DAMPIER TO BUNBURY NATURAL GAS PIPELINE
PROPOSED REVISED ACCESS ARRANGEMENT

SUBMISSION #48

AN ALTERNATIVE PART HAUL AND BACK HAUL TARIFF METHODOLOGY

PUBLIC VERSION

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DBNGP (WA) Transmission Pty Limited
ABN 69 081 609 190
Level 7, 239 Adelaide Terrace
PERTH WA 6000
Contact: Anthony Cribb
Telephone: 08 9223 4304
Facsimile: 08 9223 4301

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1. INTRODUCTION

1.1. This is one of a series of submissions being made by Operator in response to the Draft Decision on Proposed Revisions to the Access Arrangement for the Dampier to Bunbury Natural Gas Pipeline ("Draft Decision") released by the Economic Regulation Authority ("Regulator") on 11 May 2005. The Draft Decision pertained to proposed revisions to the Access Arrangement ("Proposed Revised Access Arrangement") for the Dampier to Bunbury Natural Gas Pipeline ("DBNGP") submitted by Operator on 21 January 2005.

1.2. Amendment 9 of the Draft Decision requires that the proposed Revised Access Arrangement be amended to include a Reference Tariff for Part Haul and Back Haul Services. Furthermore, this tariff should be determined as a proportion of the Reference tariff for the full haul Reference Service as follows:

$$F \times \frac{D}{1{,}399}$$

where

F is a component of the tariff that would apply if the Service were the full haul reference Service; and

D is the distance, in kilometres along the pipeline, between the relevant Receipt Point and the relevant Delivery Point.

1.3. In its Submissions #27 & 36, Operator has advanced the case that Services other than full haul Service are unlikely to be sought by a significant part of the market. Accordingly, Operator has not included Part Haul and Back Haul Reference Services in its Proposed Revised Access Arrangement, and has not proposed Reference Tariffs for those Services. (Operator has, nevertheless, recognized that costs will be incurred in the provision of Part Haul and Back Haul Services as Non Reference Services, and has deducted the incremental costs of providing those services from the total cost of service provision in the determination of its proposed full haul Reference Tariff.)

1.4. Operator maintains that its case in respect of Part Haul and Back Haul Services is valid and, in these circumstances, the Regulator should not require Amendment 9. Nothing in this submission should therefore be construed to mean that Operator resiles from this position.

1.5. If, however, Amendment 9 is retained, the Regulator should not determine Part Haul and Back Haul Reference Tariffs as simple proportions of the Reference Tariff for the full haul Reference Service. The Regulator's method of determining these tariffs effectively allocates costs between full haul, Back Haul and Part Haul Services, and between shippers, on the basis of distance between receipt point and delivery point as a proportion of the notional full haul distance, the distance from Dampier to Kwinana Junction (1,399 km). All costs of providing service are, in effect, assumed to be proportional to the distance over which gas is transported in the DBNGP.

1.6. Not all costs of providing gas transportation service are proportional to the distance over which gas is transported.

1.7. Some costs can reasonably be argued as not being distance-related but, given the relatively uniform spread of facilities along the DBNGP, the apportionment of such costs on the basis of transportation distance is not an unreasonable approximation.

1.8. Other costs are not reasonably related to the distance over which gas is transported. To allocate these costs as if they were distance-related distorts access prices to the benefit of shippers transporting over shorter rather than longer distances. It precludes any approximation to efficiency in the level and structure of the Reference Tariffs, and has the potential to distort investment decisions in Pipeline transportation systems, and in upstream and downstream industries. That is, it precludes the possibility of achieving the objectives of sections 8.1(d) and 8.1(e) of the Code.

1.9. Operator is, therefore, strongly of the view that, if Amendment 9 is to be retained, a more careful allocation of costs must be made between full haul, Back Haul and Part Haul Services, and between shippers than was done in the Draft Decision.

1.10. In this submission, Operator sets out an alternative – and, in its view, more appropriate – basis for DBNGP cost allocation based on the current operation and utilisation of the pipeline.

2. ALLOCATION OF COSTS BETWEEN USERS

2.1. The Reference Tariff of the Draft Decision retains the approach to allocation of costs between shippers adopted by the Regulator for the Access Arrangement it drafted and approved for the DBNGP in December 2003.

2.2. In accordance with that allocation, for each of full haul, Part haul and Back Haul Service:

(a) a Capacity Reservation Tariff recovers from each shipper a proportion of return and depreciation, and a proportion of the non capital costs incurred in operating and maintaining the DBNGP (excluding the cost of fuel gas), on the basis of the shipper's contracted capacity as a proportion of the total contracted capacity; and

(b) a Commodity Tariff recovers from each shipper a proportion of the cost of fuel gas, on the basis of the shipper's throughput as a proportion of the total pipeline throughput.

2.3. In effect, the structure of the Capacity Reservation Tariff gives recognition to the fact that most of the costs incurred in providing, operating and maintaining the DBNGP are incurred for the purpose of providing contracted capacity, and will not vary as shippers' use of their contracted capacities varies. Through the Capacity Reservation Tariff, costs are allocated between shippers on the basis of contracted capacity.

2.4. The structure of the Commodity Tariff gives recognition to the fact that the cost of fuel gas is incurred for the purpose of transporting gas through the pipeline, and will vary as shippers vary their throughputs. Through the Commodity Tariff, costs are allocated between shippers on the basis of throughput.

2.5. In summary, in constructing the tariffs of the Draft Decision, costs have been allocated between shippers on the basis of contracted capacity or throughput.

2.6. The same allocation of costs between shippers has been retained by Operator for the Reference Tariff of the Proposed Revised Access Arrangement, and Operator proposes that it be continued if Amendment 9 is retained.

2.7. If, however, Amendment 9 is retained, an alternative and, in Operator's view, more appropriate, basis for the allocation of costs between services is required.

3. ALLOCATION OF COSTS BETWEEN SERVICES

3.1. As noted in section 1 of this submission, the Reference Tariff of the Draft Decision allocates costs between full haul, Part Haul and Back Haul Services provided using the DBNGP on the basis of distance over which gas is transported. For some costs, this basis of allocation is reasonable and, for others, it is a reasonable approximation.

3.2. There are, however, certain costs incurred in operating and maintaining the DBNGP which are not distance-related, and which are more appropriately pooled and allocated directly to shippers on the basis of contracted capacity.

3.3. Operator is of the view that capital costs – return and depreciation – are reasonably allocated between full haul, Part Haul and Back Haul Services on the basis of distance over which gas is transported. These costs are the costs of providing the physical infrastructure through which gas is transported and, at least to a reasonable approximation, the greater the distance over which each GJ of gas is transported, the greater the cost incurred in providing the transportation infrastructure (principally, pipeline and compressor stations).

3.4. Similarly, the cost of fuel gas is reasonably allocated between full haul and Part Haul Service provision on the basis of the distance over which each GJ of gas is transported. At least to a reasonable approximation, the greater the distance over which gas is transported, the greater the quantity and, hence, the greater the cost of fuel used in transporting the gas.

3.5. The allocation of the cost of fuel gas to the provision of Back Haul Service is more problematic. An argument can be made that no fuel is required for the provision of Back Haul and hence no cost should be allocated to it. Indeed, a benefit might be attributed to the provision of Back Haul Service because it may reduce forward haul volumes and the fuel cost incurred in delivering those forward haul volumes. On this argument, the maximum cost of fuel gas which might be allocated to Back Haul Service is zero.

3.6. While such a strictly incremental approach can be applied in the allocation of fuel gas costs, Operator doubts that the same approach can be applied consistently to the allocation of other non capital costs between full haul, Part haul and Back Haul Services.

3.7. Operator has, therefore, formed the view that the operating pipeline is a single common facility which is used to provide full haul, Part Haul and Back Haul Services. The costs of this common facility are then to be allocated between Services and, in the case of fuel gas costs, distance-related cost allocation ensures a reasonable attribution of cost to Service provision. In addition to an efficiency aspect – shippers paying only for the facilities used to provide them with service – the resulting tariffs also have an equity aspect. Each unit of service, irrespective of whether it is full haul, Part Haul or Back Haul, is treated as incurring a proportion of the total cost of the common facility.

3.8. As noted above, not all of the non capital costs incurred by Operator are related to the distance over which gas is transported. Table 1 (below) reproduces the categorization of non capital costs Operator has used in **[deleted – confidential & commercial in confidence]**. In Table 1, Operator identifies each component of its total non capital costs (including the cost of fuel gas), and indicates whether it is distance related.

3.9. If the cost is distance-related, Operator is of the view that it should be allocated between Services on the basis of distance and, for this purpose, the appropriate allocation factor is

GJ kilometers (where the volume weighting may be either contracted capacity – MDQ – or throughput, depending on the type of cost being allocated).

3.10. If a component of non capital cost is not distance-related, Operator is of the view that it should be allocated directly between shippers on the basis of contracted capacity (GJ MDQ).

3.11. Accordingly, Table 1 also shows what are, in Operator's view, the appropriate allocation factors for the each of the components of total non capital costs.

Table 1: Non capital cost allocation

Cost	Description	Allocation factor
Salaries and wages	Salaries and wages of Operator's (corporate) staff	GJ MDQ km
Asset services	Technical compliance services (for example, safety case preparation) provided by ANS	GJ MDQ
Administration	Project management and support services provided by ANS	GJ MDQ km
Transportation services	Gas control, SCADA and data management services provided by ANS	GJ MDQ
Land management	Land management, heritage protection and environmental support services provided by ANS	GJ MDQ km
Engineering services	ANS engineering and technical expertise for total system issues including gas measurement, corrosion protection and operating performance improvement	GJ MDQ
Field services (recurrent)	Programmed maintenance of the pipeline itself, compressor stations, and metering facilities, and other maintenance-related activities including logistics, maintenance planning, and maintenance of communications systems and buildings	GJ MDQ km
ANS corporate	Human resource management, legal, finance and accounting, information systems and other commercial services support provided by ANS	GJ MDQ km
OSA fee	Operating Services Agreement management fee payable to ANS	GJ MDQ km
Insurance	All classes of insurance maintained by Operator (other than liquidated damages insurance required under certain transportation contracts, and any construction or expansion works related insurance)	GJ MDQ km
Equity raising costs	Amortised cost of raising the initial equity for the gas transportation business based on the DBNGP	GJ MDQ km
Asymmetric risk	Allowance for certain risks for which insurance cover cannot or has not been obtained (see Submission #33)	GJ MDQ km
Liquidated damages insurance	Liquidated damages insurance required by certain existing gas transportation contracts (see Submission #33)	GJ MDQ km

Table 1: Non capital cost allocation (continued)

Cost	Description	Allocation factor
Regulatory	Operator's costs of complying with regulation of the DBNGP	GJ MDQ
Regulatory review	Operator's estimates of the costs incurred by the Regulator in its conducting approvals processes such as the access arrangement approval process. The estimates are based on the more recent service and standing charges invoiced by the Regulator, and charges levied to cover the costs of the gas access arbitrator	GJ MDQ
Field services (non recurrent)	Major overhauls of items of plant other than compressor units, and other major maintenance activities, which vary from year to year in accordance with manufacturers' specifications and utilization (see Submission #33)	GJ MDQ km
Fuel gas	Cost of all gas used by Operator in providing a transportation service using the DBNGP, including gas used as compressor fuel, gas used as fuel in gas engine alternators and heaters, gas vented during maintenance activities, and gas lost from the pipeline	GJ (throughput) km

3.12. **[deleted – confidential & commercial in confidence]**

3.13. If Amendment 9 were to be retained in the Regulator's Final Decision, Operator would expect that the Regulator change the basis of cost allocation for Reference Tariff determination and adopt the allocation factors set out in Table 1.