**Extra Submission**

**by CITIC Pacific Mining Management Pty Ltd**

**in response to**

**the Economic Regulation Authority's Draft Decision and AGIG's Revised Final Plan relating to *the Dampier to Bunbury Natural Gas Pipeline Access Arrangement 2021* – 2025**

## PART A - INTRODUCTION

### 1 Background

In January 2020, DBNGP (WA) Transmission Pty Limited (**AGIG**) submitted to the Economic Regulation Authority (**Authority**) proposed revisions to its access arrangement for the Dampier to Bunbury Natural Gas Pipeline (**DBNGP**) and proposed amendments to the reference services agreements terms and conditions, for the period 1 January 2021 to 31 December 2025 (**AA5 Period**) (**Proposed Revisions**).

In March 2020, the Authority published its Issues Paper on Proposed Revisions to the Dampier to Bunbury Natural Gas Pipeline Access Arrangement 2021 – 2025 (**Issues Paper**).

On 31 March 2020 CITIC Pacific Mining Management Pty Ltd (**CPM**) submitted its "**Initial Submission**" in relation to AGIG's Proposed Revisions and in response to the Authority's Issues Paper.

In August 2020 the Authority issued its "**Draft Decision**" on the Proposed Revisions to the DBNGP Access Arrangements for the AA5 Period seeking for AGIG to address specific amendments.

In October 2020 AGIG submitted its "**Revised Final Plan**" responding to the Authorities Draft Decision.

This "**Extra Submission**" is made by CPM in relation to the Draft Decision and the Revised Final Plan and in response to the Authorities request for public submission so the Authority can peruse and use all to build their final positions to deliver sensible tariffs and terms applicable to DBNGP access arrangements for the AA5 Period in the form of the Authorities "**Final Decision**".

### 2 About CPM

CPM is an existing shipper on the DBNGP. CPM operates a world-class magnetite mine and processing facilities at Cape Preston in the Pilbara (**Sino Iron project**), utilising natural gas for on-site generation of electricity.

The Sino Iron project have six processing lines, currently producing 20 million tonnes of magnetite concentrate annually. The Sino Iron Project also includes large-scale supporting infrastructure and the Pilbara's first greenfield port development in 40 years.

The Sino Iron project is China's largest-ever overseas investment in the resources sector, delivering wide-ranging socio-economic benefits including the creation of a new downstream processing industry for Australia, significant long-term revenue streams to government, local employment, international technology transfer, and an overall strengthening of the Sino-Australian economic relationship.

Due to the short amount of time available for submissions to be provided by CPM on the Draft Decision and Revised Final Plan, this Extra Submission is streamlined. For more detail CPM offer the Authority the ability to discuss these matters at a convenient time should they wish.

### 3 Summarised Extra Submission Concepts

CPM requests that the Authority consider the following issues in its decision making in relation to the Proposed Revisions and Final Revised Plan, including understanding the concept adopted by CPM in developing this Extra Submission which again is one that takes a position that the gas shippers should be seen as the "owners" of the pipeline and AGIG operate it on our behalf and in doing so the Shippers pay all the capital and operating costs and based on quality operating performance, pay AGIG a solid profit so they can return such to their shareholders. Accordingly we as an Owner, want the operator to make a profit so they don't go broke (as has occurred in the past) BUT it's important that business drivers remain aligned and so AGIG must operate and maintain the pipeline and provide the services to the "Owners" in the most efficient manner possible whilst maintaining performance metrics that meet all Owners requirements (100% reliability). We as Owners need the pipe to continue to operate for the life of the Sino Iron Project and CPM must strive to ensure that the operators business drivers remain fundamentally aligned with the Owners business drivers to ensure ongoing success.

## 4 Draft Decision

4.1 CPM would like to firstly express its sincere appreciation of the evident thoroughness of the Authorities work volume and effort in completing their review of the Proposed Revisions and Public Submissions and their development of the Draft Decision. CPM believe most components of their Initial Submission were well considered by the Authority and captured appropriately within Draft Decision.

4.2 CPM submits its support for the Authorities decision not to approve AGIG's proposed revisions position' taken in the Draft Decision and trusts that all 57 "Required Amendments" have been suitably addressed by AGIG in their Revised Final Plan and future operations planning without material alteration.

4.3 CPM submits their respectful suggestion that the Authority adopt the tariff structure and outcomes as set out in the Draft Decision as an interim measure, if the final decision could not be delivered before 1st January 2021.

4.4 CPM specifically submits its strong support of the Authorities Draft Decision on amendments to clauses (and all subsequent sub clauses): 3.2, 4, 6.11, 8.10, 8.16, 9.5, 9.6, 9.8 a), 11.1 and 17.2.

4.5 With reference to the Draft Decision paragraphs 88, 1564, 1598, 1561-1574 (etc) CPM respectfully advises the Authority that CPM believe there is now evidence to confirm a change in the direction of gas flows is occurring and northern flows are "expected' to grow in the future. That evidence is the recent announcement by the Beach AWE (Mitsui) JV on their plans to toll Watsia gas through the North West Shelf (NWS) LNG production facilities, in addition; actual flow directions in the north part of the DBNGP (loop and main lines) are currently being impacted by reduced volumes being delivered into the DBNGP by the NWS with gas now believed to be flowing north rather than south. For clarity, this submission is not seeking to change the positions taken in the Draft Decision or to amend any further T&Cs to address gas flow directions, as CPM is comfortable with the P1 and B1 structures and how they operate, CPM is simply pointing out that there appear to have been a number of decisions made by the Authority that were based on not having evidence to support a change in flow direction and that such may or may not now be relevant when developing the Authorities Final Decision and will most likely have been known by AGIG on them providing their Revised Final Plan.

4.1 With reference to the Draft Decision paragraphs 1226 to 1232, CPM respectfully seeks for the Authority to reconsider the formulae to be used to adjust tariffs for inflation annually. CPM submits that depreciation particularly is a figure used in the development of the tariff which is recovering capital spent in the past and as such it is not appropriate to inflate again in the future, particularly it is a non-cash item, otherwise a potential over recovery on revenues in the later part of the AA5 Period may result, at the detriment of Shippers. CPM further submits that should the tariff stay as determined in the Draft

Decision, then the perceived over recovery will have been suitably addressed and the Authority need not consider this item further.

## 5 AGIG Revised Final Plan

5.1 **Applause & Immature market development** - CPM would like to again applaud AGIG on the enormous amount of work done, in such a short period of time, and for involving stakeholders in that process. AGIG demonstrates conclusively that they truly are an intelligent sophisticated organisation with vast resources able to be drawn upon when required and able to develop detailed robust responses able to counter all components in the Draft Decision they were not comfortable with. The writer, somewhat envious, finds themselves alone and feeling a little overwhelmed with the volume of documents and data to interrogate so as to provide value adding contributions to this process. The writer wishes to submit an early apology to the Authority for the somewhat crude structure of this Extra Submission, for it being without footnote and other direct references for the matters being addressed and for it potentially appearing to have been compiled in a hurry. The writer's intentions remain honourable and on task to participate in developing this immature market by helping it to grow and become a "normal" market as best we can for we, as early architects, have a responsibility to those that come after us, to do all we can to accelerate this markets path to becoming normal.

5.2 **A qualification and overarching statement** on the contents of this Extra Submission; CPM highlight that there are around 18 documents and models that make up AGIG's Revised Final Plan, which were submitted by AGIG on the 8th October 2020 with public responses sought by ERA to be submitted by 04 Nov 2020. There is insufficient time available to do a thorough interrogation of all documents. As such CPM submits an overarching statement covering any and all items in the Revised Final Plan that are inconsistent with or conflict with or go against any component or components of the Requested Amendments set out in the Draft Decision; CPM state that unless specifically addressed in this Extra Submission, CPM does NOT support AGIG's position and respectfully requests the Authority adopt the provisions set out in their Draft Decision as appropriate to form part of the Final Decision.

5.3 **Reference Services T&Cs** – CPM submits that AGIG have chosen to reject many of the Requested Amendments for T&C changes across the suite of reference service agreements. CPM further submits that it supports the Authority and requests it seek for all Draft Decision T&C amendments proceed by being included for in the Final Decision.

5.4 **Reference Services T&Cs Revised Final Plan attachment 14.1A section 3** and Required Amendments 44, 45 & 46 – CPM submits that AGIG have ignored the facts in the Draft Decision on the missing words in clause 11.1 and Schedule 2, and how such came about. Instead AGIG have chosen an aggressive position that purports to support non-discriminative behaviour when in fact leaving the words out does the opposite. Other than 2019 when shippers first started using the Spot Transport market, for the many years prior AGIG were comfortable with clause 11.1 and Schedule 2 in driving the right behaviours on over running. The T&Cs have always contemplated what happens when an over run occurs, as is in the normal operation of a pipeline. For many years AGIG comfortably collected charges that applied a 15% premium on the price payable per GJ (from full haul and part haul customers alike with no discrimination) for overruns, it worked as intended, to be a behaviour modifier and an extra revenue source. CPM submits that both full haulers and part haulers have the same T&C's in their contracts, each suffers a penalty for over running and so they should. The discrimination occurs where full haulers are treated differently to part hauler in the outcomes of over running, one party continues to pay a 15% premium on the tariff they normally pay and the other must pay around a 1000% premium (but only if Spot has been bid otherwise its 15% premium). With abundant spare capacity in the north and for full haul capacity to the south on the DBNGP this "penalty" is a gross over charge.

5.5 **Reference Services T&Cs Revised Final Plan attachment 14.1A section 3** and Required Amendments 44, 45 & 46 – CPM submits that only Spot transport services are viable for full haulers which is another discrimination. Overrunning remains part of the day to day running of a pipeline but part haulers are grossly discriminated against. AGIG's many arguments sound convincing, but when placed against the back drop of an error in drafting, inadvertently occurring years in the past, the arguments become completely flawed and could be considered somewhat mischievous. CPM submit that the Authorities Draft Decision is the right and fair decision and should be upheld.

5.6 **Future Business Planning** – contemplating paragraph 5.4 and 5.5 above, in a hypothetical scenario, imagine you were a pipeline business with the T&C's as they are today (clause 11.1 and Schedule 2 inadvertently missing the distance factor adjustment wording that used to be there in the past), if that business were able to look ahead and see the contracted capacity future coming their way, they would know of the potential impacts the use of Spot capacity may have and the revenues it might produce, or the change in capacity contracting that it may drive and the revenue that that might produce. That business would want the market to start using the spot market. But how do you start to get a market that's never used Spot in the past to use Spot now? Good question and the marketing people in the room will put their hand up and say "make it cheaper so people will start to use it".

5.7 **Reference Services T&Cs Revised Final Plan attachment 14.1A section 3** and Required Amendments 44, 45 & 46 - CPM further submit that AGIG, being an intelligent and sophisticated business, is expected to be fully aware of where gas flows are going in the DBNGP and with the increasing volumes being drawn from the DBNGP in the north and decreasing volumes being delivered by NWS, together with large volume producer deliveries now coming into all parts of the DBNGP (top, bottom and multiple scattered through the middle), AGIG are able to see the opportunity this creates as full haulers capacity is diminishing and shippers are rightly relinquishing capacity they no longer need or can replace with bespoke capacity to match their supply contracts. AGIG need to look for opportunities for alternative services, as any intelligent business should do. That opportunity perhaps may not be regulated. Such is clever business but it should not come at the price of altering an historically accepted position on over running and in doing so discriminating against a particular customer group. CPM submits that should the Authority revise its Requested Amendments 45, 46 and 47 CPM respectfully request the Authority consider regulation of the Pilbara Service and any Pilbara Spot service and other services offered, such that the pricing for such services be delivered on an adjusted full haul tariff multiplied by the distance factor so that pricing links specifically to the distance gas must travel in the DBNGP thus aligning new Pilbara designed services with all other part haul and back haul services where distance factors drive tariff outcomes.

5.8 **Capacity and Throughput:** AGIG's Revised Final Plan challenges the Authorities Draft Decision forecast throughputs and contracted capacity and to some degree the challenge may be justified as is somewhat apparent in the actual contracted capacity data being presented by AGIG. Further to the Revised Final Plan AGIG also addressed stakeholder questions relating to Contracted Capacity in AA5, including providing high level details on contracts expiring in the AA5 Period and some assumptions of expected capacity continuing beyond the expiring date. AGIG states, in their summary, that very few contracts are expiring in AA5 Period and the remaining is "negligible (less than 10TJ) and the GBB data reconciles to within 15TJ. This item and others in this section with the same reference title, attempt to submit thoughts to the Authority for consideration in producing the Final Decision. Specifically in respect to the answers to stakeholder questions post submission of AGIG's Revised Final Plan; CPM wish to remind the Authority of the $'s those "negligible" and "less than 2.5%" that the combined 25TJ represents to the cost structure to run "our" pipeline: 25,000GJ x $1.44 x 365 days x 5 yrs = A$65.7m, so it goes without saying even small numbers in the gas transport market represent material dollars over a 5 year access period. Meaning that any over recovery that may result if the numbers are even mildly inflated can be material and so it will always be better to align business drivers by setting a higher revenue forecast to ensure a "keep it lean" financial management structure becomes required by AGIG to maintain reasonable returns to shareholders and a reasonable tariffs for its customers.

5.9 **Capacity and Throughput:** AGIG's answers to stakeholder questions shows a cumulative variance in Full Haul capacity from 2021 (592.25TJ/d) to 2025 (499.35TJ/d) to forecast a drop of 92.9TJ/d through AA5, driven, they say, entirely by the changing electricity market conditions in the SWIS and they refer to wind generation additions as examples driving reduced gas generation. CPM submits that this all seems reasonable until you bring in real market considerations and changing market conditions, and by market we mean the gas transport market. The gas transport market in WA has changed significantly in the past 5 to 10 years and continues to evolve, shippers are getting smarter and rightfully relinquishing long term over contracted capacity that is no longer utilised every day because there are other transport products that can be used like Spot Transport and bespoke services to help shippers optimise their gas transport costs. Spot transport use was incentivized by AGIG in late 2018 with a reduced price lower than the full haul tariff. Customers will and did take time to transition to using the Spot service when AGIG dropped the price in 2018 and other services because old long term contracts are just that long term and may be years away from terminating so in the interim shippers relinquish with a plan to use Spot when needed or establish new bespoke contracts for their required capacity needs. It is these new contracts and the use of Spot that the forecasts cannot predict and which should have some contribution to expectations of manifesting in the AA5 Period.

5.10 **Business Intelligence -** Gas consumption in WA is not going to reduce in the near term and gas transport capacity cost optimisation will always be something that shippers look for to help reduce costs going forward. AGIG, as an intelligent sophisticated business, is expected to develop services in a regulated environment that delivers maximum profits to their shareholders and so sees itself having to keep a step ahead of the regulator to achieve their corporate objectives. Sadly this model has fundamental business driver misalignment which can only land on an outcome that has either the seller or the buyer taking the only win. Extrapolating that result out can mean one party may go under, which is not what anyone wants. Unable to see the final cash outcomes of AA2, AA3 and AA4 and with the understanding that AGIG gets to keep any over recovery in those and future periods, at the effective detriment of the shippers; is a difficult pill to swallow, particularly when it is believed that the "cliff" after the bail out premium was paid by all shippers for 10 years is considered to have delivered AGIG many millions over the intended 300 the bail out targeted. CPM submit their support for the Authority's position on anticipated revenues and the tariff outcomes that such produces. CPM also submit its support for the Authority and AGIG to improve on the current regulated model and adjust to a more transparent and fully open book structure with KPIs and checks and balances adopted to align business drivers and reconcile bi-annually, as such may help improve the outcomes for both parties and reflect more an "owner" engaging an operator under a performance based operator services model, which may very well allow the development of the WA gas market that eventually sees the DBNGP become the domestic gas "hub" its destined to become, where AGIG can charge all shippers based on the actual costs to transport their gas the actual distance their gas "travels" in the pipe on a virtual molecule distance movement basis from the delivery inlet point to the extraction outlet point. WA is a market like no other and could have a hub like no other, Henry has a hub in the US, WA should be striving to develop a domestic gas supply hub, perhaps it could be called the "Dom Hub"

5.11 **Rebateable Services** – AGIG Foreword in the Revised Final Plan, somewhat ratifies some statements in this Extra Submission about changing gas transport market dynamics, where it says "*As the use of some non-reference services increases we are proposing that four services be specified as rebateable services*". CPM submits that this is evidence of the fact that AGIG are fully aware of the changes occurring in gas transport contracting strategies. It goes on to say that "*this approach will ensure users of reference services are fairly and adequately compensated for any shared cost they incur, but only if demand for these rebateable services is not included in calculating reference tariffs*". CPM submits that all revenues, received from shippers paying to deliver, receive or transport gas in "our" pipeline, should be included in the wash up used to determine fair and reasonable tariffs for all users of "our" pipeline.

5.12 **AGIG Proposed Tariff** - CPM submit that the tariffs proposed by AGIG are again considered too high and do not account for the total of the expected fall in tariffs following the expiry of the negotiated inflated tariff resulting from the bail out of the DBNGP in 2004. AA4 ERA final decision captured and removed a portion of the recovery premium paid by shippers in the bail out of Epic Energy (historically referred to the "cliff" that would occur) however CPM believe AA4 tariff reduction did not go low enough so there should be further reductions applied in AA5 and such just may mean AGIG have to hone their skills in cost optimisations and belt tightening to deliver the same quality outcomes for users and maintain the healthy margin they seek for their shareholders. CPM respectfully suggest the Authority consider finalising the "cliff adjustment" by reconciling fully the increased profits taken by AGIG through AA2 and AA3 via the recovery premium and increased revenues taken through AA4 due to the cliff not dropping the tariff far enough and from recontracted parties. For ease of finding the details of the cliff CPM has included the AGIG Tariff History herein as Appendix 1 and notes it also formed part of its Initial Submission.

5.13 **AGIG Proposed Tariff Required Amendment 7** - CPM submits a somewhat empathetic position in respect to the Authorities Draft Decision on capacity AGIG must use in their modelling. AGIG's Revised Final Plan uses 601TJ Contracted Capacity and the Authority is directing a volume of 763TJ be fixed for AA5. It is suggested that both of these are likely to be incorrect at the end of AA5, however this process requires a figure to be used for the Final Decision. CPM submits that the difficulties in forecasting accurately will always challenge the robustness of any Access Arrangement process and in saying so CPM suggest using the midpoint of these 2 figures, as such gives rise to the validity and accuracy of both forecasts. Accordingly CPM submit that a contracted capacity figure of 682TJ be used and included for in the Final Decision. This midpoint figure will assist in aligning business drivers on lower tariffs for users (to complete the cliff drop) and increases revenues from those calculated using the tariff in the Draft Decision, together with supporting the position AGIG have taken in accepting that 70% of other services revenues will be measured and rebateable to shippers throughout the AA5 Period.

5.14 **Depreciation –** whilst it is accepted that an accelerated depreciation may be applicable in the general sense, CPM wish to reiterate its belief that it is too early to adopt such for AA5 on the basis that what will be happening in 2026 is an unknown let alone 2050. There is an expectation that the Sino Iron operations will need a natural gas supply available from the DBNGP for the long term way beyond that proposed by AGIG, therefore CPM suggest the Authority consider a 2070 timeline for depreciation to apply for AA5 and for the acceleration to again be considered in the next review in AA6.

## Appendix 1 – AGIG Tariff History

1. In 1998, Epic Group purchased the DBNGP for approximately $2.4 billion as part of the then State Government's privatisation process.[1]

2. The Authority determined, in its approved Access Arrangement for the period of 2000-2004, that the initial capital base of the DBNGP was approximately $1.55 billion[2] – roughly $300 million less than the debt Epic owed to the consortium of banks to finance the purchase of the pipeline. Epic consequently entered insolvency which created the need for an acquisition of the pipeline on terms that would see the banks recover the debt owing to them.

3. Macquarie developed a pipeline "rescue deal" that featured the following:

    a) the DBNGP Consortium (comprising DUET, Alinta Limited and Alcoa of Australia Limited), referred to here as " AGIG", purchased the pipeline for $1.86 billion.[3] The purchase allowed the banks to recover the full amount owing to them and effectively released the pipeline from Epic Energy's insolvency; and

    b) the major shippers on the DBNGP entered negotiations with AGIG to secure long term capacity rights in the DBNGP and major capacity expansions. The negotiations continued intensively up to the execution of a new suite of contracts by all major shippers and AGIG in October 2004 which came to be known as the "standard shipper contracts" (**SSC's**).

4. The SSC's accounted for approximately 95% of the then current pipeline capacity, and specified an agreed tariff profile for a term of 11 years until 2016, after which the tariff was to revert to the Reference Tariff established by the Authority under an approved Access Arrangement at that time.[4]

5. Three important outcomes of the rescue deal were that:

    a) the tariff payable by shippers under their SSC's was higher than the reference tariff forecast to be approved by the Authority for the period from 2004 to 2016; [5]

    b) the quantum of the tariff over-payment was intended to equal the roughly $300m shortfall;[6] and

    c) the intention of the parties entering into the SSC's on the date of executing the SSC was that, with effect from 1 January 2016, the base tariff would be adjusted so that the base T1 tariff, T1 capacity reservation tariff and T1 commodity tariff fell back to the level of the firm service Reference Tariff.[7] It was expected that on 1 January 2016 the applicable regulated tariff would be substantially lower than the inflated contractual tariff.

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[1] Alcoa World Alumina Australia, *Submission to the Productivity Commission on the Review of the National Third Party Access Regime for Natural Gas Pipelines*, 15 September 2003, available at: http://www.pc.gov.au/inquiries/completed/gas/submissions/alcoa_world_alumina_australia/sub065.pdf

[2] Economic Regulation Authority, *Approved Access Arrangement for the Dampier to Bunbury Natural Gas Pipeline*, 30 December 2003, page 13

[3] The Age, *Pipeline epic to end*, 26 October 2004, available at: http://www.theage.com.au/articles/2004/10/25/1098667688219.html?from=moreStories

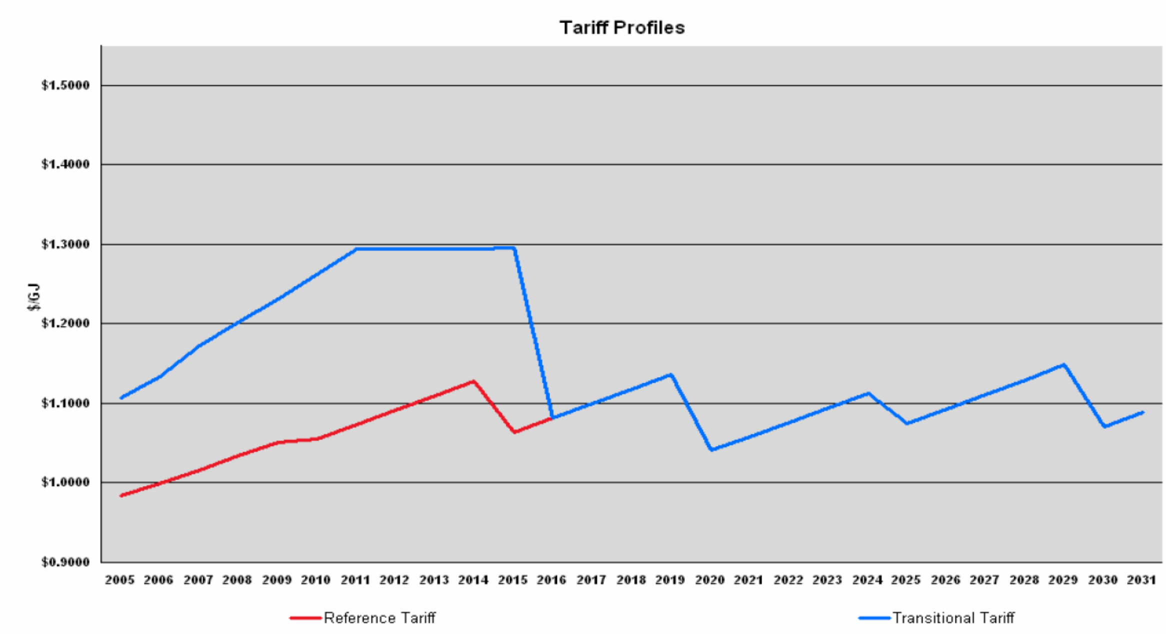
[4] Diversified Utility and Energy Trusts (DUET), *Product Disclosure Statement*, 19 November 2004, pages 45, 47

[5] Ibid, page 46.

[6] Ibid, page 46.

[7] Ibid, page 153.

6. The expectation of the parties entering into the SSC's as to the future tariff path was enshrined by including the tariff model in the SSC's themselves - the "tariff cliff" that shippers and the pipeline owner expected to occur at the beginning of 2016 was represented in the following graph that has been taken from the 2004 SSC:




7. From one perspective, the 2004 negotiations and parties' expectations are ancient history, and the ERA's job is simply to apply the NGL and NGR in this reset to determine the appropriate reference tariff for the coming access arrangement period.

8. But CPM submits that the history is relevant for 2 reasons:

   a) First, it is important to remember that the contractual tariff being paid by most shippers before this reset (or immediately before the 2014 recontracting), is an artificially inflated tariff imposed to allow the pipeline's rescue from insolvency, and is a wholly inappropriate comparator for determining whether there is an upwards or downwards "tariff shock" as a result of the current reset.

   b) Second, more generally, CPM submits that the NGO will be best served if AGIG is held to the spirit of the 2004 rescue. The essence of the deal in 2004 was that shippers would pay an upfront premium tariff to pay out the banks, with a promise of tariff relief from 2016 onwards. The concern among shippers at the time was that AGIG may try to capture the up-front benefit but avoid the post-2016 cost, by shaping its tariff path and regulatory activity in the intervening years in a way which caused the post-2016 result to be more favourable to it than the original bargain. CPM submits that if the ERA were to allow that outcome, it would undermine the reason for the shippers' paying the premium tariff in the early years, would undermine the commercial deal and hence disincentivise other such commercial transactions in the future, and it would certainly not be in the long term interests of shippers as required by the NGO. CPM also submit that the AA4 tariff adjustment did not fully capture the full reduction needed to correct fully.