

# **CMS GAS TRANSMISSION of AUSTRALIA**

## **PUBLIC SUBMISSION No. 1**

### **DRAFT DECISION: ALINTAGAS ACCESS ARRANGEMENT**

**Submitted to OffGAR 5 May 2000**

## INTRODUCTION

CMS Gas Transmission of Australia (CMS) makes this first public submission in response to the notice of 14 March 2000 published by the Office of Gas Access Regulation (OffGAR). This notice invited submissions by AlintaGas and other interested parties on OffGAR's Draft Decision on the proposed Access Arrangement submitted by AlintaGas for its Mid-West and South-West Gas Distribution Systems.

The intended purpose of this submission is to identify and discuss several key aspects of the Draft Decision on AlintaGas Access Arrangement for Mid-West and South-West Gas Distribution Systems (Access Arrangement). CMS intends to comment further on other aspects of the Draft Decision in a later submission.

## SUMMARY

CMS believes that these provisions are denying it access to a gas market, which amounts to gas sales revenue of about \$250 million<sup>1</sup>. In fact, these provisions will allow AlintaGas to maintain its monopoly and hold out competitors for at least five years (i.e., Access Arrangement Period). Furthermore, the proposed tariff structures will stifle any Gas Retailer competition and this has the potential to reduce revenue on the Parmelia Pipeline and for Perth Basin Gas Producers.

CMS has identified the following provisions in the Access Arrangement that CMS considers being anti-competitive:

1. Proposal for a more stringent Gas Quality Specification;
2. Reference Tariff A - Tariff Structure
  - a) Reference Service A - basis for calculation of Interconnection Distance; and
  - b) Reference Tariff A - Standing Charge - set at an excessive level

CMS reviewed these provisions in relation to the following legislation:

- i) Gas Pipelines Access (WA) Act 1998 (GPAA);
- ii) Trade Practices Act 1974 (TPA); and
- iii) National Third Party Access Code for Natural Gas Pipeline Systems (Code).

According to legal advice that CMS has received, these provisions infringe parts of Schedule 1, Part 3, Clause 13 of the GPAA (Clause 13) and parts of s46 of the TPA.

Furthermore, CMS considers that OffGAR in issuing its draft determination in regard to these matters may have not fully discharged its duties under the Code. OffGAR's duties in reviewing any draft application include taking into account:

- the public interest, including the public interest in having competition in markets; and
- the interests of Prospective Users.

Each provision will be discussed separately in relation to the above legislation.

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<sup>1</sup> Source: AlintaGas Annual Report 1999 and CMS estimate

## DISCUSSION

### 1. GAS QUALITY SPECIFICATION

CMS is opposed to OffGAR's decision to provisionally accept AlintaGas' proposed gas quality specification for gas entering and being transported through the AlintaGas Gas Distribution Systems as it is anti-competitive and hinders gas producers, gas retailers and gas transporters accessing the AlintaGas Distribution System.

The proposed gas quality specification is more stringent than the requirements laid down in the Gas Standards (Natural Gas) Regulations 1999 issued under the Gas Standards Act 1972.

Table 1 supports CMS' assertion that the proposed gas quality specification for AlintaGas Gas Distribution System has been narrowed. CMS considers the proposed gas quality specification directly discriminates against gas from the Perth Basin from where the majority of gas is transported by the Parmelia Pipeline. AlintaGas' proposed gas quality specification incorporate the Dampier to Bunbury Natural Gas Pipeline (DBNGP) gas quality specification, which is more narrowly defined over a wider range of gas components.

The Parmelia Pipeline gas quality specification meets the gas quality specification laid down in the Gas Standards (Natural Gas) Regulations 1999 issued under the Gas Standards Act 1972.

**Table 1: Gas Quality Specification: Western Australia**

Gas Component	Units	Gas Standards Regs (WA)	Broadest <sup>1</sup> Specification	Broadest Specification More Stringent	Proposed Stringent Specification	Parmelia Pipeline Specification	Parmelia Pipeline Meets Stringent Specification
Carbon Dioxide	%		4.0	Yes	4.0	3.6	Yes
Inert Gases	%		7.0	Yes	7.0	5.5	Yes
Higher Heating Value (Min)	MJ/m <sup>3</sup>	37.0	35.1	No	37.0	37.0	Yes
Higher Heating Value (Max)	MJ/m <sup>3</sup>	41.0	42.3	No	41.0	41.0	Yes
Wobbe Index (Min)	MJ/m <sup>3</sup>	46.0	46.0	No	46.0	46.5	No
Wobbe Index (Max)	MJ/m <sup>3</sup>	52.0	51.5	Yes	51.5	51.0	Yes
Total Sulphur	mg/m <sup>3</sup>	50.0	10.0	Yes	10.0	23.0	No
Total Sulphur (including Odorant)	mg/m <sup>3</sup>		20.0	Yes	20.0	NA	No
Hydrogen Sulphide	mg/m <sup>3</sup>		2.0	Yes	2.0	4.6	No
Oxygen	%		0.2	Yes	0.2	0.2	Yes
Water	mg/m <sup>3</sup>		48.0	Yes	48.0	110.0	No
Hydrocarbon Dewpoint over the pressure range 2.5 to 8.72 MPa	degrees Celsius		<0	Yes	<0	10.0	No
Radioactive Components	Bq/m <sup>3</sup>		600.0	Yes	600.0	600.0	Yes

nb. Maximum Specifications unless specified.

NA - no odorant used in Parmelia Pipeline.

1: The Broadest Specification is really a misnomer, applied in existing regulations to what is really an alternate specification, actually narrower in some respects.

The decision by OffGAR to provisionally accept the more stringent gas quality specification can not be justified for the following reasons:

- i) Safety Issues
- ii) Anti-competitive
- iii) Value of AlintaGas

Each reason will be discussed separately below:

- i) Safety

The gas flowing through the Parmelia Pipeline meets the gas quality specification under the Gas Standards (Natural Gas) Regulations 1999. These are based and refer to the Gas Standards Act 1972, which defined the gas specification for gas supplied to customers of the State Energy Commission of Western Australia for the period 1971 to 1984 prior to any gas production from the North West Shelf and transport via the DBNGP.

During this period, all natural gas supplied to the Perth region was produced in the Perth Basin and obviously complied with the Gas Standards Act 1972. This occurred without any safety issues or concerns in regard to gas quality.

In fact, the current Parmelia Pipeline's gas quality specification is more stringent than that laid down in Gas Standards Act 1972.

- ii) Anti-competitive

The GPAA legislates that AlintaGas must not engage in conduct for the express or inferred purpose of preventing or hindering the access of any person to a service provided by means of the AlintaGas Distribution System.

The gas quality specification proposed by AlintaGas and provisionally accepted by OffGAR would mean that current and future gas sourced from Perth Basin producers would require additional processing. For some producers this might mean continued production is no longer viable. At the very least it would have the effect of increasing rather than decreasing costs and therefore lessening competition between gas producers and also between gas transporters.

CMS considers that the proposed gas quality specification will hinder gas producers, gas retailers and gas transporters in accessing the AlintaGas Distribution System. Therefore, CMS believes that the proposed gas quality specification in the Access Arrangement infringes parts of Clause 13 that deals with preventing or hindering access.

Any barriers to entry to any market mitigate against competition, and the ability of end consumers of gas to exercise choice over gas supplier, retailer, or trader.

Furthermore, the TPA legislates that AlintaGas being a corporation that has a substantial degree of power in the market must not take advantage of that power for the purpose of preventing the entry of a person into that or any other market. CMS believes that the gas quality specification in the Access Arrangement infringes parts of s46 of the TPA.

CMS believes that OffGAR's decision to provisionally accept a more stringent gas quality specification is in direct conflict with the Operative Provisions Clause 2.1(c) of the Council of Australian Governments' Natural Gas Pipelines Access Agreement 1997 that the Western Australian Government agreed to. Clause 2.1(c) states that:

*"The objective of this agreement is to establish a uniform national framework for third party access to natural gas pipelines that:*

*.....*

*promotes a competitive market for natural gas in which customers may choose suppliers, including producers, retailers and traders;"*

iii) Value of AlintaGas

OffGAR must also be cognisant that the Western Australian Government intends to sell AlintaGas at a price that will maximise its proceeds. Furthermore, the new owners of AlintaGas will undoubtedly wish to implement strategies to diversify its sources of gas and gas transport arrangements.

The Parmelia Pipeline provides the new owners of AlintaGas with an opportunity to successfully implement such strategies due to its lower transportation costs, its interconnection with Mondarra Gas Storage and its ability to offer AlintaGas' customers with a greater choice of gas supply.

Therefore, the ability to use alternate sources of gas supply, including the Parmelia Pipeline, will increase the value of AlintaGas for potential bidders for the cornerstone shareholding in AlintaGas. Furthermore, having competitive sources of gas supply will foster industry development both in gas production and end use of gas.

<b>CMS Proposal:</b>	<b>OffGAR substitute the proposed gas quality specification with the gas quality specifications of the Gas Standards Act 1972.</b>
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## 2. REFERENCE TARIFF A - TARIFF STRUCTURE

CMS is opposed to OffGAR's decision to provisionally accept a tariff structure for Reference Service A that incorporates AlintaGas' definition of interconnection distance and a standing charge that has been set at an excessive and discriminatory level. CMS believes these components hinder competition and ensure that third parties do not compete on a level playing field. In fact, CMS can demonstrate that these provisions will allow AlintaGas to maintain its monopoly and hold out competitors for at least five years (i.e., Access Arrangement Period).

CMS notes that OffGAR has proposed that:

*"Clause 21 of the Access Arrangement should be amended to provide a tariff structure for Reference Service A (or a succession of tariff structures for each year of the Access Arrangement Period) that accommodates a reasonable transition to the Reference Service A tariff from distribution tariffs that would have occurred for Users under the Gas Distribution Regulations 1996."*

However, it should be noted that this only provides for a transition and so Users will eventually incur the proposed standing charge of \$50,000 and therefore be much worse off than they would have been on the distribution tariffs that would have occurred under the current Gas Distribution Regulations 1996.

CMS argues that the tariff structure for Reference Service A is anti-competitive and discriminates against third parties due to:

- a) the basis for calculation of interconnection distance; and
- b) the imposition of a standing charge that is set at an excessive level.

Each issue will be discussed separately below.

### a) Basis for Calculation of Interconnection Distance

The basis for calculation of the interconnection distance is defined in Chapter 10 of the Access Arrangement and is as follows:

*".... a distance measured along the straight line which represents the shortest distance between the delivery point and the nearest pipeline or storage system from which gas is (or would be if an Interconnection Contract were entered into and necessary physical gate points and associated facilities were constructed) supplied into the AlintaGas Network;"*

This means that Reference Tariff A is to be calculated on the basis of the straight line distance from a User's delivery point to either the Parmelia Pipeline or the DBNGP, whichever is closest.

OffGAR and AlintaGas justify this approach as quoted from the AlintaGas Access Arrangement Information (section 2.2.1) on the basis that:

*"Use of distance to the nearest transmission pipeline as the measure of distance in the demand charge of Reference Tariff A is intended to mitigate the risk of inefficient by-pass of the AlintaGas Network."*

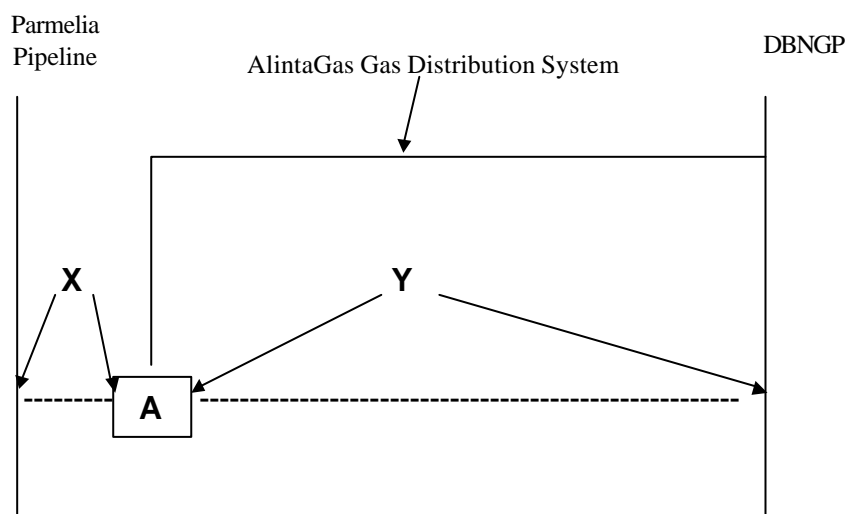
Although the intent of the language is clear, the effect of the language, if taken literally, will be anti-competitive to Parmelia Pipeline in favour of the DBNGP.

The following example will show how the proposed language will result in a pricing structure that disadvantages the Parmelia Pipeline in favour of the DBNGP.

### Example:

Currently User A (refer to diagram below) is connected to the AlintaGas Gas Distribution System and gas is supplied via the DBNGP. The straight line distance between the Parmelia Pipeline and User A's delivery point is "X" and the straight line distance between the DBNGP and User A's delivery point is "Y". The straight line distance "X" is less than the straight line distance "Y".

Under the proposed Access Arrangement, service to User A will be priced based on the straight line distance "X" as it is defined to be the interconnection distance, regardless of whether gas was delivered by the Parmelia Pipeline or not. Therefore, AlintaGas can price their transportation service at an opportunity cost discount and therefore make it less attractive for User A to receive service from the Parmelia Pipeline. Furthermore, the costs attributable to the difference between straight line distance "Y" and the straight line distance "X" are shifted to all other Users in a cross subsidy arrangement.



CMS has been negotiating with AlintaGas to interconnect the Parmelia Pipeline to the AlintaGas Distribution System. A proposal document jointly produced by CMS and AlintaGas to allow blending of Perth Basin gas with DBNGP gas in the AlintaGas Distribution System was accepted by the Office of Energy. However, the negotiation process with AlintaGas has been going on for nearly two years with a number of issues still to be resolved before interconnection can proceed.

The most recent hurdle has been the expressed desire on the part of AlintaGas to include Epic Energy (operator of the DBNGP) as a party to the interconnection agreement. A requirement to include a competitor into the interconnection agreement, and that competitor's demands to extract unilateral balancing fees and service charges, threatened to delay the competitive process even further.

A pricing mechanism that has the intentional or unintentional effect of holding out competitors is clearly anti-competitive. The TPA legislates that AlintaGas being a corporation that has a substantial degree of power in the market must not take advantage of that power for the purpose of deterring or preventing any person (eg. CMS) from engaging in competitive conduct in that or any other market.

CMS considers that the basis for calculating the interconnection distance as proposed in the Access Arrangement will have the effect of preventing CMS and other parties engaging in competitive conduct. In fact, this provision will allow AlintaGas to maintain its monopoly and hold out competitors for at least five years (i.e., Access Arrangement Period).

Therefore, CMS believes that this provision infringes parts of s46 of the TPA.

Furthermore, CMS considers that this provision does not meet the principles outlined in Section 8 of the Code. The Code indicates that a Reference Tariff should be designed to:

- replicate the outcome of a competitive market; and
- not distort investment decisions in pipeline transportation systems or any upstream/downstream industries.

<p><b>CMS Proposal:</b></p>	<p><b>OffGAR amend the definition for interconnection distance to:</b></p> <p><i><b>"interconnection distance means a distance measured along the straight line which represents the shortest distance between the delivery point and the nearest pipeline or storage system that supplies gas to that delivery point from which a User takes gas."</b></i></p>
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**b) Reference Tariff A - Standing Charge**

CMS considers that the standing charge of \$50,000 for Reference Service A has been specifically set at a high level by AlintaGas to ensure that third parties find it difficult to capture any AlintaGas' customers if they have to supply gas via the AlintaGas Gas Distribution System.

This provision protects the AlintaGas Trading Business, who can use the diversity of its customer base to maintain supply to customers under competitive threat, i.e., it can use its residential market to cross subsidise its industrial market. In fact, this provision will allow AlintaGas to maintain its monopoly and hold out competitors for at least five years (i.e., Access Arrangement Period).

The impact of the proposed standing charge results in the tariffs for Reference Service A proposed in the Access Arrangement generally being substantially higher than those currently prevailing under the Gas Distribution Regulations. Table 2 provides a comparison of regulatory regime tariffs for varying gas usage and distance.

**Table 2: Comparison: Gas Distribution Regulations and Access Arrangement Reference Service A Tariffs (\$/GJ)**

Annual Quantity TJ/year	Tariff regime	Distance (km) from nearest gate station					
		0.1	1	2	5	10	20
35	GDR (old)	0.0043	0.0434	0.0869	0.2172	0.4344	0.8688
	AA (new)	1.4000	1.4900	1.5800	1.8800	2.3700	2.8600
100	GDR (old)	0.0043	0.0434	0.0869	0.2172	0.4344	0.8688
	AA (new)	0.5100	0.6000	0.7000	0.9900	1.4800	1.9700
250	GDR (old)	0.0043	0.0434	0.0869	0.2172	0.4344	0.8688
	AA (new)	0.2100	0.3000	0.4000	0.6900	1.1800	1.6700

Table 3 highlights the extent of the difference in percentage terms.

**Table 3: Percentage Increase: Access Arrangement Reference Service A over Gas Distribution Regulations**

Annual Quantity TJ/year	Distance (km) from nearest gate station					
	0.1	1	2	5	10	20
35	32228%	3430%	1819%	866%	546%	329%
100	11740%	1381%	806%	456%	341%	227%
250	4834%	691%	460%	318%	272%	192%

The imposition of a \$50,000 per year standing charge constitutes a substantial barrier to entry for third party producers, retailers and traders alike. For an AlintaGas competitor to secure gas supply to a 100 terajoules per year customer who became contestable on 1 January 2000, just under half of the transport tariff paid by that AlintaGas competitor would be paid to AlintaGas to simply gain access to the market.

One of the stated objectives of the National Third Party Access Code for Natural Gas Pipeline Systems (the Code) is the promotion of a competitive market for natural gas in which customers may choose suppliers, including producers, retailers and traders.

Any barriers to entry to any market mitigate against competition, and the ability of end consumers of gas to exercise choice over gas supplier, retailer, or trader. The fixed charge incorporated in Reference Tariff A constitutes a substantial barrier to entry for competitors of AlintaGas.

Therefore, it may be seen that the tariff structure applicable to Reference Service A as currently proposed does not comply with the intent of the Code.

Whether it is intended, or unintended this provision hinders competition and therefore infringes Clause 13 of the GPAA. Furthermore, CMS considers that the standing charge will have the effect of preventing CMS and other parties engaging in competitive conduct. Therefore, CMS believes that this provision infringes parts of s46 of the TPA.

Overall CMS' contention is that the Standing Charge is either designed to block, or has the effect of blocking, access for third party producers, retailers and traders to the AlintaGas market.

We note that the submission by Apache Energy Ltd came to the same conclusion as CMS. Furthermore, the submissions by the Chamber of Minerals & Energy and Chamber of Commerce & Industry (respectively) question the Standing Charge in terms of not being cost reflective or promoting an efficient market.

We contend that the draft decision of the Regulator does not address the concerns that have been raised in the above submissions.

<b>CMS Proposal:</b>	<b>OffGAR mandates that AlintaGas withdraws the currently proposed tariff structure for Reference Service A and puts in its place a structure which is fair and reasonable, and is in accordance with the intent of the Code.</b>
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