# DBNGP Draft Decision

## Submission to the Gas Access Regulator

**AlintaGas Sales Pty Ltd**

**21 September 2001**

**ALINTAGAS SALES'S SUBMISSION**

**ON THE**

**DBNGP ACCESS ARRANGEMENT DRAFT DECISION**

## 1. INTRODUCTION

This Submission has been prepared by AlintaGas Sales Pty Ltd ("**AlintaGas**") in response to a request from the Western Australian Independent Gas Pipelines Access Regulator ("**Regulator**") for submissions from interested parties concerning the Regulator's Draft Decision ("**Draft Decision**") on Epic Energy's proposed Access Arrangement ("**Access Arrangement**") for the Dampier to Bunbury Natural Gas Pipeline ("**DBNGP**").

AlintaGas is also a party to two joint Submissions, one addressing the need for a T1-Equivalent Reference Service, and the other addressing Epic Energy's contention that the Draft Decision, if approved, will create a group of shippers that are "second class citizens".

Whilst AlintaGas has concerns with some aspects of the Draft Decision, it generally believes that the Regulator's final decision ("Final Decision") will, if it is consistent with the Draft Decision and amended to incorporate the further submissions made by AlintaGas in this Submission and in the two joint Submissions to which AlintaGas was a party, provide an appropriate outcome for the Western Australian gas industry.

In that light, AlintaGas generally supports many of the Regulator's proposed amendments, including those relating to the Initial Capital Base, the rate of return, depreciation and the reference tariff, and the overall position reached by the Regulator in the Draft Decision. As an example, AlintaGas believes that the value of the Initial Capital Base proposed by the Regulator is at the upper limit of the range of acceptable values. However, while AlintaGas acknowledges that the Initial Capital Base as determined by the Regulator may be appropriate when considered in the context of the Draft Decision as a whole, AlintaGas submits that there is no justification for a higher value in the Final Decision.

AlintaGas submits that, to achieve an appropriate and reasonable outcome, the Final Decision must appropriately address the matters set out in the following Sections 2-5 :

## 2. THE INITIAL CAPITAL BASE AND THE ALLEGED "REGULATORY COMPACT"

As discussed in Section 1, AlintaGas generally acknowledges the Regulator's conclusion in relation to the value of the Initial Capital Base. However, it has concerns about some of the statements made by the Regulator in relation to the alleged existence and relevance of a "regulatory compact".

## 2.1 Epic Energy's alleged "regulatory compact"

Epic Energy's proposed Initial Capital Base value and reference tariff relied heavily upon the alleged existence of a "regulatory compact".

The nature of the alleged "regulatory compact" was outlined by the Regulator in the Draft Decision at B:97. Put at its strongest, the alleged "regulatory compact" is a so called "set of common understandings and expectations between Epic Energy and the Government of Western Australia that developed during the pipeline sale process"[1] in relation to the transmission tariffs that would apply to the transportation of gas in the DBNGP.

## 2.2 AlintaGas's position on the alleged "regulatory compact"

AlintaGas made extensive submissions to the Regulator on Epic Energy's assertion that a "regulatory compact" was established during the sale process for the DBNGP. The content of those submissions is generally summarised in the Draft Decision at Part B:103.

The central elements of AlintaGas's position on the alleged "regulatory compact" are that:

(a) there has never been any "regulatory compact" between the State and Epic Energy; and

(b) it is irrelevant to the Regulator whether there is a "regulatory compact" (which is denied) or not, in carrying out the function of determining an appropriate value for the Initial Capital Base for the DBNGP and reference tariff under the relevant provisions of the *National Third Party Access Code for Natural Gas Pipeline Systems* ("**Code**").

## 2.3 The Regulator's position in relation to the alleged "regulatory compact"

In the Draft Decision, the Regulator went to some lengths to outline how Epic Energy seeks to value the Initial Capital Base (effectively by reference to the purchase price that it paid for the DBNGP) and reference tariff by relying on the alleged "regulatory compact": Part B:97 to B:99. The Regulator also went to some lengths to summarise AlintaGas's submissions on the point, as well as Epic Energy's submissions in response: Part B:103 to B:106.

However, the Draft Decision does not express any firm conclusion as regards Epic Energy's alleged "regulatory compact". It could be inferred that the Regulator rejected the "regulatory compact" argument by stating in the Draft Decision that:

> "regardless of the purchase price paid by the successful bidder for the DBNGP assets, the circumstances of the DBNGP sale do not provide a basis for a prospective purchaser to reasonably expect a regulatory asset value under the Code in excess of a DORC value": Draft Decision, Part B:154.

However, it is not clear from that conclusion that the Regulator actually rejects Epic Energy's submissions concerning the relevance of its alleged "regulatory compact".

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[1] These are Epic Energy's words as quoted by the Regulator at B:97.

The issue is clouded further by the Notice of the Draft Decision issued by the Regulator on 21 June 2001, in which the following statement appears:

> "Epic Energy submitted that the manner in which the sale was conducted gave rise to the understanding of a regulatory compact between it and the Government on the price that may be charged for transmission of gas on the pipeline. While a number of references to transmission tariffs for the DBNGP were made at the time of the sale of the pipeline and subsequently, the Regulator has not been able to verify a regulatory compact."

One possible interpretation of that statement is that the Regulator is yet to draw any final conclusion and remains open to further submissions by Epic Energy that may persuade the Regulator that he is able to "verify a regulatory compact". The implication of this interpretation must be that if the Regulator were able to verify the existence of a "regulatory compact", this would be of some relevance to him. AlintaGas rejects any suggestion that a "regulatory compact" could be of relevance to the Regulator.

### 2.4 Further submission on the alleged "regulatory compact"

AlintaGas submits that Epic Energy's argument as to an alleged "regulatory compact" should be unambiguously dismissed.

AlintaGas reiterates that there is no, and never has been any, regulatory compact and considers that Epic Energy's arguments fail to justify an Initial Capital Base value that is $1.3 billion (or 108%) above what the Regulator has concluded is a fair and reasonable value.

In relation to the statement in the Regulator's Notice of the Draft Decision, AlintaGas submits that Epic Energy cannot "verify the regulatory compact" because there is no "regulatory compact". However, even if Epic Energy sought to persuade the Regulator to "verify" the existence and terms of the alleged "regulatory compact", the Final Decision should not change from the Draft Decision in relation to the Initial Capital Base and reference tariff. AlintaGas submits that the Regulator should clearly and expressly confirm that position.

AlintaGas makes this submission on the grounds that:

(a) in this jurisdiction, the term "regulatory compact" has no meaning and is not recognised; and

(b) the issue of whether or not there is, or ever has been, any "regulatory compact" is irrelevant to the Regulator's task of determining an appropriate Initial Capital Base for the DBNGP and reference tariff under the Code.

As the proponent of this novel concept, Epic Energy has the burden of establishing that a "regulatory compact" has meaning and relevance in Australian law, and specifically under the Code. Furthermore, if Epic Energy satisfies that burden (which it cannot), it also bears the burden of establishing:

1. the existence of the alleged "regulatory compact" in this case;

2. the relevance of the alleged "regulatory compact" to the determination of the Initial Capital Base value for the DBNGP and the reference tariff; and

3. that any weight should be attached to the existence of the alleged "regulatory capital base".

Epic Energy has failed to establish any of those things.

Further, AlintaGas submits that it would be of serious concern if the independence of the Regulator, in satisfying the requirements of the Code in relation to the DBNGP in the interests of all relevant interested parties, were to be adversely affected by the continuing uncertainty surrounding this issue.

Finally, AlintaGas reiterates its earlier submissions in relation to the alleged "regulatory compact".

## 3. PROPOSED GAS QUALITY SPECIFICATION

AlintaGas submits that the Regulator's proposed Amendment 9, which requires, from 1 July 2005, the gas quality specifications to be similar to the broadest specifications contained in the *Dampier to Bunbury Pipeline Regulations 1998* ("**DBPRs**"), is inappropriate.

AlintaGas also submits that it is beyond the Regulator's power to approve the Access Arrangement if it requires gas to be of a quality that is similar to the broadest specifications in the DBPRs. This is because, in doing so, the Regulator would deprive AlintaGas of a contractual right in existence prior to the date on which the proposed Access Arrangement was submitted to the Regulator.

The Draft Decision states:

> "The Regulator considers that after June 2005, there is no reason for Epic Energy to not accept into the pipeline gas that meets the broadest specifications currently set out in Schedule 1 of the *Dampier to Bunbury Pipeline Regulations 1998*": Draft Decision, Part B:48

AlintaGas disputes this, since it understands that some shippers (including AlintaGas) continue to have contracted gas quality specifications beyond 30 June 2005 that are more stringent than the broadest specifications. This being the case, the adoption from 1 July 2005 of the broadest specifications will compromise Epic Energy's contractual obligations to deliver gas to those shippers with the more stringent gas quality specifications. The shippers (including AlintaGas) would be deprived of a contractual right in existence prior to the date on which the proposed Access Arrangement was submitted to the Regulator, contrary to section 2.25 of the Code.

AlintaGas submits that the Regulator would be acting beyond the power conferred by the Code if the Regulator were to approve Amendment 9 for inclusion in the Final Decision.

AlintaGas notes that the comments received by the Regulator to Epic Energy's proposed DBNGP Access Arrangement did not propose that the broadest specifications actually be adopted. Rather, both the Treasury / Office of Energy and CMS Gas Transmission

submissions merely proposed that the *concept* of the broadest specifications be explicitly incorporated within the Access Arrangement.

AlintaGas is not convinced that industry or consumers in Western Australia want to, or see a need to, adopt the broadest specifications. However, if the Regulator considers that industry and consumers should adopt the broadest specifications, in a way that is not contrary to section 2.25 of the Code, then AlintaGas submits that the broadest specifications should be phased in over a number of years in a way that will not compromise Epic Energy's existing contractual obligations with various shippers.

## 4. RELIABILITY OF THE AMENDED FIRM SERVICE

AlintaGas notes that the Regulator has not accepted AlintaGas's arguments from its third submission to the effect that Epic Energy's proposed Permissible Limit of 1% is excessive and inappropriate. AlintaGas has reviewed the issues surrounding the Permissible Limit and, in the light of additional information presented here, requests the Regulator to re-consider his proposed decision.

Epic Energy is proposing, in clause 14 of the Access Contract Terms and Conditions, that it may curtail or interrupt a shipper without liability:

(a) when Epic Energy considers it necessary as a reasonable and prudent pipeline operator provided that the interruption or curtailment is within the Permissible Limit; or

(b) for Force Majeure; or

(c) if, when delivering gas at a particular delivery point, a shipper does not have sufficient contracted capacity at the delivery point and there is another shipper that does have sufficient contracted capacity at the delivery point.

Epic Energy may also curtail or interrupt a shipper in situations not covered by the above circumstances. However, in that case, Epic Energy must compensate the shipper for any direct losses the shipper suffers and must credit the shipper with the applicable Receipt and Capacity Charges.

The Permissible Limit is 1% of the shipper's contracted capacity multiplied by the number of days in the year. Thus, item (a) above could result in Epic Energy interrupting all shippers for more than 3 days in each year – being the 1% Permissible Limit multiplied by 365 days each year, to give 3.65 days – without any liability. AlintaGas submits that this is excessive and inappropriate for a supposedly "firm" service.

A report prepared in November 1996 by Tenneco Energy International (a firm which effectively folded into the Epic Energy group of companies), titled "*A Study of the Dampier to Bunbury Natural Gas Pipeline*" (the "**Tenneco Report**"), reviewed the operational and capacity practices in respect to the DBNGP.

The Tenneco Report discusses the concept of firm capacity. Specifically:

> "Firm capacity is a contractual concept rooted in the commercial relationship between the transporter and the shipper …

> "Typically, the transporter takes on the responsibility for interruptions under their control. These include the pipeline design, operations, maintenance and negotiated contract conditions that do not favor the firm capacity of one shipper over another.
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> "A firm shipper usually expects continuous access to firm capacity. He pays a reservation fee 100% of the time and expects access 100% of the time. If the transporter fails to provide capacity on demand then, the shipper can reasonably expect a refund of the reservation charge for the period of interruption. Exceptions would include force majeure events and mutually agreed shutdown periods for maintenance. Contracts usually allow service interruption without penalty for force majeure. But the transporter must refund reservation charges if they don't provide capacity under normal conditions. Since the transporter is selling an assurance that capacity will be available when called upon, they must plan facility outages to minimize loss of capacity." [Page 19]

AlintaGas concurs with the conclusions of the Tenneco Report concerning the level of reliability of a firm capacity service that is consistent with generally accepted industry practices. Specifically, firm capacity should be capacity that is available except for clearly defined cut-off conditions.

AlintaGas is not aware of other Australian Access Arrangements where mechanisms similar to Epic Energy's proposed Permissible Limit are utilised. For example, the proposed Access Arrangement for the Goldfields Gas Transmission pipeline and the Access Arrangement for the Parmelia pipeline both provide for firm capacity being available on a continuous basis except for force majeure, for planned maintenance or where there is an emergency that threatens the safety of people, plant or property.

Epic Energy's proposed Permissible Limit approach could result in ad hoc interruptibility. Such ad hoc interruptibility is very unusual for a "firm" service[2]. Effectively, the firm capacity service, as proposed, has the potential to be a firm service with unpredictable elements of an interruptible service included in it. There could be the potential for Epic Energy to oversell firm capacity, on the basis that the Permissible Limit defines the level of reliability that shippers of a firm service on the DBNGP contract for and should expect, in preference to providing a reasonable level of backup for plant and equipment. This would be unacceptable.

AlintaGas submits that the Regulator, in the Final Decision, should require Epic Energy to modify the curtailment and interruption provisions in the Access Arrangement so that shippers of the firm service are only curtailed or interrupted for:

(a) routine maintenance, provided that Epic Energy has first given shippers reasonable notification of its intentions, has used reasonable endeavours to agree with shippers the timing of the maintenance work and will minimise the period and extent of the capacity interruption; or

(b) emergencies, where the safety of people or property is at risk; or

(c) force majeure.

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2 Tenneco Report, Page 42.

## 5. COVERAGE OF EXPANSIONS AND EXTENSIONS BY THE ACCESS ARRANGEMENT

Clauses 12.4 and 12.5 of the proposed DBNGP Access Arrangement deal with expansions or extensions being included or excluded as part of the "Covered Pipeline". In conjunction with Amendment 45 of the Draft Decision, the clauses require Epic Energy to notify the Regulator if Epic Energy decides that an expansion or extension should not be covered by the Access Arrangement.

AlintaGas considers that the requirement to simply provide notice to the Regulator is inadequate. AlintaGas submits that the Regulator should also be required to provide its consent before an expansion or extension can be excluded from being covered by the DBNGP Access Arrangement.

A concern AlintaGas has if a pipeline owner is free to decide whether an expansion or extension is to be covered by the Access Arrangement, is that the pipeline owner may choose to cover only those expansions and extensions that will result in a general increase in pipeline tariffs. Conversely, the pipeline owner may choose to exclude the coverage of expansions and extensions that would reduce pipeline tariffs.

AlintaGas submits that a more appropriate set of conditions for determining if an expansion or extension of the DBNGP is to be covered by the Access Arrangement, are the requirements in AlintaGas's Access Arrangement for the Mid-West and South-West Distribution Systems. Clause 60 of that Access Arrangement requires the Regulator's consent before AlintaGas can declare that an expansion or extension (which would otherwise become part of the AlintaGas Gas Distribution System) is to be excluded from being covered by the Access Arrangement.