Kleenheat

Economic Regulation Authority
Level 4, Albert Facey House
469 Wellington Street
Perth
Western Australia 6000

4 November 2020

Re: Wesfarmers Energy (Gas Sales) Limited submission on the proposed Dampier to Bunbury Natural Gas Pipeline Access Arrangement (2021-2025) and the Revised Final Plan

Dear Sir/Madam,

Wesfarmers Energy (Gas Sales) Limited ("WEGS") purchases and transports natural gas for the manufacture of LNG, LPG, Ammonia and Sodium Cyanide; and, for the on-sale to commercial, industrial, small-to-medium-enterprise and residential customers in WA. WEGS holds its transportation agreements with the group of companies that own and operate the DBNGP, now collectively called Australian Gas Infrastructure Group ("AGIG") and manages the supply and transportation optimisation for the following entities:

- CSBP Limited;
- Wesfarmers Gas Limited; and
- Kleenheat Gas Pty Ltd.

WEGS appreciates the opportunity to comment on the Economic Regulation Authority's ("ERA") draft decision of 14 August 2020 ("Draft Decision") on AGIG's proposed revisions to the Dampier to Bunbury Natural Gas Pipeline ("DBNGP") Access Arrangement for 2021-2025 ("AA5") and to AGIG's Revised Final Plan for AA5 submitted to the ERA on 7 October 2020 in response to the Draft Decision ("Final Plan").

WEGS notes that in assessing the Final Plan, the ERA must apply the provisions of the National Gas Law ("NGL") and National Gas Rules ("NGR"). WEGS remains concerned about AGIG's revised contracted capacity and throughput forecasts included

Building 161, Car Park 12,
Murdoch University, Murdoch WA 6150

PO Box 4184,
Myaree Business Centre WA 6960

P 08 9312 9333 | F 08 9312 9833
kleenheat.com.au

in the Final Plan as well as the contribution of the Peaking Service to the costs of the pipeline and has structured its submission on three key issues:

1. Composition and transparency of AA4 capacity and throughput and AA5 assumptions
2. Peaking Service and its contribution to pipeline costs
3. Cross subsidisation of the cost of flexibility

Composition and transparency of AA4 capacity and throughput and AA5 assumptions (Issue 1)

Reduction in subscribed capacity will likely cause demand for new services, including new T1 service.

a) WEGS understands that changes to electricity generation in Western Australia and to the natural gas market are prompting gas shippers to seek flexibility and optimise their gas supply and transportation portfolios. AGIG has proactively responded to these needs by offering flexibility:
   i. In the movement of gas: as exemplified by the Pilbara Service, allowing Part Haul and Back Haul users more flexibility of inlet and outlet points.
   ii. In accommodating the volatile usage of firm transport capacity: as exemplified by the Peaking Service which is understood to be offered on a lower reservation and higher commodity charge basis.

b) As expressed in WesCEF's first submission[1], WEGS holds the view that the utilisation factor of electricity generators' T1 gas transmission capacity may decrease for some time (prior to the closure of Muja C) as a result of a lower utilisation of their generation assets in the West Australian Electricity Market (WEM).

c) While this information has not been included by AGIG in the publicly available information it has provided in response to the Draft Decision, WEGS submits that it is reasonable to assume that a portion of the reduction in the capacity forecasts that AGIG proposes in its Final Plan for AA5 (relative to the levels in AA4) is attributable to the contracted capacity that was held by major shippers but actually utilised by third parties in AA4. WEGS urges the ERA to:
   i. enquire of AGIG the extent to which contracted capacity of each major

[1] https://www.erawa.com.au/cproot/21146/2/Wesfarmers-Chemicals-Energy-and-Fertilisers.pdf

shipper during AA4 was, in fact, used by a third party during AA4;

ii. enquire of AGIG whether the forecast contracted capacity during AA5 of each major shipper includes capacity to be used by a third party and the extent to which the levels of third party contracted capacity forecast for AA5 are less than the levels in AA4; and

iii. include in the Contracted Capacity forecast for AA5 an amount at least equal to this difference as these entities will need a substitute service from the pipeline operator.

d) From its presence in the Wholesale and Retail gas markets in the South West of Western Australia, WEGS has observed that power generators have regularly offered wholesale transport services and gas supply and transport solutions to retail gas customers and wholesale traders using the generator's own T1 contracted capacity. As power generators set their T1 capacity subscriptions closer to their average power station gas requirements, it is reasonable to assume that both natural gas retailers and wholesale traders will therefore need to take up T1 capacity through other means along with some commitments for the Peaking Service.

e) As capacity and throughput for AA5 are forecasts, Rule 74 of the NGR requires that they:

i. be supported by a statement of the basis of the forecast or estimate;

ii. be arrived at on a reasonable basis; and

iii. represent the best forecast or estimate possible in the circumstances.

f) WEGS believes that not only is it clear that this third party capacity will be transferred to another service in AA5 but that the basis to establish the quantity is relatively straightforward; and should not be assumed to be zero.

g) WEGS has reviewed the distribution of natural gas consumption by electricity generation in the South West and Metro regions of the State[2] and concludes that over the last 12 months, this class of users has consumed on average 151TJ/d, the P90 and maximum gas consumption of these users has been 201TJ/d and 276TJ/d respectively. WEGS also notes that the consumption of this class of users above their average demand has been 12.5TJ/d.

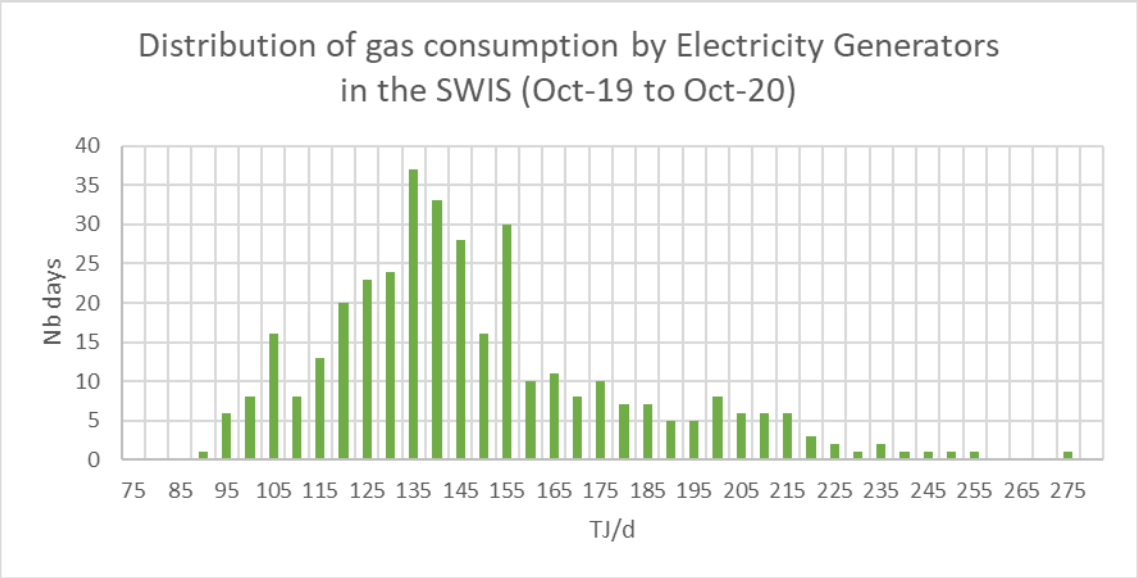
h) As AGIG has proposed to re-align its forecasts of contracted capacity for AA5 closer to its average estimated throughput, WEGS believes it is important to not

[2] WA Gas Bulletin Board: https://aemo.com.au/en/energy-systems/gas/wa-gas-bulletin-board-wa-gbb

lose sight of:

i. AGIG's ability to estimate future peaking throughput of at least 12.5TJ/d and likely growing with AGIG's expected increase in electricity market volatility.

ii. AGIG's need to reserve up to 125TJ/d of additional full haul capacity in order the meet the maximum requirements of its future Peaker Service customers.



Source: Gas Bulletin Board WA.

Forecasts are inconsistently using known and assumed contract assumptions.

i) WEGS notes that AGIG has proposed to use "known" contracted capacity to inform its forecasts of demand. AGIG claims this information to be "known and not controversial".

j) However, WEGS does note that AGIG has ***assumed*** that Part Haul capacity would substitute Full Haul capacity as a direct result of supply increases from the Perth Basin. However, WEGS believes that:

i. The Perth Basin is still at very early stages of exploration and is operating at depths that far exceed sectoral standards. The uncertainty of its exploration pathway and future development may warrant the same prudence in determining its impact on contracted capacity as does the uncertainty of subscription and usage of the Peaking Service by gas fired generators.

ii. AGIG makes the assumption that shippers will maximise the relinquishment of their Full Haul contracted capacity during AA5, however it is not clear how AGIG has formed this assumption particularly when WEGS understands that AGIG has not made direct enquiries from shippers on this issue. It is not apparent that adopting this assumption in deriving its forecasts is evidence that AGIG's forecasts are either arrived at on a reasonable basis or that they represent the best forecast or estimate possible in the circumstances.

k) Finally, WEGS notes (obviously referring to Alcoa) that "the effect of one of the shipper's announcement is that 50TJ/d shifts from Full Haul to Part Haul from 2024 ***for regulatory purposes***"[3]. WEGS urges the ERA to review the contractual rights of Alcoa under its contract to switch Full Haul capacity to Part Haul capacity to assess whether the provisions entitle it to use that capacity (or some of it) as full haul capacity and for AGIG to levy charges as if it were Full Haul capacity. If that is the position, the relevant amount of capacity should be treated as full haul capacity for regulatory purposes as AGIG would have to ensure that capacity was always available as full haul capacity and it would not otherwise be accessible for a full haul service by a prospective shipper.

l) AGIG reports a reduction in forecast Full Haul capacity from 718TJ/d in CY20 to 592TJ/d in CY21. From its understanding of shippers' contractual rights, WEGS calculates that the maximum relinquishment capability of shippers may result in a level of contracted capacity in CY21 that is closer to 645TJ/d should those shippers that are gas-fired generators wish to relinquish capacity. In the subsequent year, WEGS understands T1 capacity may be further relinquished to the level expected by AGIG (582TJ/d). WEGS would expect the ERA to test the accuracy of this by reviewing all gas transportation contracts that contain a right of the shipper to relinquish contracted capacity.

m) WEGS notes that AGIG has assumed a loss of Full Haul capacity equal to the "Parmelia deliveries"[4]. AGIG's assumption is 33TJ/d over the plan. However, WEGS is of the view that AGIG will not lose transportation services to the Parmelia pipeline beyond the forecasted production level of the Beharra Springs production facility. This is so for the following reasons:

i. currently, the Beharra Springs plant is the only plant connected to the Parmelia pipeline. Any other gas transported through the Parmelia

[3] Shipper Round table Meeting 12 – Follow up notes dated 26th October 2020.
[4] Same.

pipeline must first be delivered into this pipeline by the DBNGP,

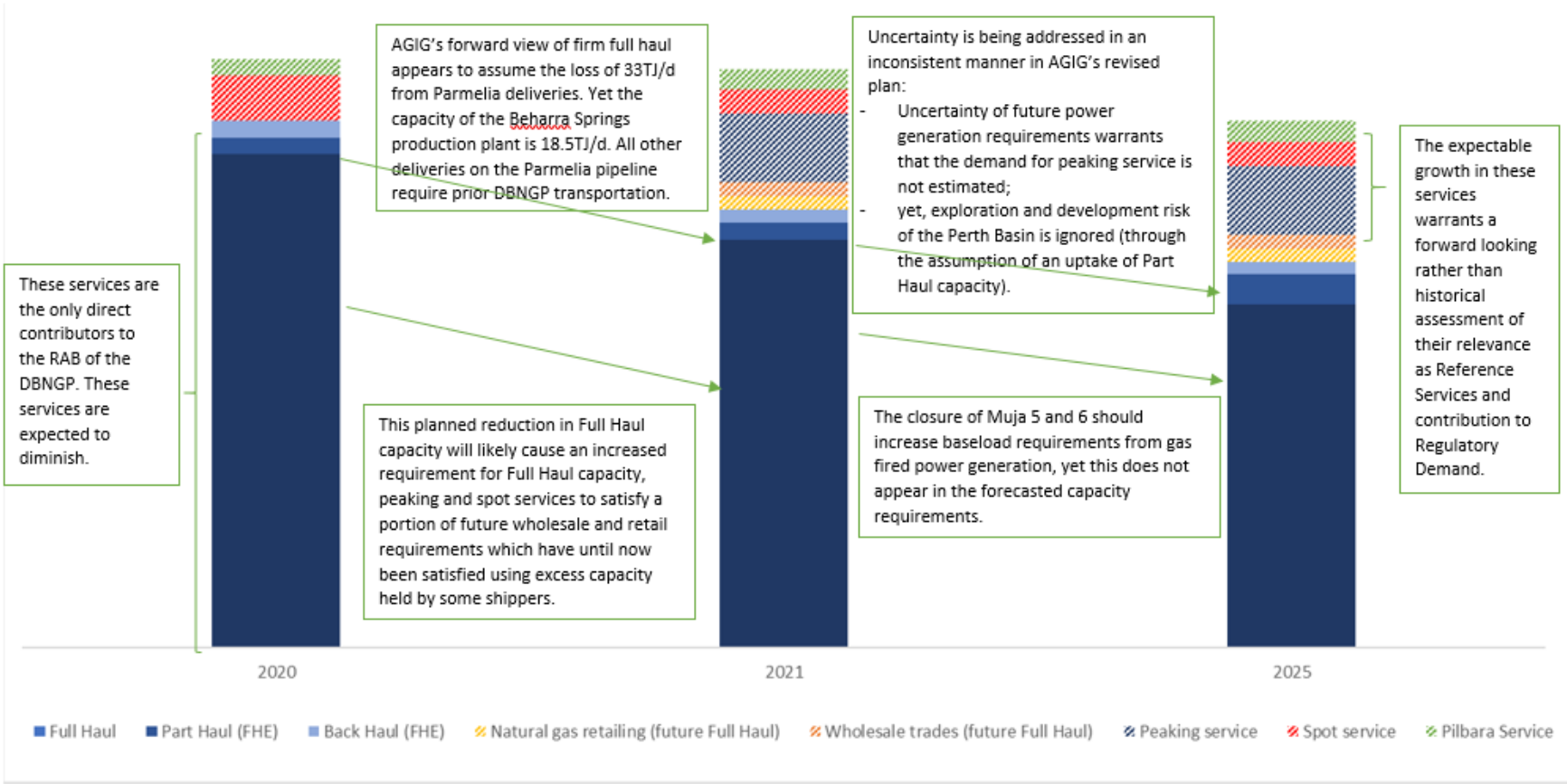
ii. this plant has a production capacity of 18.5TJ/d, and

iii. Beach Energy has only announced a supply agreement of 10TJ/d from this plant starting Q3 FY21 with Alinta.

n) Given the above, it may be a more reasonable estimate or forecast in the circumstances to assume that, during AA5, the plant will be producing at levels between the Alinta contract (ie 10 TJ/d) and plant capacity (ie 18.5TJ/d) and so, the loss of Full Haul capacity attributable to the Parmelia pipeline should be somewhere in between these two figures, rather than 33TJ/d. This would lead to an increase of between 15 and 23TJ/d in demand for Full Haul capacity during AA5.

o) WEGS does not observe a rise in gas usage assumptions arising from the closure of Muja C across CY22 and CY24 in AGIG's forecasts. As mentioned in its earlier submission, WEGS also believes this reduction in coal fired generation will prompt an increased baseload usage of gas fired generation which in turn will attract interest for Full Haul capacity.

The graph proposed below provides a visual summary of the effects on AGIG's forecast of contracted capacity:



Graph for illustration purposes only.

Peaking Service contribution to pipeline costs (Issue 2)

Defining the Peaking Service.

a) WEGS understands that the Peaking Service would have the following attributes:
    a. Its tariff would be set at a premium to the T1 reference tariff, circa 115%.
    b. The tariff would be "largely based on throughput"[5]. WEGS believes it is reasonable to conclude that its reservation component would be 20% of the tariff and its commodity component would be 80% of the tariff.
    c. It would rank at the same level as "Other Reserved Services" in priority and curtailment, that is, it would offer its users a lower firmness than reference services, yet it would rank ahead of the Spot Service.

b) While primarily requested by gas fired power generators, WEGS understands this service may be available on a stand-alone basis to any shipper that may request it.

c) From this, WEGS concludes that this service will largely offer shippers whose utilisation rate of contracted capacity is low, an opportunity to reduce their net cost of access to pipeline capacity.

Contribution of the Peaking Service to pipeline costs.

d) AGIG proposes to distinguish this service from the reference services on the basis that it does not meet the Service Factors. More specifically, it becomes apparent that the distinction of this service from the T1 service is on the basis that this service is not offered on the same firmness.

e) However, WEGS submits that at times where AGIG has been able to demonstrate that forecast demand for Full Haul Services during AA5 is highly unlikely to reach anywhere near the pipeline's rated capacity and given the obligations of AGIG under the section 133 of the NGL to not prevent or hinder access to a pipeline service by means of a covered pipeline[6], consideration of firmness of a service, at least for the duration of AA5, becomes a theoretical distinction rather than an operational one. Further to this point (and to WEGS's

[5] Shipper Round table Meeting 12 – Follow up notes dated 26th October 2020.
[6] Note in particular section 133(5)(a) of the NGL provides that "a reference to engaging in conduct is a reference to doing or refusing to do any act, including refusing to supply a pipeline service or, without reasonable grounds, limiting or disrupting a pipeline service, or making, or giving effect to, a provision of, a contract or arrangement, arriving at, or giving effect to, a provision of, an understanding or requiring the giving of, or giving, a covenant."

concern), WEGS notes in AGIG's Final Plan that under the queuing requirements, AGIG proposes to "maintain a single queue for access to Reference Services and Non-Reference Services that are Haulage Services (Queue)". On this basis, WEGS believes that the Peaking Service may reasonably be considered a firm service for the purpose of AA5 determination.

f) AGIG is proposing a forecast of capacity assumptions that align closely to the average forecast throughput of shippers. WEGS believes this assumption to be inconsistent with the pipeline capacity requirements of electricity generators (for the reasons stated above but which are summarised as follows):
    a. The recent historical gas usage data of electricity generators demonstrates the need for contracted capacity to consistently be approximately 125TJ/d above average usage.
    b. Further, AGIG has consistently presented its understanding that gas fired electricity generators require not only increasing yearly flexibility (low utilisation rate of their daily capacity subscription), but also greater intra-day flexibility (as demonstrated anecdotally by AGIG in its plans).

g) Under its rebate proposal, AGIG suggests that the "costs associated with providing this service [are] likely incremental costs only because the service [does] not require new capital expenditure"[7]. From the view it presented above, WEGS strongly disagrees and believes instead that this service may only be delivered by AGIG to its customers by operating and maintaining the required capacity of the pipeline.

h) From another angle, WEGS believes that, should the pipeline be rightly sized to the ***average throughput*** of its shippers as presented by AGIG, it would become apparent that users which are now forecasted to request access to the Peaking Service from AGIG would instead secure the corresponding reference service and thereby contribute to the full costs (capital and operating expenses) of the pipeline. In WEGS's view, this supports the argument that, while the Peaking Service may not necessarily be classified yet as a Reference Service, the estimated contracted capacity under this service should be counted as if it were equivalent to the capacity and throughput for each relevant reference service on the pipeline so that the users of the Peaking Service equally share the costs of providing services on the pipeline with Reference Service users. This would ensure consistency with Rule 93 of the NGR. WEGS would however agree to AGIG's point that, should this service be included in the forecasted

[7] ERA Draft Decision.

demand, AGIG should not be required to rebate the revenues derived from this service to its Reference Service customers.

i) Finally, WEGS believes that a similar argument applies to the Pilbara Service proposed by AGIG.

Inconsistency in AGIG's approach to rebating the revenues of its non-reference services.

j) AGIG has submitted that the revenues derived from rebateable, non-reference services including Peaking Service and the Pilbara Service should be rebated to Reference Service shippers on a 70/30 split. AGIG claims that "the costs associated with providing [the Peaking] service [are] likely incremental costs only because the service [does] not require new capital expenditure. Incremental costs would include fuel gas and the increased impact on volume driven tasks such as turbine overhaul operating costs"[8].

k) WEGS has demonstrated above its disagreement with the fact these services may not need to contribute to the full (capital and operational) costs of the pipeline where predicted spare capacity renders such "interruptible" services as firm as reference services.

l) If however, the ERA does not accept this submission and is inclined to retain the rebateable non-reference services as per the Draft Decision, WEGS submits that allowing AGIG to retain 30% of the revenue earned from the sale of these services is not consistent with the NGR. AGIG's suggestion that 30% of the revenues of the Peaking service should allow it to cover its variable costs in respect of that service is unacceptably inconsistent with AGIG's other submissions that, for the delivery of its Reference Services, AGIG incurs a variable cost of only 6% of the tariff. AGIG has consistently proposed that only its System Use Gas be used to determine its variable costs and therefore the commodity charge of Reference Services. In suggesting to retain 30% of Peaking Service and Pilbara Service Revenues, AGIG is considering that these services cause other incremental costs such as turbine overhauls which WEGS had brought to the ERA's attention in its first submission.

m) WEGS holds the view that, should a rebate mechanism apply to these non-reference services revenues, it should be based on a 94% redistribution to reference service customers.

[8] ERA Draft Decision.

Cross subsidy between the natural gas and electricity markets (Issue 3)

a) WEGS strongly welcomes product and service innovation. The Peaking Service seems to arise from the need of power generators to access pipeline capacity on an irregular basis. However, WEGS believes that the way and context in which this service is being offered simply reduces the cost contribution of the Peaking Service customers towards the costs of the pipeline.

b) In its first submission, WesCEF had proposed that users of the Full Haul T1 service be separated in different classes reflecting their use of the pipeline:
   a. the baseload users with a steady and predictable gas load, and
   b. the peak users with less predictable within year and intra-day peak requirements, consuming on average less than their maximum requirements.

   WEGS notes that in the Draft Decision, the ERA has rejected WesCEF's proposal on the basis that "while electricity generators may not use the DBNGP in the same manner as other customers, it is not in the long-term interests of industrial, commercial and residential customers (as referred to by WesCEF) to set higher reference tariffs for electricity customers, which may create a perverse incentive for them to reduce their consumption".

c) WEGS does not challenge the ERA's decision in this respect but submits that, as a result of allowing non-reference services to be offered by AGIG on a pipeline that holds significant spare capacity and maintaining a calculation of the reference tariff only by counting the predictable reference service demand, it is causing the baseload and predictable users of the pipeline to pay a higher tariff for access to capacity than the peak users of the pipeline. WEGS's high level example below directly demonstrates that access to capacity on the pipeline is significantly cheaper for peak users than for users of the T1 reference service.

The table below illustrates, using simplified assumptions, that the cost of access to capacity is comparatively low for "Gas for Power Generation" shippers ($0.99/GJ) vs baseload industry users ($1.44/GJ). It also demonstrates that the rebate mechanism does not equalise this tariff difference amongst classes of shippers.

Assumptions	Level	Reservation	Commodity
T1 tariff	$ 1.44	94%	6%
Peak tariff	$ 1.66	20%	80%
Rebated Non-Ref Services	70%		

	Average forecast use 2020	Use above average	Max use	Service subscribed	Reservation	Commodity	Average cost of transport	Average cost of access to capacity
	TJ/d	TJ/d	TJ/d	class	$/GJ	$/GJ	$/GJ transport	$/GJ reserved
Mineral processing	305	-	305	T1	$ 1.35	$ 0.09	$ 1.44	$ 1.44
Mining	15	-	15		$ 1.35	$ 0.09	$ 1.44	$ 1.44
Industrial	60	-	60		$ 1.35	$ 0.09	$ 1.44	$ 1.44
GPG	150	12	275	T1 and Peaking	$ 0.89	$ 0.19	$ 1.82	$ 0.99
Distribution	73	7	112		$ 1.00	$ 0.21	$ 1.74	$ 1.13
Total usage	603	19	767					

Rebate value	$/T1/day	0.04

Volumes interpreted from Figure 7 of Attachment 11.3 and historical GBB data

d) Moreover, WEGS notes that gas fired power generators have avenues to recover their cost of gas flexibility:
    a. Gas fired power generators may be able to price their cost of gas flexibility in their electricity Short Run Marginal Cost in the WEM. In fact, WEGS holds the view that generators will increasingly be able to do so under the current WEM Rules as they are exposed to a higher variable tariff and a lower fixed tariff for the use of gas transmission flexibility.
    b. Gas fired power generators forming part of the WEM have access to a capacity credit market which provides them with financial support on their fixed operating costs, including fuel supply costs.
e) On the contrary, much of the gas consuming industry subscribing to the Reference Services is export facing and does not have the commercial ability to pass-through the increasing cost of gas transmission. A failure to recognise the cost contribution of the power generation industry to its appropriate level of reservation of gas transmission capacity may increase the cost pressure on Reference Service holders to the extent that their gas demand may be in question.

WEGS has commented only on certain issues arising from the Final Plan, and the absence of a comment on any specific issue should not be taken to indicate that WEGS supports that particular issue. To the contrary, WEGS endorses the position reached by the ERA in the Draft Decision on each particular issue.

As was the case with respect to AGIG's initial proposal the comments above have been provided in good faith and reflect WEGS's broad view on the Final Plan proposed by AGIG for AA5. They are not intended to be used as expert technical advice; but to provide comments for consideration by the ERA in reviewing the Final Plan.

Should you wish to discuss any points raised in this submission please contact Vincent Blondeau on [redacted] or Hans Niklasson on [redacted]

Yours sincerely,

[redacted]

Mark Gadsby
General Manager
Wesfarmers Kleenheat Gas Pty Ltd