGA, submission to consultation paper, 37.

network available capacity, we currently lack visibility on where and how big the new electric loads arising from customers leaving the gas network are.

Other jurisdictions are beginning to implement these types of plans for the same reasons. Up to a point it includes the NEM, where AEMO's system level gas planning is increasingly seeking to integrate gas and electricity planning. Similar initiatives can be found in the UK, Germany[27] and the Netherlands.[28] While these jurisdictions typically start with transmission-level planning, they are moving to more granular approaches, such as the UK's Regional Energy Strategic Plans.[29] A more bottom-up approach has been trialled in California, based on identifying prospective areas for strategic gas network decommissioning.[30]

For clarity we consider that our proposal is useful on its own terms as well as being a potential first step towards more integrated gas and electricity planning but is not predicated on that end goal. Similarly, we recognise the AEMC's statement that it is not in a position to develop a strategic decommissioning framework, but that is no reason to fail to progress rule changes for the publication of the kind of information that would be a necessary precursor to developing a decommissioning project.

As well as being insufficient for the purposes cited by respondents to the consultation paper, the format of existing information is often hard to engage with: "Where information is published, it is often inaccessible, located among hundreds of documents and spreadsheets submitted to access arrangements – much of it redacted."[31]

The increasingly uncertain outlook for gas demand, and the interaction with national and jurisdictional policy decisions means that the five years between access arrangements is too long a time frame. This is evidenced by AusNet's request for a reopener of its 2023-28 Access Arrangement "in response to new policy announcements by the Victorian Government since the AER's final decision on its 2023-28 access arrangement period."[32] This resulted (in Ausnet's view) in "material changes in long-term outlook."[33] The fact that the AER ultimately determined the request did not meet the specific criteria for a reopener in no way undermines the point that expectations can change materially between access arrangements.

Ausnet also cite two of their initiatives that entail voluntary engagement with stakeholders:

a) "Voluntary consideration of new approaches to further minimise capital expenditure, through our trial to avoid a gas augmentation in the township of Ballan"[34] - this belies the claim by other networks that there is no scope to consider demand management.

b) "We are working with our stakeholders, including government and regulators, to voluntarily publish network data to support innovation and transparency applicable to the policy settings and the pace of the transition in Victoria.[35]

We commend AusNet for both these initiatives. Unfortunately, not all networks are similarly accommodating, with Rewiring Australia noting that they "sought to engage the local gas distributor on

[27] ReGlobal, Germany's 2025 NEP: Adapting grid planning to new market conditions, 2026, available at: https://reglobal.org/germanys-2025-nep-adapting-grid-planning-to-new-market-conditions/
[28] https://www.publicatiesgasunie.nl/en/2024-annual-report/we-are-gasunie
[29] National Energy System Operator, Regional Energy Strategic Planning, available at: https://www.neso.energy/what-we-do/strategic-planning/regional-energy-strategic-planning-resp
[30] Grid Works, Strategic Pathways and Analytics for Tactical Decommissioning of Portions of Gas Infrastructure in Northern California, 2023, available at: https://gridworks.org/wp-content/uploads/2023/06/Evaluation-Framework-for-Strategic-Gas-Decommissioning-in-Northern-California-Interim-Report-for-CEC-PIR-20-009.pdf
[31] Brotherhood of St Laurence, Submission to consultation paper, 6.
[32] AusNet, Submission to consultation paper, 11.
[33] Ibid
[34] Ibid. 12.
[35] Ibid, 12.

several occasions to discuss coordination, planning and access to network data. Despite multiple requests, we received no response and were unable to access basic network information such as gas connection maps."[36]

We agree that a longer-term outlook can be valuable providing it is appropriately scoped. In practice, once the outlook moves beyond a five-year horizon it is likely to be predicated on projecting out existing trends and/or some broad assumptions about future changes. This is still useful to the extent it can provide stakeholders with some understanding of how fast their network costs will increase and when their local network may become economically stranded. However, the outputs will be heavily dependent on the assumptions and the AEMC must consider the risk of bias if undue discretion is given to the networks to choose their assumptions. One option would be to require them to use AEMO's planning assumptions where relevant, while another would be to empower the AER to set the terms on which assumptions are made.

In summary, while we consider the AEMC's proposal is a step in the right direction, it remains wholly inadequate to deliver the very real benefits outlined in stakeholder submissions. We urge ongoing dialogue between the proponents and other supportive stakeholders, the AEMC, the AER and networks to find a way to deliver these benefits at a proportionate cost.

Question 5: Capital cost recovery

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

We do not support the proposed direction on accelerated depreciation

ECA welcomes the AEMC's identification of the need to clarify the use of the capital cost recovery tools in the NGR, but we have significant concerns with the proposed direction. Despite rule change proposals from both ECA and JEC seeking to limit the use of accelerated depreciation, the AEMC's draft direction would seemingly encourage greater and more frequent use of depreciation. Indeed, the AEMC acknowledges that its proposed direction 'may result in more capital recovery being brought forward and today's gas consumers facing higher prices'.[37]

Without seeking to restate our original rule change proposal, we remind the AEMC that the costs and risks to consumers arising from use of accelerated depreciation arise from *actual* network proposals which impose real costs on consumers today. As the AEMC notes these proposals across the most recent access arrangement periods have been in the region of $900 million across all networks.[38] While it is useful for the AEMC to conduct modelling as a theoretical exercise, modelling based on a hypothetical network that bears little relation to any real network is not a sufficient basis for the AEMC to conclude its reform package is in the long-term interests of consumers.

[36] Rewiring Australia, submission to consultation paper, 4.
[37] AEMC, Directions paper, 43.
[38] AEMC, Directions paper, 56.

Accelerated depreciation increases bills without meaningfully reducing stranding risks

In addition to the analysis of the Jemena gas network, we highlighted in our rule change proposal,[39] more recent modelling on the South Australian gas network further reinforces that accelerated depreciation increases bills without meaningfully reducing the risk of stranded assets.[40] AGN SA's depreciation proposals would see consumers paying $170 more over the 2027-2031 period and reduce the RAB by only 2.8 per cent over that period.[41] In the context of affordability pressures, this significant impost on consumers results in an insignificant reduction in the RAB. Under the AEMC's proposal, these future costs would still need to be paid by future consumers.

It is unclear how the AEMC can logically conclude that this does not involve a transfer of costs and risks from networks to consumers. The AEMC says, "***absent any decline in demand*** [emphasis added], consumers would have paid the same capital costs in net present value terms; acceleration changes only the timing of the recovery, not the total".[42] And yet declining demand is the reason accelerated depreciation is being proposed: without it networks do not face the stranding risks that the AEMC says accelerated depreciation is meant to mitigate. Likewise, declining demand creates the risk that networks will not recover their full costs – it is these risks and costs that networks seek to shift onto consumers.

We do not agree with much of the framing that the AEMC has used to justify its position, which we consider is too focused on guaranteeing network recovery of its capital. We do not consider that appropriate for several reasons.

We don't think this is the correct interpretation of the "regulatory compact". In practice, consumers have not made an explicit commitment to fund the future costs of the network to which they are currently connected (and neither have retailers on their behalf). They are only committed to paying the *current* costs of being connected, while they remain connected.

The AEMC repeatedly states that networks are entitled to "a reasonable opportunity to recover at least the efficient costs of providing services."[43] However, it then elides costs with *efficient* costs. RAB additions are not formally subject to an efficiency test. The AER's ex ante assessments seek to restrict *forecast* expenditure to an efficient level, but networks are not bound to spend in line with this forecast. Additionally, efficiency should be considered in the broadest context, including the likelihood that in the changing circumstances, some expenditure in line with the rules at the time was not in fact efficient.

The AEMC has already determined that subsidising connections expenditure is no longer an efficient approach[44] and is contemplating tightening the capex criteria as part of this process. It is implausible that the turning point from efficient to inefficient occurs at just the point the rules change. To be clear, we are not seeking retrospective removal of – for example – connections costs from the RAB, rather emphasising that it's inappropriate to assume the RAB only represents efficient costs. The networks need to be accountable for their decisions, including decisions not to pursue rule changes that would have reduced RAB additions – such as the connections rule change. This is part of the underlying thesis of our proposal.

In any case, it is unlikely to be feasible to guarantee RAB recovery on behalf of customers. As the directions paper notes: "CEPA modelling for the AEMC indicates the regulatory framework is unlikely to

[39] Dynamic Analysis, Turning down the gas: Reducing consumer risk | Energy Consumers Australia.
[40] Dynamic Analysis, SA Residential Gas Customers long term analysis.
[41] Ibid, 2.
[42] AEMC, Directions paper, 23.
[43] AEMC, Directions paper, 44.
[44] ECA, Rule change GRC0085

fully mitigate the impacts of uncertain or declining demand on gas consumers and service providers".[45] Our view is that, if anything, the CEPA modelling understates the probability of networks being unable to fully recover their RAB from customers. Modelling carried out on the Jemena (NSW) and AGN (SA) networks by Dynamic Analysis indicated that accelerated depreciation would only decrease the 2055 RAB value by around 11 percent[46] and around 2.5 percent, respectively.[47]

This finding is important as it bears out our view that accelerated depreciation is a transfer of cost and risk from network investors to consumers, as it is changing – even if only to a limited extent – the size of the RAB that is likely to be ultimately stranded.

Gas networks' incentives are not aligned with the long-term interests of consumers

We disagree with the AEMC's contention that, where service providers are facing the risk of stranding, their incentives will be aligned with the NGO and RPPs (and therefore the long-term interests of consumers).[48] It is clear that networks have a strong incentive to maximise accelerated depreciation to a point beyond the long-term interest of their customers, including their future customers. Indeed, it is these risks that can cause their interests to diverge from the long-term interests of consumers.

Embedding this assumption would be a significant departure from the current framework. Existing rules do not make this assumption, which is why the Australian Energy Regulator (AER) currently has the discretion to modify or reject accelerated depreciation proposals to protect customers. The AEMC's proposed direction would effectively impose this assumption at exactly the time when network incentives and consumer interests are diverging.

While gas networks are structurally incentivised to maintain operations and recover costs for assets that will become stranded, this does not serve consumers when it results in the concentration of fixed costs being recovered more rapidly from a shrinking customer base. In any competitive sector, if a business model cannot adapt to technological change, investors face losses. To ensure an orderly transition to net zero, the regulatory framework must equitably allocate the cost of stranded assets between investors, government and consumers.

It's salient to recall why we price-regulate these networks. It is because they are natural monopolies and thus have pricing power. As such, the AEMC's statement that "they are likely to be well-placed and have a strong incentive to appropriately balance the risks associated with accelerating depreciation and triggering early exit" is not true.

While some customers may be prompted to electrify in response to rising prices, many are currently unable to respond to price signals in this way:

- many businesses use gas for processes for which there is currently no economic substitute
- renters do not have the power to choose to electrify their homes
- apartment dwellers with shared hot water or heating services cannot individually choose to electrify
- single dwelling homeowners may face barriers if they cannot access the capital required to electrify, especially if this necessitates electrical upgrades or other expensive renovation requirements

[45] AEMC, Directions paper, 44.
[46] Dynamic Analysis, Turning Down the Gas.
[47] Dynamic Analysis, Managing the transition from gas for South Australians; ECA, Power Move, 37
[48] Directions paper, 73.

- households and businesses have purchased gas appliances without any clear warning about the long-term likelihood of increasing gas prices and, despite increased gas prices, may be subject to sunk cost fallacy and an inability to admit that their assets (i.e. appliances) themselves are becoming uneconomic.

Without tight controls over their pricing power, networks could and would be incentivised to exploit these barriers. Handing them full discretion over accelerated depreciation is tantamount to handing them pricing power. The lack of restraint is illustrated by Table B.1 of the directions paper, in which there is only one instance where a network's proposed amount for accelerated depreciation was accepted by the regulator. In all other cases, the regulator judged that a far lower amount best met the NGO. Under the AEMC's proposed option C1, regulators would be far less able to overrule the businesses' proposals. It is also worth noting networks' depreciation proposals to date may already have been moderated to some degree by awareness of the AER's approach and discretion to reject or substitute claims for accelerated depreciation.[49] Without this level of regulatory discretion, we may see networks making even greater depreciation claims.

The AEMC should reconsider the propose-respond model for depreciation claims

This is an area of the regulatory framework that may not be well suited to a propose-respond model. The propose-respond model works best when it is used to elicit information about expenditure plans, simply because of the information asymmetries in the network's favour. A regulator may have difficulty calibrating, say, a repex plan without the network's proposal as a starting point. But it has significant downsides, too. It systematically transfers agenda-setting power to the regulated business, and behavioural economics tells us that this power is significant. The combination of anchoring, framing, and cognitive load effects means the regulator (let alone consumers and their representatives) is structurally disadvantaged through the process.

- The regulated business's opening proposal establishes a reference point that shapes the entire subsequent negotiation. Even a well-resourced regulator will tend to make insufficient adjustments from the anchor, meaning the final determination systematically skews toward the proposer's preferred position.
- In a propose-respond model, the proposal effectively becomes the *default*. Behavioural research consistently shows that defaults are sticky — departing from a stated position requires active justification, which shifts the burden of proof onto the regulator. The business proposes; the regulator must *argue* to go lower. This is a structural asymmetry.
- The business controls how costs, risks, and investment needs are framed. Presenting accelerated depreciation as essential for financial viability and to support future investment, rather than as a revenue-maximising decision, exploits the regulator's tendency to evaluate arguments in terms of the frame offered, rather than reconstructing an independent frame. Consumer advocates are then in a reactive, defensive position.
- Regulated businesses can exhibit both overconfidence and overoptimism – this may be genuine rather than strategic but still shapes the process.

Despite these disadvantages, we consider that regulators have done well to resist network claims for high levels of accelerated depreciation. The AER, in particular, with its price-path approach has avoided getting drawn into a fruitless argument with networks about the "correct" amount of accelerated

[49] See e.g. AGN SA 2026-2031 final plan, available at Proposal | Australian Energy Regulator (AER), 55.

depreciation to allow. There is no objectively correct answer, given the uncertainty around exactly how the transition will unfold.

The paper relies too heavily on the 'switching point' analysis and model

In this respect, we consider the directions paper exhibits undue confidence about the utility of concepts such as the "switching point". This is a high-level concept that reflects the fact that *some* customers may electrify once prices reach a certain level and that this *in principle*, acts as a constraint on the prices that can be charged. It is not a single objectively discoverable price point that accelerated depreciation can be calibrated against. This point holds, even if the network tariff was the entire delivered price of gas, which it isn't. This point is worth repeating: the AEMC's analysis relies on an assumption about a price that is well outside the network and the AER's ability to control.

In a workably competitive market, as the AEMC identifies, charging prices above the level of long-run average costs is impossible because higher returns would lead customers to "choose a rival supplier or product."[50] A business with a declining product in a competitive sector cannot simply hike prices for its remaining customers to recoup its initial investment faster. To do so would only drive customers away and accelerate the firm's exit.

The analysis also appears to assume energy users are rational economic actors with the immediate capacity to electrify. The reliance on the "switching point" as a price constraint is flawed because it ignores the significant technical and financial barriers facing renters, apartment dwellers and small businesses. For these consumers, a price hike does not signal an "efficient exit". It simply results in unavoidable energy stress and increased struggle to pay bills. It also fails to account for external drivers of electrification such as policies in Victoria that will prohibit new gas appliance installations from March 2027.In the gas market, a large portion (approximately 40% of all Australian households either rent or live in multi-unit buildings)[51] of the consumer base is captive. Renters, apartment dwellers with centralised systems and low-income households cannot easily choose to electrify regardless of price increases. We consider that further enabling this direction would be inconsistent with the spirit of the RPP.

The rules should not curtail the regulator's discretion to revise depreciation proposals

These factors all point to the best interests of consumers being served by putting accelerated depreciation decisions firmly in the hands of the regulator (option D or E in the AEMC's spectrum of options). This recognises that the level of depreciation in the context of stranding risk is essentially an abstract financial balancing act between the need to support ongoing investment in the network where necessary and the need to keep consumer prices as low as possible. In this respect it is somewhat analogous to the rate of return decision, which has already been successfully removed from the propose respond model. To be clear, we recognise that depreciation decisions still require some network specific information, and so should remain part of the individual access arrangement rather than a standalone review (as was done with the rate of return), but the relevant information can still be obtained from the networks.

The above notwithstanding, we still consider there is merit in our original proposal, which could be applied alongside Options D/E. This sought to create a threshold, to be evaluated by the regulator, based on the actions by the network to manage its stranding risk other than through accelerated depreciation. We consider that this would have both an incentive effect – encouraging the network to explicitly take any and all other steps to manage stranding risk – and a signalling effect – increasing

[50] AEMC (citing the Independent Committee on National Competition Policy), Directions paper, 53.
[51] ECA, Power Move, 2026, 43.

stakeholders' confidence that accelerated depreciation was only one among a suite of mitigation measures.

Our proposed approach was developed from participating actively in access arrangements and watching the ways in which most, if not all, networks proposals were not internally consistent. That is to say, they were both proposing accelerated depreciation under the premise that their consumer base was declining, while also seeking to expand their RAB, through new connections, new meters, and new connections to renewable gas projects. Some networks have also proposed accelerated depreciation 'to assist the network in its evolution towards a competitive future.'[52] It is unclear how the AEMC proposes such claims would be assessed under its proposal.

While the AEMC may theorise that network businesses align with consumers, this assumption is not reflected in the history of recent access arrangement proposals. Rather than assuming network businesses actions align with consumers best interests (and ignoring the recent history), the rules can and should make accelerated depreciation contingent on the network actively demonstrating that it is taking actions to ensure its future aligns with consumer interests.

We support expanded use of capital redundancy – but not only as a 'last resort'

We consider that an enhanced use of the capital redundancy provisions could have similar effects. We agree that partial redundancy should be fully recognised in the rules to ensure capital redundancy adjustments can be applied to a RAB as a whole in the context of declining demand.

We disagree that it should be characterised as a "last resort" which seems to rest on a very specific reading of previous regulatory statements. It seems to us that a network level asset becomes partially stranded once there is a certain probability of not recovering its cost in full. We recognise there is some ambiguity of the level of probability that would apply. Nevertheless, we consider that the illustrative modelling by CEPA reflects networks that can be judged as having met that threshold. We consider that this should then trigger application of the capital redundancy provisions. Noting the AEMC's comment that "removing redundant capital would reduce a service provider's revenue requirement and, in turn, reference tariffs. A reduction in reference tariffs would mean that: consumers face the switching point later," the last resort approach runs a high risk of capital redundancy not being applied until too late. If the purpose is to defer the switching point – and as discussed above, there isn't one single switching point in any case – then the uncertainty about when a "disorderly exit" could be triggered means that it is best to begin applying capital redundancy early rather than late.

Capital redundancy could be applied progressively, with a small adjustment to the RAB in the first instance, reflecting the uncertainty of the transition. There is a spectrum of approaches that includes the JEC proposal that all maintain the principle that capital redundancy is most effective where it is identified early and is a complement to any accelerated depreciation rather than something that is applied only when accelerated depreciation has ceased to be effective.

Importantly this also provides a signal to consumers and other stakeholders that networks have "skin in the game" when they are proposing accelerated depreciation if there is also a RAB adjustment, even a modest one. It serves as an incentive for networks to only seek accelerated depreciation when they are sufficiently concerned about stranding risk that they are prepared to accept some of the risk upfront.

We consider that there could be value in the context of both accelerated depreciation and capital redundancy to consider whether greater granularity can be applied than whole of network. Specifically, the most likely longer-term users of the network are large hard-to-electrify businesses who might

[52] AGN, 2026-2031 Final Plan, Proposal | Australian Energy Regulator (AER), 16.

plausibly switch to renewable gases and who are likely to be connected at medium-high pressures. Such businesses may be concerned that the protections we consider appropriate for low pressure customers may leave them at risk of having to pay for parts of the network they don't use. To be clear we do not think that is an appropriate outcome. To the extent it's possible to apply capital recovery tools to different parts of the network differently, this could assist in protecting those customers, providing the outcomes can be appropriately reflected in network tariffs.

The other capital recovery tool canvased in the directions paper is a shift away from indexing the RAB. The challenge here is that it appears to be a blunt instrument, as we assume that part-indexation is not a realistic option. So there is a binary choice between indexation or no indexation applied to the full RAB, as compared to the options for calibration inherent in the other tools. It's unclear how a nominal approach fits with the AEMC's stated goal that "cost recovery is more in line with the expected use of the pipeline". Additionally, there is a high risk that embedding an option to "turn off" indexation for individual networks into the rules, especially combined with a high level of network discretion over use of these tools, would lead to consumers bearing a rapidly accelerated capital cost recovery because a network has proposed both a nominal approach and accelerated depreciation. Accordingly, if such a provision is enacted it must be clearly at the discretion of the regulator, and they should be required to explicitly consider the impact of all capital recovery tools holistically.

The treatment of inflation in the regulatory framework has been raised recently in the context of the AER's Rate of Return Instrument review.[53] Any change to RAB indexation must also be considered in terms of how it interacts with the Rate of Return.

Question 6: Expenditure

- Clarifying that service providers must justify all capex through a quantitative assessment of all credible options that support the provision of regulated pipeline services.
  - 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).
  - Amending the justification for capex to maintain capacity to meet forecast (instead of
  - existing) demand for services under NGR 79(2)(c)(iv).

  What are your views on the need for the NPV test in rule 79(2)(b)?
- What are your views on our proposed direction to amend the NGR opex definition?

We welcome the direction of the capex and opex changes

ECA broadly welcomes the proposed direction, which supports our overall thesis that the expenditure provisions in the NGR would benefit from further clarity and new spending on the gas network should be minimised to that which is absolutely necessary to meet the NGO. We agree with the CEPA modelling that if capex can be reduced to more efficient levels, then this is a further tool to mitigate stranding risk. Modelling we have previously commissioned on the Jemena gas network demonstrates that minimising capex reduces asset stranding risks more significantly than accelerating depreciation.[54]

In particular, we support:

- proposals to consider all credible options for meeting an identified need and a quantitative assessment of all credible options

[53] EMAS report appended to the ECA's submission to the AER's Rate of Return Instrument Issues Paper
[54] Dynamic Analysis, Turning down the gas.

- proposals to amend the justification for safety capex
- proposals to adjust the opex definition to remove growth-oriented phrases, and
- proposals to orient capacity requirements to forecast demand rather than existing demand (which may be higher than future demand) – noting that it is important that this appropriately allows scope for demand management as an alternative to augmentation.

We consider that the NPV test continues to have merit as a threshold test but is not a sufficient justification on its own.

The AEMC should further consider our other proposed capex changes

We are disappointed that the AEMC considers that the NGL does not allow for consideration of non-pipeline alternatives. AusNet's Ballan project indicates that there are at least some circumstances where this could support achievement of the NGO, and we consider it insufficient to rely on a combination of government support and network goodwill to identify and implement such solutions where they represent a lower overall cost. We agree that there are further considerations to implementing such an approach, but they do not present as insuperable barriers.

We proposed six other distinct and varied changes to the expenditure framework. It is unhelpful for the AEMC to dismiss these en masse rather than engage with them individually and to fail to explain the reasons for rejecting them.[55] We recommend the AEMC consider these further before progressing to a draft decision.

Some of these additional changes appear to us to be relatively uncontroversial, such as the need to consider the impact of declining demand in capex programs. This would support appropriate NPV calculations and quantitative assessments. Since the AEMC proposes to require long-term forecasts as part of access arrangements we can't see how it increases the regulatory burden, is impractical or is unaligned with customers' interests. If the AEMC considers this is already covered by other existing rules or proposed rule changes, this should be explained.

We are also unclear what value the advance determination process has for consumers.

We also remain convinced that the framework would benefit from greater clarity about what costs are allowable with respect to renewable gases and who should bear these costs. As set out in our rule change proposals, we find it highly unlikely that residential and small business customers will benefit from renewable gases in the long term. There is insufficient feedstock for all gas users to consume biomethane, and it is implausible that small consumers will switch to hydrogen appliances. Both industries are currently in a nascent stage, and these gases are materially more expensive than natural gas. International and Australia-specific independent studies inform and support our perspective.[56] Accordingly, we consider that investments to support potential future renewable gases are too speculative to warrant a regulated return and that the long-term interests of small consumers is not enhanced by renewable gases.

To be clear, we have no objection to biomethane injections into the gas network if there is an off taker prepared to supply it. But since biomethane is chemically identical to natural gas, we can't see why there is a need for additional expenditure that must be borne by consumers. The off taker should be responsible for their connection costs.

[55] AEMC, Directions paper, 104.
[56] ECA, Power Move, 2026, 20.

We recognise that some hard-to-electrify larger users may take a different perspective. In this case we think the fairest approach is to seek to use the reference tariff principles to ensure that those who see benefit in such investments are those who pay for it.

We also recognise that some networks may consider that their future prospects would be improved by supporting renewable gases. Nonetheless, we consider such expenditure to be sufficiently risky that it should be borne by shareholders. We accept that the quid pro quo is that if such investments pay off in the long term, the returns to shareholders should not be constrained in the way that the return on conforming capex is. The onus should be on the proponents of such expenditure to find ways to accommodate this principle in the framework.

Question 7: Tariff arrangements

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

The ECA's rule change proposals did not specifically seek changes in the tariff arrangements and so we do not start from a definitive position. ECA acknowledges that tariff design can be an important factor in how consumers use the gas system and their incentives to maintain a gas connection versus electrification. We are generally supportive of tariff guidance emphasising the importance of customer impacts in setting tariffs and tariff variation mechanisms. We note, however, that customer impacts have been a required consideration in electricity network tariffs for some time and despite this, the AEMC considers that these tariffs need material redesign (a position which the ECA broadly supports). This indicates that customer impact considerations are necessary but not sufficient for the implementation of tariffs that work for customers.

We note that conventional economic wisdom indicates that monopolies operating under a price cap are incentivised to maximise revenue by applying Ramsey pricing. This seeks to weight revenue recovery towards customers with a low-price elasticity of demand and away from those with a high elasticity of demand. This often manifests as a reweighting of revenue recovery from large business users to residential users. This is because the former are at greater risk of exiting the market if they consider prices are too high.

Such pricing approaches create equity concerns, especially in the light of the significant barriers to switching some customer groups face. These concerns must be taken into account in considering the constraints that should be applied to reference tariff setting as well as the continuing appropriateness of a price cap approach.

We agree with the AEMC's logic that:

- tariffs should not be set below avoidable cost for the relevant tariff class
- tariffs should not be set above standalone cost for the relevant tariff class, and
- avoidable and standalone cost calculations should be robust and appropriate to the context.

However, absent any quantitative analysis of how wide the band these principles create, it is unclear how much of a constraint they apply in practice. That is, they may be necessary, but not sufficient to support sound tariff design. While we don't have an issue in isolation with the proposal to relegate the role of LRMC in informing tariff setting, we are cautious about supporting it without further clarity around what will in practice serve as the constraint on tariff setting and drive well-designed tariffs.

While policymakers and regulators may be uncomfortable being required to accommodate equity considerations, they remain better placed to do so than networks. The AEMC should consider whether it would be better for the regulator to determine tariffs, taking account of relevant cost and other information provided by the networks as well as customer views, rather than have the network propose tariffs that the regulator has limited scope to adjust.

Question 8: Incentive mechanisms

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

The ECA's rule change proposals did not specifically seek changes to the incentive mechanisms for gas networks. This was a scope change introduced by the AEMC. Given this, we are a little surprised that the AEMC has not carried out a deeper dive into the explicit and implicit incentives of the current framework. Even if no changes are made to the explicit incentives, a consideration of the implicit incentives can assist in determining the best approach in the other areas being consulted on.

For example, AEMC notes that with respect to demand risk: "The reference tariff variation mechanism proposed and approved as part of the AA determines who bears the risk that demand within the access arrangement period will be more or less than what was forecast by the service provider. This provides a financial incentive for service providers to increase demand under a price cap or hybrid reference tariff mechanism (based on a combination of price and revenue caps)."[57]

We agree with this assessment, and this should inform how tariffs are set and, in particular, who decides what sort of mechanism should apply and on what grounds the decision is made.

The AEMC also notes "It may also provide an implicit incentive for service providers to present forecasts with lower levels of demand."[58] We consider that "may" is too equivocal here. It follows logically that if a network operating under a price cap benefits from demand exceeding the forecast, it also benefits from a low forecast as that makes the forecast easier to beat. For this reason, regulatory scrutiny of demand forecasting is very important. This is only heightened by the use of longer-term demand forecasts to support accelerated depreciation claims. The AEMC should consider how the strength of these incentives can inform the best way to determine demand forecasts.

Conversely, we agree with the use of "may" in the statement "In the context of uncertain demand, service providers may have an incentive to minimise new capex entering the capital base to minimise potential stranding risk. This means that service providers may seek to limit new expenditure, while continuing to support the safe operation of the network."[59] In other words, consumers cannot be fully confident that this incentive is effective, which is why we need strong guidance on capex criteria and robust capital recovery tools that balance customer and shareholder risks with respect to stranding.

[57] AEMC, Directions Paper, 140.
[58] Ibid
[59] ibid

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