

4/53/8-K2
David Randle
9486 3240

3 March 2000

Mr Mike Jansen
Office of Gas Access Regulation
Level 6, Governor Stirling Tower
197 St George's Terrace
Perth WA 6000

Dear Mr Jansen

AlintaGas's Submission on GGT's Goldfields Gas Pipeline Access Arrangement

I refer to the *Goldfields Gas Pipeline Access Arrangement* submitted to the Regulator by Goldfields Gas Transmission Pty Ltd ("GGT") dated 15 December 1999, and to the Regulator's Invitation for Public Submissions.

This Submission is provided from the perspective of AlintaGas's Trading Business, which procures, ships and markets natural gas. These activities are separate from the distribution of natural gas, which is the responsibility of AlintaGas's Distribution Business.

AlintaGas considers that GGT has taken a positive approach in its proposed Access Arrangement by basing its Reference Service upon the existing firm service that GGT offers to users.

This is the first time that GGT's firm service has been subject to review in a public consultation process by an independent regulator. AlintaGas welcomes such a review. It provides the opportunity for the Regulator to scrutinise a number of aspects of GGT's existing firm service. AlintaGas considers that a number of the existing terms and conditions and pricing favour GGT, which AlintaGas submits is unacceptable in accordance with the National Access Code. In its proposed Access Arrangement, GGT has incorporated factors not included with GGT's existing firm service that further imbalance the arrangements in GGT's favour. An example is the proposed imposition of charges, which AlintaGas considers are in the nature of penalties (see below).

AlintaGas has a number of specific comments concerning GGT's proposed Access Arrangement. These comments are given below. AlintaGas requests that the Regulator address each issue to ensure compliance with the National Access Code.

Specific comments are not provided on a number of issues, such as GGT's demand forecast during the Access Arrangement Period. However, it should not be inferred, simply because AlintaGas has not commented on an issue, that AlintaGas supports the issue. AlintaGas encourages the Regulator to review all aspects of the proposed Access Arrangement and to develop a decision that takes into account the matters specified in the National Access Code to ensure an appropriate balance between the interests of GGT and users of the GGT pipeline.

1. Charges

GGT proposes to impose charges, at GGT's discretion, if a user exceeds the limits set on the Accumulated Imbalance, Hourly Overrun and Variance Quantities.

AlintaGas submits that charges should not be imposed unless GGT can demonstrate that a user is consistently and excessively exceeding the limits and GGT is incurring additional costs that it is otherwise unable to recover. Furthermore, where these circumstances are met, the amount of the charge should be the additional cost incurred by GGT that could not otherwise be recovered. AlintaGas contends that the charges proposed by GGT are excessive as they exceed the costs GGT incurs in providing the service. In addition, before Hourly Overrun Charges are imposed, AlintaGas submits that users should have timely access to appropriate data to enable users to manage their daily demand profiles.

In the Sixth Schedule of the General Terms and Conditions, GGT proposes that it may vary a number of the charges for the firm service by notice in writing to all users. AlintaGas submits that GGT should not be able to modify or substitute the charges without the prior written approval of the Regulator.

The imposition of charges that exceed GGT's cost of providing the service could result in users reserving additional firm capacity as a way to mitigate the impact of the charges. This would be an inefficient use of resources.

Furthermore, GGT states:

“Quantity Variation Charges are intended to constitute a potential disincentive to Users which do not utilise the Pipeline in the manner intended.” (Section 9.6 of the General Terms and Conditions).

Contractual provisions intended to have penal or coercive effect are likely to be unlawful. AlintaGas requests the Regulator to review all proposed charges in this context.

2. Escalation rate

In section 9.8 of the General Terms and Conditions, GGT is proposing to escalate all of its charges at 100% of the quarterly change in CPI. AlintaGas considers this to be excessive. Contrary to the objective set out in section 8.1(f) of the National Access Code, such escalation does not provide GGT with an incentive to reduce its operating costs and does not provide a reducing price path for users.

AlintaGas submits that the escalation of prices using a CPI mechanism is acceptable if it is a properly designed incentive mechanism. However, AlintaGas submits that it is inappropriate for GGT's charges to be escalated at 100% of CPI in the first two or three years of the Access Arrangement Period because of the impact of a Goods and Services Tax ("GST"). Escalation should be such that it nullifies the impact of the GST and then it provides an incentive mechanism. Additionally, to the extent that increases in CPI are linked to the costs of borrowing, GGT already receives compensation for CPI increases through the weighted average cost of capital.

3. Uniqueness of the GGT pipeline

GGT suggests the circumstances that apply to the GGT pipeline are unique within Australian transmission pipelines. GGT uses this uniqueness to propose risk factors such as an equity beta of 1.4 that AlintaGas considers are excessive.

GGT suggests that the risk profile it faces is similar to that of the industries it serves. AlintaGas submits that such a proposal is wrong. GGT states at section 11.1 of its proposed Access Arrangement that the GGT pipeline is a contract carriage pipeline. As such, GGT requires users to contract for firm capacity. In so doing, GGT significantly reduces its own risks by transferring market risk onto the mining companies that use the GGT pipeline. The contracts insulate GGT from the various risks that a mining company faces, such as volatile commodity prices. Such volatility is reflected in the variability of return received by equity investors in the mining projects, but this does not flow through to any variability of return to the GGT as pipeline operator. Furthermore, under section 9.3 of the proposed general terms and conditions, the Toll Charge and Capacity Reservation Charge are fixed charges payable monthly, whether or not the User delivers or accepts gas under the Service Agreement.

Further, GGT is not exposed to an excessive amount of default risk. Mining companies tend to have lower gearing levels than pipeline operators. There is thus less risk that the mining companies will default on their bank loans and hence less risk that they will default on their contractual commitments to GGT.

In addition, GGT contracts with a number of mining companies who do not all produce the same minerals. This provides GGT with supply diversity and further insulates GGT from the risks faced by the individual companies.

GGT also suggests that an additional risk uniquely faced by GGT is that it does not hold any gas transportation contracts whose remaining life is in excess of 20 years. AlintaGas submits that the lack of a contract for a term of 20 years or more is not unusual. Rather, AlintaGas considers it unusual for a user to contract for pipeline capacity for a term in excess of 20 years. As an example, AlintaGas's contracts on the Dampier to Bunbury Natural Gas Pipeline are for less than 20 years. In AlintaGas's view, the lack of long-term transport contracts does not mean that the GGT pipeline has a limited commercial life, or that it faces significant commercial risk beyond the term of its current access contracts.

In summary, AlintaGas submits that by virtue of future revenue being largely underpinned by take-or-pay (firm capacity) reservations, and terms and conditions that favour GGT, the GGT pipeline is in fact a low risk pipeline.

4. Historical Tariffs for the GGT

GGT states:

“... the current tariff determination process should be viewed as a cross check on a tariff which is currently accepted as being appropriate.” (Section 3.4.6 Access Arrangement Information)

AlintaGas disagrees with this statement. AlintaGas does not agree that the existing tariffs are appropriate. AlintaGas is of the opinion, and has been for some time, that the existing tariffs are excessive. AlintaGas appreciates the opportunity that this Access Arrangement provides for the Regulator to review GGT's tariff structure and levels.

5. Use of the purchase price to determine DAC

AlintaGas does not agree with GGT's depreciated actual cost (“DAC”) valuation. GGT states:

“‘Actual capital cost’ faced by the owners of the Goldfields Gas Pipeline is the asset's 1999 purchase price.” (Section 4.1.2 of the Access Arrangement Information)

AlintaGas disagrees with this contention.

The price paid by various companies for the GGT in 1999 are subjective valuations made by each purchaser. The purchase price is likely to include factors that each purchaser considers will justify the payment of a price above the DAC valuation. Strategic benefits perceived by the purchasers and growth potential are two such factors. The purchase price should have no role in the determination of a DAC valuation. The DAC is determined from a knowledge of the actual construction cost of the GGT pipeline and the use of an appropriate depreciation schedule.

6. Weighted Average Cost of Capital

GGT proposes a pre-tax real weighted average cost of capital (“WACC”) of 12.2%. AlintaGas does not intend to discuss each parameter that is used to derive the WACC. However, AlintaGas submits that the WACC proposed by GGT is not justified and warrants careful scrutiny by the Regulator.

GGT states:

“On balance, the wider consequences of a low WACC are worse than the wider consequences of a high WACC. Therefore, if regulators are to err, it should be towards a decision which does not compromise the long term viability of the natural gas transport industry.” (Section 7.4.1.3 of the Access Arrangement Information)

AlintaGas considers that such a statement is irrelevant in this context. The optimum outcome is for the WACC to be set at a level that, in the Regulator’s opinion, is appropriate to the GGT pipeline.

7. Other Issues

- (a) GGT’s proposed terms and conditions requires the user to represent and warrant that the user’s gas consuming equipment supplied at the outlet facilities complies with all relevant laws. AlintaGas submits that this representation and warranty is inappropriate as it places GGT in the role of a regulatory safety-body.

The user is also required to represent and warrant that neither the user nor any of its related bodies corporate has impliedly or expressly represented to any person, including by silence or action, that a continuous supply of gas is guaranteed and can be relied upon. In AlintaGas’s case, this is unworkable, given AlintaGas’s obligations under the draft licences for the Kalgoorlie-Boulder supply area under the *Energy Coordination Act*. Furthermore, such a representation duplicates the operation of a proposed limitation of liability provision.

AlintaGas requests the Regulator to consider whether these proposed representations and warranties are acceptable under the National Access Code.

- (b) GGT proposes, as part of its “application for service” section, that it may require the prospective user to keep confidential any information GGT discloses to the prospective user throughout the course of the application for service, and may require that the obligation of confidentiality be a condition precedent to negotiations (section 6.12). This requirement is drafted very broadly. AlintaGas submits that it should not be used to stifle either negotiations or arbitrations between a prospective user and GGT. AlintaGas requests the Regulator to consider the practical implications of this clause.

- v
- (c) There is a requirement that a prospective user contribute to the costs of Developable Capacity, under the “application for service” section. AlintaGas queries the interaction of this requirement with sections 6.22, 6.23 and 8.23 – 8.26 of the National Access Code, which deal with the obligation to develop capacity. AlintaGas requests that the Regulator consider the practical implication of this requirement.
 - (d) The queuing policy in clause 7.1 of the proposed Access Arrangement allocates priority between prospective users seeking a reference service on a “first come first served” basis where a completed and executed order form is received by GGT. AlintaGas considers that a first come first served regime, although superficially attractive, is in fact too simplistic. Such a regime does not provide the flexibility to, for example:
 - (1) accept later in time prospective users seeking only the reference service whilst an earlier in time prospective user is “bogged down” in negotiation or arbitration with GGT; or
 - (2) accept a later in time prospective user who seeks the reference service for a greater amount of capacity and longer duration than the first in time prospective user.

AlintaGas submits that the “pure” first come first served regime proposed by GGT does not meet the requirements of section 3.13(b) and (c) of the National Access Code.

- (e) The proposed trading policy in clause 20.6 of the general terms and conditions states that the user must, prior to the use of the transferred capacity by the new user, advise GGT of, amongst others, the outlet points to be utilised by the new user, the respective MDQ for the inlet and outlet points, the term of the transfer and any rights reserved by the user in the transferred capacity regarding priority to capacity if there is an interruption or curtailment of supply.

AlintaGas submits that some, if not all, of these requirements go beyond that permitted by section 3.10 of the National Access Code. Section 3.10 states that the trading policy may require the transferee to notify the service provider that there has been a bare transfer and the nature of the contracted capacity subject to the bare transfer, but not any other details regarding the transfer.

Furthermore, GGT has included as clause 20.6(c) a provision stating that the terms of the service agreement are deemed to be altered by a transfer if, in the reasonable opinion of GGT, the transferred capacity and the rights retained by the user under the service agreement are in excess of the rights originally granted to the user under the service agreement. The clause operates to make such a transfer outside the definition of “bare transfer”.

GGT should not have this deeming right. AlintaGas submits that a transfer is either a bare transfer or it is not. Any attempts by GGT to deem a transfer as not a bare transfer should not affect the operations of section 8.10 of the National Access Code. AlintaGas requests the Regulator to consider whether the deeming provision in section 20.6(c) complies with section 8.10 of the National Access Code.

AlintaGas would welcome the opportunity to provide further input and comment on this Submission. As such, please feel free to contact either myself on 9486 3220 or David Randle on 9486 3240 if we can be of further assistance.

Yours sincerely

Jim Hennessy
Manager Gas Supply

../kal/offgar/l_submission_00301.doc