

Final decision

**Jemena Gas Networks (NSW) access
arrangement 2025 to 2030
(1 July 2025 to 30 June 2030)**

**Attachment 13 – Capital expenditure sharing
scheme**

May 2025

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List of attachments

This attachment forms part of our final decision on the access arrangement that will apply to Jemena Gas Networks' (NSW) for the 2025–30 access arrangement period. It should be read with all other parts of this final decision.

For some issues that had draft decision attachments, and which were settled at the draft decision stage or required only minor updates, the reasons in the draft decision attachments and, where relevant, in the final decision Overview set out our reasons for our final decision on the issue. In these circumstances, we have not prepared all attachments, and our draft decision reasons form part of this final decision. The final decision attachments have been numbered consistently with the equivalent attachments to our draft decision.

The final decision includes the following documents:

Overview

Attachment 2 – Capital base

Attachment 4 – Regulatory depreciation

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 7 – Corporate income tax

Attachment 9 – Reference tariff setting

Attachment 10 – Reference tariff variation mechanism

Attachment 12 – Demand

Attachment 13 – Capital expenditure sharing scheme

Contents

List of attachments	iii
13 Capital expenditure sharing scheme	1
13.1 Final decision	1
13.2 JGN's proposal	2
13.3 Submissions.....	5
13.4 Assessment approach.....	5
13.5 Reasons for final decision	6
13.6 Revisions	8
Glossary	9

13 Capital expenditure sharing scheme

This attachment outlines our assessment of Jemena Gas Networks' (JGN) proposal for a capital expenditure sharing scheme (CESS) for the 2025–30 access arrangement period (2025–30 period). This includes CESS rewards or penalties to be applied next period based on JGN's performance this period.

The CESS is designed to incentivise efficient spending on capital expenditure (capex) by rewarding Network Service Providers (NSP) for lowering their capex below the amount approved for the access arrangement period. The rewards are shared between the NSPs and consumers.

To ensure lower capex does not compromise service standards, the reward amounts are modified by a contingent payment factor (CPF). If service standards fall below target levels, reward amounts are reduced. Below a certain service standard threshold, rewards are reduced to 0. Conversely, the CESS will lead to a penalty if the NSP spends above its approved capex forecast. The CPF does not apply to penalties, so if a penalty is incurred, it will not be reduced.

JGN's proposed CESS design, and our final decision, for the 2025-30 period is based on JGN's 2020-25 CESS design, but with adjustments. The most significant adjustment is that the CESS' sharing factor will now be tiered, as per our update to the CESS mechanism in April 2023.¹

13.1 Final decision

JGN is expected to spend less capex in the 2020–25 access arrangement period than our forecast capex in the final decision for the 2020-25 access arrangement period. This results in a CESS reward being added to JGN's revenue in the 2025–30 access arrangement period. Our final decision is to not approve JGN's proposed CESS revenue increment of \$33.567 million (\$2024-25), but our alternative CESS revenue increment of \$33.574 million is broadly similar. Table 13.1 outlines JGN's proposal and our final decision.

Table 13.1 Our final decision on JGN's CESS increments (\$ million, \$2024/25)

	2023-24	2024-25	2025-26	2026-27	2027-28	Total
JGN's proposed increment	6.713	6.713	6.713	6.713	6.713	33.567
AER final decision increment	6.715	6.715	6.715	6.715	6.715	33.574

Source: AER analysis. JGN, *JGN - RP - Att 7.8M - CESS model - 20250115 - Public*, January 2025. Numbers may not add up due to rounding.

The difference between our decision and JGN's proposal is that we have updated the consumer price index (CPI) and real vanilla weighted average cost of capital (WACC)

¹ AER, [Final decision - Review of incentive schemes for networks](#), April 2023.

figures.² We are otherwise satisfied that JGN’s application of the CESS is appropriate, and consistent with the CESS mechanism set out in its access arrangement.

We accept JGN’s proposal to retain a CESS for the 2025–30 Access Arrangement period, including the exclusion of customer connections capex from the CESS.³ JGN has sought to exclude renewables connection capex forecast from the calculation of the CESS. We note that we have not included forecast capex for these projects in our final decision. Consequently, they do not currently form part of forecast capex against which the CESS is calculated. Nevertheless, our final decision envisages a scenario where JGN may pursue these projects.⁴

We will exclude any renewable connections capex JGN does spend in the 2025-30 period from the CESS. JGN may choose to make the investments in the pipeline assets during the 2025-30 period and can seek to include this capex in the opening capital base in 2030. We consider there will be a strong incentive for JGN to only achieve an efficient cost for any assets it chooses to invest in, such that it is not necessary to provide a further incentive through the CESS. We set out our reasoning for this view in section 13.5.2.3.

Separately, JGN will apply a tiered sharing factor to its CESS mechanism, as per the AER’s update to the CESS mechanism in April 2023. The details of this update and our reasons are set out in our Draft Decision.⁵

13.2 JGN’s proposal

13.2.1 CESS amounts from the 2020–25 access arrangement period

JGN proposed a \$33.567 million (\$2024-25) reward be added to its revenue in the 2025–30 access arrangement period.⁶

As part of its contingent payment index, JGN has adopted measures to monitor service performance. The five target measures are:

- unplanned System Average Interruption Frequency Index (SAIFI) (weighting 10%)
- unplanned System Average Interruption Duration Index (SAIDI) (weighting 10%)

² Attachment 2 on the capital base sets out our CPI final decision, while the Overview section of this final decision details our vanilla WACC final decision.

³ In this attachment, “customer connections” refers to all connections capex except renewable connections capex.

⁴ For more information, see Attachment 5 of this final decision.

⁵ AER, *AER - Draft decision - JGN access arrangement 2025–30 - Attachment 13 - Capital expenditure sharing scheme - November 2024*, November 2024, pp. 7-8.

⁶ JGN, *JGN - RP - Att 7.8M - CESS model - 20250115 - Public*, January 2025.

- mains and service leaks (weighting 30%)
- meter leaks (weighting 10%)
- poor quality supply (weighting 30%)
- meter read estimation rate (weighting 10%)

Performance targets for each measure were set in our Final Decision for 2020–25 using the previous five years of historical data. JGN’s performance against all its targets is represented by the contingent payment index, which then informs the CPF. The contingent payment index measures performance and can have any value. The CPF adjusts JGN’s CESS revenue reward. The CPF is equal to the contingent payment index only between the values of 80 and 100: when the contingent payment index is above 100, the CPF equals 100; when the contingent payment index is below 80, the CPF equals 0.

The CPF is used to scale down rewards if service performance is less than the target level. Consistent with the previous access arrangement period’s CESS, the threshold of performance below which no reward is payable to JGN for an underspend is an index score of 80 (base is 100).

In its revised proposal, JGN has updated its reported performance for 2023–24 with actual data. As seen in Table 13.2, owing to strong performance against its most heavily weighted targets, JGN has a contingent payment index of 105.2, leading to a CPF of 100. JGN will receive 100% of its revenue increment as a reward.

Table 13.2 JGN’s reported performance and CPF

Measures	Actual	Target	Index	Weight	Contribution
Unplanned SAIFI	3.9	3.3	83.8	10%	8.4
Unplanned SAIDI	22.4	13.1	28.8	10%	2.9
Mains and services leaks	0.1	0.2	117.1	30%	35.1
Meter leaks	7.9	8.2	102.7	10%	10.3
Poor quality supply	0.7	0.9	128.4	30%	38.5
Meter read estimation rate	0.1	0.1	100.0	10%	10.0
Contingent Payment Index	105.2				
CPF	100%				

Source: JGN, JGN - RP - Att 7.8M - CESS model - 20250115 - Public, January 2025. Numbers may not sum due to rounding.

13.2.2 Application of CESS in the 2025–30 access arrangement period

JGN proposes to continue using a CESS into the 2025–30 access arrangement period. As per our draft decision, JGN has included the updated sharing ratio in its access arrangement. Consistent with its initial proposal, JGN proposes to update the CESS from how it was implemented in the 2020–25 access arrangement period by excluding renewable connections capex.

13.2.2.1 Contingent payment index targets

As part of its CPF, JGN has adopted measures to monitor service performance. JGN broadly proposes to maintain the measures and weightings it used during the 2020-25 access arrangement period. It has formulated its targets using the average of the most recent five years of actual data that were available at the time of its initial proposal, 2018-19 to 2022-23.⁷ Table 13.3 outlines JGN's proposed performance targets. As all these figures were actual rather than estimated during the draft decision process, JGN's proposed performance targets are the same as its initial proposal and our draft decision.

Table 13.3 JGN's proposed performance targets (\$ million, \$2024/25)

	Target	Weighting
Unplanned SAIFI	3.6	10%
Unplanned SAIDI	34.5	10%
Mains and services leaks	0.1	30%
Meter leaks	8.3	10%
Poor quality supply	0.6	30%
Meter read estimation rate	5.4%	10%

Source: JGN, *JGN - RP - Att 7.8M - CESS model - 20250115 - Public*, January 2025; JGN, *JGN - RP - 2025-2030 - Access Arrangement - 20250115 - Public*, January 2025, pp. 99-100. Numbers may not add up due to rounding.

13.2.2.2 The sharing factor

The CESS includes a sharing factor or ratio, which determines how an efficiency gain/loss is shared between the NSP and its customers. Following a review in 2023, the CESS mechanism was updated, most relevantly the sharing factor. Previously, the sharing factor was 30% without variation for both underspends and overspends. The updated CESS guideline introduces a tiered sharing factor for underspends. Thirty per cent will apply to any underspend amount up to and including 10% of the approved capex forecast; and 20% will apply to any underspend amount greater than 10% of the approved forecast. For overspends, the sharing factor remains a constant 30%. In short, the updated scheme reduces the rewards when a network business outperforms against its approved forecast by more than 10% but maintains the same penalties for underperformance. This asymmetry is intended to reduce the costs of the CESS to consumers while maintaining strong incentives for efficiency.⁸

Our draft decision required JGN to include a tiered sharing factor in its access arrangement. In its revised proposal, JGN has included a tiered sharing factor as per the CESS guideline.⁹

⁷ Since JGN's initial proposal, actual data for 2023-24 has become available. JGN has not adjusted the five-years of actual data to be 2019-20 to 2023-24, and it instead maintains the timespan it used in its initial proposal and our draft decision. This is consistent with JGN's and our approach in the 2020-25 access arrangement review, where the timespan 2013-14 to 2017-18 was used even when 2018-19 became available. The year 2023-24 will be represented when setting JGN's targets for 2030-35

⁸ AER, [AER - Final decision - Capital expenditure incentive guideline - 28 April 2023](#), April 2023, pp. 4-5.

⁹ JGN, *JGN - RP - 2025-2030 - Access Arrangement - 20250115 - Public*, January 2025, pp. 28-29.

13.2.2.3 Capex applicable to the CESS

Consistent with its initial proposal and our draft decision, JGN proposes to continue excluding capex related to new customer connections from the CESS. This exclusion was first proposed and accepted for JGN's 2020-25 access arrangement. This was on the basis that such capex is driven by customer-initiated connection volumes broadly beyond JGN's control. As the purpose of the CESS is to incentivise efficient spending, the CESS should ideally apply only to capex within JGN's control.

In addition to capex relating to customer connections, JGN proposes to exclude renewable connections capex from the CESS in the 2025-30 period. Renewable connections capex includes the 8 biomethane renewable connections projects (in total \$78.9 million) JGN is proposing.¹⁰ In our draft decision, we considered that renewable connections and customer connections were not analogous, as renewable connections are not largely outside JGN's control (like customer-initiated connections are). As such, renewable connections could not be excluded on the same basis as customer connections. In its revised proposal, JGN states that there is limited ability for it to influence expenditure on renewable gas connections and that regulation should allow innovation by promoting more of these connections.¹¹

13.3 Submissions

We have received 1 submission on the proposed exclusion of renewable connections from the CESS. The Justice and Equity Centre supported our draft decision not to exclude renewable connections, because JGN can control its spending on these.¹²

13.4 Assessment approach

A full access arrangement may include (or we may require it to include) one or more incentive mechanisms to encourage efficiency in the provision of services by the service provider.¹³ Incentive mechanisms may provide for carrying over increments for efficiency gains, or decrements for efficiency losses, from one access arrangement period into the next.¹⁴ An incentive mechanism must be consistent with the revenue and pricing principles.¹⁵

We consider the following revenue and pricing principle is most relevant for assessing JGN's proposed incentive scheme:

'A scheme pipeline service provider should be provided with effective incentives in order to promote economic efficiency with respect to reference services the service provider provides. The economic efficiency that should be promoted includes—

¹⁰ These projects are discussed in more detail in Attachment 5 of this final decision.

¹¹ JGN, *JGN Revised 2025 Plan*, January 2025, p. 54.

¹² JEC, JEC - Submission on JGN's 2025–30 revised proposal and draft decision - February 2025, February 2025.

¹³ NGR, r. 98(1).

¹⁴ NGR, r. 98(2).

¹⁵ NGR, r. 98(3).

(a) efficient investment in, or in connection with, a pipeline with which the service provider provides reference services; and

(b) the efficient provision of pipeline services; and

(c) the efficient use of the pipeline.¹⁶

13.5 Reasons for final decision

13.5.1 CESS amounts from the 2020–25 access arrangement period

We consider JGN’s proposed reward of \$6.713 million per year and \$33.567 million overall is consistent with the CESS mechanism in its 2020-25 access arrangement. As JGN performed strongly against its CPF targets, its CPF is 100, meaning it will receive 100% of its reward. However, we have updated the CESS calculations to reflect our final decision on CPI and WACC. These updates lead to a CESS reward of \$6.715 million per year and \$33.575 million overall.

13.5.2 Application of the CESS in the 2025–30 access arrangement period

We accept JGN’s proposal to apply the CESS in the 2025-30 access arrangement period, including the tiered sharing factor. We accept the exclusion of customer connections and renewable connections capex, and outline our reasons below.

13.5.2.1 Contingent payment index targets

In our draft decision, we accepted JGN’s contingent payment index targets. We also accepted its proposal to include residential, commercial, and industrial customers in its calculations of CPF targets for the 2025-30 period. JGN’s revised proposal has not proposed any changes to its performance targets. Our final decision is to accept JGN’s performance targets.

Table 13.4 JGN’s actual performance and AER’s final decision targets for 2025-30

	Target	Weighting
Unplanned SAIFI	3.6	10%
Unplanned SAIDI	34.5	10%
Mains and services leaks	0.1	30%
Meter leaks	8.3	10%
Poor quality supply	0.6	30%
Meter read estimation rate	5.4%	10%

¹⁶ NGL, s. 24(3).

Source: Source: JGN, JGN - RP - Att 7.8M - CESS model - 20250115 - Public, January 2025; JGN, *JGN – RP - 2025-2030 - Access Arrangement - 20250115 – Public*, January 2025, pp. 99-100. Numbers may not add up due to rounding. Numbers may not add up due to rounding.

13.5.2.2 The sharing factor

Following a review in 2023, the CESS mechanism was updated, most relevantly the sharing factor. The updated scheme reduces the rewards when a network business outperforms against its approved forecast by more than 10% but maintains the same penalties for underperformance. This asymmetry is intended to reduce the costs of the CESS to consumers while maintaining strong incentives for efficiency.¹⁷

In our draft decision, we required JGN to include this tiered sharing factor in its access arrangement. JGN has done so. We accept the modification.

13.5.2.3 Capex applicable to the CESS

Consistent with our draft decision, we accept the continued exclusion of capex related to customer connections from the CESS. As set out in that draft decision, our reasoning for this view is provided in the draft and final decisions for JGN's 2020-25 access arrangement.¹⁸

We also accept JGN's proposed exclusion of renewable connections from the CESS, but for reasons that differ from those set out by JGN.

In our draft decision, we considered renewable connections projects are not analogous to regular customer connections, because we considered JGN has greater discretion to control its spending on these projects. As such, we considered that renewable connections could not be excluded on the same basis as customer connections, and therefore could not be excluded from the CESS for the reasons set out by JGN.

We consider these points are still relevant. However, we have ultimately decided to exclude renewable connections capex from the CESS in the 2025-30 access arrangement period. In Attachment 5 of this final decision, we note our reasons for not accepting JGN's proposed renewable connections capex – with the key reason being the significant uncertainty surrounding whether the projects will take place in the access arrangement period. However, we also note that JGN may choose to make these investments within the 2025-30 access arrangement period. It is open for JGN to seek to have such expenditure assessed as part of the calculation of the opening capital base for the 2030-35 access arrangement period. In this case, JGN is already exposed to the risk that the AER may consider any renewable connections capex JGN spends in the 2025-30 period is not conforming. This would mean that JGN would not have the ability to recover the expenditure from customers. In these circumstances, we consider that, were JGN to make these investments, it is strongly incentivised to incur only efficient costs, such that the CESS is unnecessary to provide a further incentive.

¹⁷ AER, [Final decision - Review of incentive schemes for networks](#), April 2023.

¹⁸ AER, [JGN 2020-25 - Final decision - Attachment 13 - Capital expenditure sharing scheme](#), November 2019; AER, [Final decision - JGN access arrangement 2020-25 - Attachment 13 - Capital expenditure sharing scheme](#), June 2020.

Further, the CESS would penalise JGN for choosing to invest in renewable connections even if it ultimately gained sufficiently firm commitments from counterparties. Under the circumstances, we do not consider it appropriate to create a financial disincentive for JGN to invest in renewable connections assets should it form the view that it has sufficiently firm commitments from counterparties in place.

We have therefore decided not to apply the CESS to renewable connections capex.

13.6 Revisions

We have proposed the following revisions to the access arrangement as set out in Table 13.5.

Table 13.5 CESS revisions

Revision	Amendment
Revision 13.1	Make revisions necessary to update CPI, real vanilla WACC, reported performance inputs, and reported capex inputs in the calculation of the CESS revenue increment, in line with our final decision.
Revision 13.2	Change clause 13.1(b)(v)(A) to: <ul style="list-style-type: none"> A. Exclude expenditure related to connecting: <ul style="list-style-type: none"> 1) Renewable Gas facilities; and 2) customers (i.e. connections capex under Part 12A of the National Gas Rules);
Revision 13.3	In Schedule 1 Definitions and interpretation, include the following definition of Renewable Gas: <p>Renewable Gas means:</p> <ul style="list-style-type: none"> a) renewable methane, other than methane produced using biomass from timber native to Australia; b) hydrogen produced using renewable energy, other than biomass from timber native to Australia; c) any other renewable gas prescribed by Applicable Law; and d) a blend of Gas which includes a gas referred to in paragraphs (a) to (c);

Glossary

Term	Definition
capex	capital expenditure
CCP31	Consumer Challenge Panel, sub-panel 31
CESS	capital expenditure sharing scheme
CPF	contingent payment factor
CPI	consumer price index
JGN	Jemena Gas Networks
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
NSP	Network Service Provider
NSW	New South Wales
opex	operating expenditure
SADI	System Average Interruption Duration Index
SAIFI	System Average Interruption Frequency Index
VIC GAAR	Victorian gas access arrangement reset
WACC	weighted average cost of capital