



14th March 2005

Ms Annette Watkins
Manager Projects
Economic Regulation Authority
Level 6
Governor Stirling Tower
197 St George's Terrace
Perth WA 6000

email: annette.watkins@era.wa.gov.au

Dear Ms Watkins

Proposed Revised Access Arrangement

We refer to the Economic Regulation Authority's notices of 25 January 2005 and 11 February 2005 inviting submissions on DBNGP (WA) Transmission Pty Ltd's ("**Transmission**") proposed revisions to the Access Arrangement and Access Arrangement Information for the DBNGP ("**Proposed Revisions**") in relation to the period 1 July 2005 to 30 December 2010 ("**2005 -2010 Period**").

CSBP Limited's ("**CSBP**") interest in the Proposed Revisions are fivefold:

- CSBP has existing gas transport contracts with Transmission for in excess of 20TJ/d ("**Existing Contracts**");
- Several of CSBP's industrial operations purchase significant quantities of gas (in excess of 30 TJ/d) delivered via the DBNGP, for use as chemical feedstock and energy (the most significant being the CSBP ammonia plant at Kwinana);
- CSBP is a substantial consumer of electricity from the South West Interconnected System in its fertiliser and chemical manufacture and distribution operations at Kwinana, Geraldton, Bunbury and Albany;
- CSBP is constantly investigating opportunities to expand its existing operations, including installation of new chemical or fertiliser production facilities requiring natural gas as feedstock or fuel and supply of electricity; and



CSBP Limited

ABN 81 008 668 371

PO Box 345, Kwinana
Western Australia 6966
Telephone: +61 8 9411 8777
Facsimile: +61 8 9411 8282

www.csbp.com.au



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Managing Director
Quality Systems
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Standards Australia

- As a locally based industrial company competing in highly competitive domestic and export markets, CSBP is concerned to promote the sustainable growth and international competitiveness of the Western Australian economy.

With these factors in mind, and taking into account the factors that the ERA must take into account under, inter alia, section 2.24 of the National Third Party Access Code for Natural Gas Pipeline Systems (“**Code**”), we make the following submissions on the Proposed Revisions.

1 The Proposed Reference Service: Tf Service

- 1.1 Tf Service is the only type of Reference Service offered under the Proposed Revisions.
- 1.2 CSBP understands that the Tf Service is materially different to, and less certain and more restrictive than, the ‘T1 type service’ to which CSBP understands the majority of the DBNGP has been contracted.
- 1.3 CSBP has concerns as to whether the Tf Service is a type of service which is likely to be sought by “*a significant part of the market*”¹ and further whether, in any case, a ‘T1 type Service’ should be offered as a Reference Service (either in addition, or as an alternative to, the Tf Service).
- 1.4 However, without prejudice to CSBP’s rights to make submissions in the future in relation to any revisions or access arrangements proposed from time to time, at this stage, CSBP does not propose to press these concerns. Further please note that by not making a submission on this issue in relation to the 2005-2010 Period, CSBP does not wish to be seen as supporting this part of the Proposed Revisions. At this stage CSBP would expect Transmission to offer a T1 Reference Service (as this is a service sought by a large part of the market) by no later than 1 January 2016, but it may be appropriate for this service to be available as a Reference Service prior to this date.

2 Priority order of Proposed Tf Service

- 2.1 The order of priority of the Tf Service upon curtailment (vis-à-vis other types of capacity services) should be made clearer to give certainty to all shippers of priority of service among different services, particularly as the proposed new Reference Service is a service which has not previously been available on the DBNGP. CSBP suggests a new clause 14.3 be inserted into the proposed Annexure A: Access Contract Terms and Conditions as follows:

“For the avoidance of doubt, for the purposes of existing capacity contracts the Tf Service is an ‘Other Reserved Service’ and shall be curtailed accordingly.”

3 The proposed ‘Incentive Mechanism’

- 3.1 Essentially, under the proposed ‘Incentive Mechanism’ (set out in section 7.12 of the Proposed Revised Access Arrangement), the Total Revenue from which the Reference Tariff is to be calculated during the period from 1 January 2011 to 31 December 2015 (the “**2011-2015 Period**”) includes the unexpected non-capital cost savings arising during the 2005-2010 Period (“**Relevant Cost Savings**”).

- 3 issues

¹ As referred to in paragraph 3.2 of the Code.

- 3.2 CSBP submits that the proposed ‘Incentive Mechanism’ is too heavily weighted in favour of Transmission in three key areas.
- 3.3 Firstly, the Proposed Revisions should make it clear that Transmission may only include a share of Relevant Cost Savings in the forecast Total Revenue for the 2011-2015 Period to the extent that those cost savings continue to be realised in the 2011-2015 Period (“**Ongoing Savings**”). In other words, the Total Revenue recoverable in the 2011-2015 Period through the Reference Tariff should not be artificially inflated by a cost saving incentive when the cost saving is not available in the 2011-2015 Period.
- 3.4 Secondly, Transmission should only be entitled to continue to reap the Ongoing Savings in the 2011-2015 Period for a maximum of 5 years from the year that such savings were first realised. Therefore, the table on page 16 of the Proposed Revised Access Arrangement should be replaced with the following:

Year	Share of returns
2011	$S_{2011} = E_{2006} + E_{2007} + E_{2008} + E_{2009}$
2012	$S_{2012} = E_{2007} + E_{2008} + E_{2009}$
2013	$S_{2013} = E_{2008} + E_{2009}$
2014	$S_{2014} = E_{2009}$
2015	

- 3.5 Thirdly, Transmission should share the Relevant Cost Savings with the users of the Reference Services. CSBP suggests that Transmission should receive only 50% of the relevant Relevant Cost Savings in the 2011-2015 Period.

- an apportionment of the Relevant Cost Savings will also be required

- 3.6 CSBP notes that the proposed ‘Incentive Mechanism’ assumes that the Total Revenue which is used for the purposes of calculation of the Tf Service Reference Tariff will be calculated as if “*all Shippers using Full Haul Services are users of the Tf Service*”. Largely consistent with this assumption, Transmission proposes that 100% of the Relevant Cost Savings are added to the Total Revenue figure used to calculate the Tf Service Reference Tariff. However, CSBP notes that not all costs are properly attributable to the provision of the Tf Service.
- 3.7 As noted in section 4 below, CSBP reserves its rights to make submissions as to whether the Total Revenue figure (from which the Reference Tariff is derived) has been correctly calculated in accordance with section 8.38 of the Code. Further, as noted in section 1 above, CSBP reserves its rights to make submissions that alternative or additional Reference Services should be offered in the future.
- 3.8 As the allocation of costs between services may be determined on a different basis in future Access Arrangement Periods, CSBP submits that the proposed Incentive Mechanism (which has an impact in a future Access Arrangement Period) should be amended so as to make clear that only that portion of the Relevant Cost Savings that relate to that portion of the Total Revenue used to derive the relevant Reference Tariff for a particular Reference Service may be added to the relevant Total Revenue figure when deriving such Reference Tariff.

4 Section 8.38 of the Code: apportionment of Total Revenue

- 4.1 As stated in the Proposed Revised Access Arrangement Information, “[t]he Reference Tariff has been determined under an assumption that all Shippers using Full Haul Services are users of the Tf Service” (“**Total Revenue Assumption**”).
- 4.2 CSBP believes that it is strongly arguable that this approach is inconsistent with section 8.38 of the Code.
- 4.3 CSBP has decided to not object to the Total Revenue Assumption during the 2005-2010 Period. However, CSBP reserves the right to make submissions in relation to the appropriate basis for apportioning costs pursuant to the Code in any future Access Arrangement period. Further, CSBP does not intend, by not making a submission on this issue in relation to the 2005-2010 Period, to be seen as supporting the Total Revenue Assumption as a proper basis for apportioning Total Revenue recoverable under any particular Reference Tariff.

5 Rebatable Revenue

- 5.1 The current access arrangement provides for rebate of certain revenues derived from certain Rebatable Service to shippers. These provisions have been removed from the proposed access arrangement.
- 5.2 Consistent with section 8.40 of the Code, CSBP submits that:
- (a) Rebatable Revenue be rebated to the users of the Reference Service via a reduction in the Reference Tariff;
 - (b) Rebatable Revenue should include:
 - (i) at least 50% of revenue derived from Spot Capacity Service, Park and Loan Service and Seasonal Service Peaking Service; and
 - (ii) all “penalty revenue” (being overrun charges, imbalance charges, peaking charges and nomination surcharges) derived under all contracts for capacity on the DBNGP insofar as those charges are in excess of the costs incurred as a result of the matters giving rise to those charges.

6 Fixed Principles

- 6.1 Transmission is seeking to fix, until 2031:
- (a) the method of determination of the Capital Base at the commencement of each year of the Access Arrangement Period (the “**First Fixed Principle**”);
 - (b) the method of determination of the Rate of Return and the elements used in that determination (the “**Second Fixed Principle**”); and
 - (c) the principle that the revenue earned by Transmission during the period commencing on 1 July 2005 and ending on 31 December 2015 from the sale of any Services which revenue is in excess of the amount equal to the sum of:
 - 1. the revenue received from the sale of Full Haul Services had those Services been sold at the Reference Tariff; and

2. the revenue actually earned from the sales of non-Full Haul Services,

must not be taken into account by the Regulator directly or indirectly for the purposes of setting a Reference Tariff (etc.) which applies after 1 January 2011 (the “**Third Fixed Principle**”).

- first fixed principle

6.2 CSBP is concerned to ensure that the manner in which Transmission proposes to inflate the Capital Base of the DBNGP is fair and reasonable and does not prejudice users of the DBNGP. CSBP would welcome the opportunity to discuss with the Regulator whether the basis of expressing the Capital Base and Depreciation and the manner in which the effects of inflation are dealt with under the Proposed Revised Access Arrangement are fair, reasonable and appropriate.

6.3 CSBP submits that there is a lack of certainty as to the relationship between, and operation of, sections 7.3(c) and 7.4(b) of the Proposed Revised Access Arrangement. CSBP submits that section 7.3(c) of the Proposed Revised Access Arrangement should be subject to section 7.4(b) of the Proposed Revised Access Arrangement, and that if sections 7.3(b)(iii) and 7.3(c) are “Fixed Principles”, then section 7.4(b) of the Proposed Revised Access Arrangement should also be a “Fixed Principle”. CSBP also submits that section 7.3(c) should be amended by replacing the words “during the Access Arrangement Period” with the words “during the relevant year”.

- second fixed principle

6.4 CSBP does not agree that the elements listed in section 7.6(d) of the Proposed Revised Access Arrangement should be Fixed Principles and submits that:

- (a) it is not appropriate to fix any of the elements listed in section 7.6(d) of the Proposed Revised Access Arrangement as these elements are, in CSBP’s view, “Market Variable Elements” (as defined in the Code). A Market Variable Element is defined in section 10.8 of the code as “...a factor that has a value assumed in the calculation of a Reference Tariff, where the value of that factor will vary with changing market conditions during the Access Arrangement Period or in future Access Arrangement Periods, and includes the sales or forecast sales of Services, any index used to estimate the general price level, real interest rates, Non Capital Cost and any costs in the nature of capital costs”. Section 8.48 of the Code provides that “[a] Market Variable Element can not be a Fixed Principle.” In CSBP’s view, the elements listed in section 7.6(d) of the Proposed Revised Access Arrangement are Market Variable Elements on the basis that the value of these elements will vary with changing market conditions and therefore cannot be Fixed Principles; and
- (b) flexibility should be retained to adjust any estimate of the Rate of Return to reflect economic and market conditions at the time future access arrangements are entered into.

The Institute for Research into International Competitiveness in its report “Review of Rate of Return Methodologies and Practice” dated September 2003, and submitted to The Office of Gas Access Regulation, makes the following statements in sections 2.3 and 2.4 of the report which support CSBP’s submission:

- (i) “QCA (2001 p234) shows 12 recent decisions with a choice of 0.5, and the remaining 6 choosing a range between 0.3 and 0.5” – the Regulator may determine that gamma should change from its current value of 0.5 based on decisions made by other regulators in response to changes in market conditions;
- (ii) “The market risk premium used by the Western Australian Regulator has been six

- (iii) percent, in line with research suggesting that this has represented a reasonable proxy of the market risk premium. However, the (sic) maintains a watching brief to ascertain whether this figure should change”;
- (iv) “Beta is calculated on a case-by-case basis based on current market information”; and
- (v) “Capital structure is calculated in accordance with the requirements of the Code having regard to the gearing level of an efficient firm for the industry” – gearing levels for an efficient firm in the industry would change in response to improving or deteriorating market conditions.

On this basis, it is clear that the elements listed in section 7.6(d) of the Proposed Revised Access Arrangement are Market Variable Elements which may change with changing market conditions, and accordingly, CSBP submits that it is inappropriate for these to be Fixed Principles.

- third fixed principle

6.5 CSBP does not agree with the Third Fixed Principle as drafted and submits as follows.

- (a) The Third Fixed Principle should not apply on and from the date on which any access arrangement applying on or after 1 January 2016 comes into effect (in other words, the Third Fixed Principle should not continue to apply up until 2031).
- (b) In any event, the only additional revenue which should not be taken into account under the Third Fixed Principle is additional revenue received as a result of the tariffs under contracts which are in force as at 28 October 2004 being higher than the Reference Tariff. This allows Transmission to keep the benefit of any higher tariffs under 28 October 2004 contracts, but does not, for example, preclude the Regulator from taking into account additional revenue earned due to actual sales volumes being higher than forecast sales volumes.
- (c) The second limb of the Third Fixed Principle must be subject to any obligation to rebate Rebatable Services (either by an actual rebate or tariff adjustment) as referred to in section 5 above.
- (d) Further, to reflect the ‘flip side’ of the Third Fixed Principle proposed by Transmission, CSBP submits that the Third Fixed Principle, must also preclude the regulator from taking into account the fact that Transmission may receive lower revenues under one or more of its contracts for full haul services which are in force as at 28 October 2004 than the revenues it would have received had those services been sold at the Reference Tariff for the purpose of setting a Reference Tariff or applying the Reference Tariff Policy which applies on or after 1 January 2011 or otherwise take this into account (directly or indirectly) in performing any of the Regulator’s functions under the Code.

7 Out of specification gas

7.1 Any change to broaden the gas specifications as set out in Schedule 2 to Annexure A: Access Contract Terms and Conditions (“**Access Contract Terms and Conditions**”) (“**Current Gas Specification**”) or otherwise may have significant detrimental effects on CSBP for the following reasons:

- (a) CSBP uses natural gas as the major process feedstock in the production of ammonia, an important input to downstream fertiliser and chemical processing in Western Australia. The introduction of lower quality gas into the DBNGP would have the potential to adversely impact the quality of gas delivered to CSBP at its DBNGP Delivery Point (outlet point)

which would have a negative impact on the production capacity and energy efficiency of CSBP's ammonia plant, and which in turn would increase CSBP's ammonia production cost. This would have the potential to cause consequent cost increases to downstream users, most of which compete in export markets.

- (b) CSBP, appointed by Australian Gold Reagents ("AGR")² as the operator of AGR's sodium cyanide production facilities, uses natural gas as a critical process feedstock in the production of sodium cyanide, an important reagent used by the gold industry. The introduction of lower quality gas into the DBNGP would have the potential to adversely impact the quality of gas delivered to AGR at its DBNGP Delivery Point (outlet point) which would add significant costs to the manufacture of sodium cyanide which could in turn have negative impacts on the costs of the domestic gold industry. AGR is also a significant exporter of sodium cyanide and any such increased costs could have a major negative impact on AGR's ability to compete in a highly competitive international market.
- (c) CSBP has significant capital invested (over \$200 million) in both the ammonia plant and sodium cyanide plants. These plants have been recently expanded to support growth in the domestic market, and any future returns on this capital would be seriously damaged by any widening of gas specifications.

7.2 In the wider context, if Western Australia is to grow its chemical industry, based on natural gas as a feedstock not just as an energy source, the quality of gas needs to be maintained or improved in the longer term in order to attract capital investment in major new chemical processing facilities and associated infrastructure.

- clause 2.8

7.3 Clause 2.8 of the Access Contract Terms and Conditions permits the Operator to change the Current Gas Specifications if certain conditions are met. One of those conditions is that there is no shipper with an Inconsistent Existing Contractual Specification.

7.4 CSBP submits that the definition of 'Inconsistent Existing Contractual Specification' does not adequately address the issues faced by a shipper who, like CSBP, uses gas as feedstock. Accordingly, CSBP suggests that the definition of 'Inconsistent Existing Contractual Specification' be amended to include, in relation to a Delivery Point:

- (a) the circumstance where a change in gas specification would require modifications to plant, owned by a User, that uses gas delivered via the DBNGP as feedstock; and
- (b) the circumstance where a change in gas specification will have a materially adverse affect on the operation of or costs of running plant, owned by a User, that uses gas delivered via the DBNGP as feedstock.

This amendment would prevent the Operator from changing the Current Gas Specification when either the circumstances described in either of (a) or (b) above is likely to arise.

- clause 2.10

7.5 Further, CSBP submits that clause 2.10 of the Access Contract Terms and Conditions be deleted. This is because, on any of at least 2 possible interpretations of clause 2.10, this clause will potentially have detrimental effects on the quality of gas delivered on the DBNGP and, as a result, upon the CSBP operations that use such gas as feedstock.

² AGR is a joint venture between CSBP and Coogee Chemicals Pty Ltd.

- 7.6 Clause 2.10 provides that a Shipper may from time to time request that the Operator vary the gas specification for a Receipt Point. Subject to certain conditions, the Operator must make this change and a “corresponding change” to the Delivery Points specification. It is not clear whether the “corresponding change” in the Delivery Points specification means a change in the Delivery Points specification to make it the same as the Receipt Point specification, or a change to the Delivery Points specification of the same margin as the change to the Receipt Point specification.
- 7.7 If it is the former, a change to Receipt Point specification and a corresponding change to the Delivery Points specification would limit the control Transmission can exercise over the composition of gas delivered via the DBNGP. Accordingly, it would be more likely that Transmission would be unable to provide the gas within the specification CSBP has contracted for.
- 7.8 On the latter interpretation, clause 2.10 is likely to result in a general broadening of the gas specifications on the DBNGP. If this occurred, it would be extremely likely that CSBP would receive gas of a lower quality than it has contracted for.
- 7.9 As set out in paragraph 7.1, both of these outcomes will be materially detrimental to CSBP.
- 7.10 As an aside, in any case, CSBP does not believe that clause 2.10 protects the interests of Transmission or third parties in the manner ostensibly intended by the clause. The effect of clause 2.10 is unclear in many respects. For example:
- (a) The receipt of gas will never render the Operator incapable of complying with the Delivery Point specification as the gas can always be blended or processed at the Operator’s expense. Therefore, on its face, the test set out in 2.10(a) does not make sense.
 - (b) On its face, clause 2.10(c) gives no practical protection to the Operator. To say, as provided in clause 2.10(c), that nothing in clause 2.10 requires the processing of gas misses the point. This is because gas processing (or blending) may become necessary as a result of the shipper obtaining a change to the Existing Gas Specification pursuant to clause 2.10(a) (ie. this may be the only way in which the Operator can comply with its obligations to take gas of a broader specification while still meeting its obligations relating to the specification of gas delivered at Delivery Points (outlet points) on the DBNGP).
 - (c) Clause 2.10(d) provides that, once the Existing Gas Specification has changed, Operator may refuse to take receipt of gas if certain circumstances arise. However, as a practical matter, it seems unlikely that the Operator would be willing to enforce this remedy because of the detrimental financial effect of such enforcement on the Operator.
 - (d) In any case, even if it was financially practicable for the Operator to refuse receipt of gas, it will be likely to be difficult for the Operator to prove, as is required by clause 2.10(d), that the receipt of the out of specification gas:
 - (i) *“materially increased the Operator’s costs”* - as the receipt of out of specification gas is likely to reduce the revenues the Operator receives, possibly without materially increasing the Operator’s costs; and
 - (ii) *“adversely affected the rights of any shipper”* - as any change to the gas specifications for one shipper will not affect the “rights” of other shippers (in contrast to the quality of the gas those other shippers receive - which will be adversely affected).

8 Miscellaneous

- 8.1 CSBP submits that section 5.3(a) of the Proposed Revised Access Arrangement be amended to require the Operator to assess and respond to an Access Request as a reasonable and prudent pipeline operator (as per section 5.2 of the existing Access Arrangement).
- 8.2 Section 5.3(c) requires the Shipper, but not the Operator, to negotiate terms and conditions of access in good faith. Under the existing queuing policy, there is no express ability to remove Access Requests from the queue if negotiations on the terms and conditions of access are not progressing. Under the Proposed Revised Access Arrangement, the Operator may remove the Access Request from the queue if the parties have not reached agreement as to the terms and conditions within 40/60 Business Days (for Spare Capacity and other capacity, respectively). CSBP submits that section 5.3(c) of the Proposed Revised Access Arrangement be amended to require the Operator to negotiate terms and conditions of access in good faith, and also that the time periods referred to in sections 5.4(f)(i) and (ii) of the Proposed Revised Access Arrangement be changed from 40 Business Days and 60 Business Days to 60 Business Days and 80 Business Days respectively.
- 8.3 CSBP submits that section 5 of the Proposed Revised Access Arrangement be amended so that the Operator is required to notify a Prospective Shipper of its position in the queue (in addition to the Operator's obligations already set out in section 5.4(o) of the Proposed Revised Access Arrangement).
- 8.4 CSBP makes the following submissions:
- (a) The word "*adjusted*" in section 5.2(d) of the Proposed Revised Access Arrangement should be amended to read "*reduced*".
 - (b) The words "*without interruption or curtailment except as permitted by the Access Contract*" at the end of section 6.2(a)(ii) of the Proposed Revised Access Arrangement should be moved down a line and taken to the margin so that they apply to both paragraphs (i) and (ii) of section 6.2(a).
 - (c) In section 3.1(b) of the Proposed Revised Access Arrangement Information delete the words "*down stream of Compressor Station 9*" because the Commodity Tariff is payable regardless of where the gas is delivered.
 - (d) "*Shippers MDQ*" (as used in section 6.2(a) of the Proposed Revised Access Arrangement) should be defined.

Yours sincerely
CSBP Limited



Ian Hansen
General Manager – Chemicals