

Dampier Bunbury Pipeline ABN 78 081 609 289

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Jenness Gardner
Chief Executive Officer
Level 4, 469-489 Wellington Street
Perth
Western Australia, 6000

Dear Jenness,

Thank you for the opportunity to respond to the Economic Regulation Authority's (ERA) Further Consultation on the Dampier to Bunbury Natural Gas Pipeline (DBNGP) Access Arrangement for the 2026 to 2030 period (AA6). The matters under consideration are the treatment of overrun revenue and a mechanism for demand uncertainty.

As the ERA notes, the outcome of the ERA's consideration of these matters may result in material change to the positions set out in the Draft Decision. We agree that the potential changes are material. We also therefore consider these issues would be better considered as part of the subsequent 2031 to 2035 AA period (AA7). We form this view because:

1. This further consultation occurs very late in the AA6 review process.
2. Only one week has been allowed to review the proposals as well as drafting of relevant clauses, which will result in material changes to the outcome and the matters consulted on during the AA process.
3. The timeline for response is inadequate and procedurally unfair. It provides no ability for either DBP or shippers to understand and contemplate:
 - a. what is the desired outcome the proposed changes are trying to achieve;
 - b. whether the proposed changes are the best way to achieve that outcome; and
 - c. what impact this will have on the operation of the DBNGP and the behaviour of shippers.

This therefore presents significant risks of unintended consequences. We consider the better approach would be for these matters to be the subject of a fulsome consultation process as part of AA7.

Overrun Charges

Notwithstanding the issues of constrained timing and materiality raised above, in this response, we cover three key issues in respect of overrun:

1. The impact of continuing to base overrun charges on some multiple (whatever multiple it might be) of the current reference tariff.
2. The potential for the ERA's estimates of "net overrun revenues" to grossly over-estimate our actual net revenues.
3. The significant legal and operational concerns the overrun charge may create once it interacts with the actual operations and contracts of our shippers; unintended consequences that the ERA may not have considered.

If the ERA is minded to proceed with its proposed changes, the drafting proposed by the ERA is very imprecise, and does not adequately define key terms. Nor has it adequately considered the interaction between overrun and other aspects of reference contracts. We have started the process of considering alternative drafting to address these concerns but are not yet able, in the very short time provided, to provide a robust set of drafting. We aim to do so as soon as possible. However, as an interim comment, the proposed use of an Overrun Tariff is inconsistent with the terms of all current and previously negotiated shipper contracts and as such could be unworkable, as the terms of all negotiated shipper contracts (i.e non reference shipper contracts) are unable to be amended unilaterally. We propose to provide specific comments on the proposed drafting later this week.

Of the three issues noted above, the third is the most substantive, and is the key reason why we consider that the ERA should avoid change until AA7 when more time than one week can be provided to parties to work through the issues. The first two issues are, in our view, solvable, and we present our solutions below; noting that solving these two less substantive issues does nothing to reduce the overall issue of unintended consequences.

Basing Overrun charges on a multiple of current reference tariffs

At present, overrun charges are set at 115 percent of the relevant reference tariff. As we point out in our response to the ERA's Draft Decision, we consider this is likely to be too low to act as an incentive not to rely on overrun. The ERA has suggested it may change. However, the issue here is not what the percentage may be, but rather that the percentage is applied to whatever is the reference tariff in a given year.

Consider a case whereby the ERA determines, in its Final Decision, that the efficient reference tariff in 2028 is \$2.40/GJ, and that the appropriate overrun charge is 115 percent of the reference tariff. If overrun volumes in 2026 (which determine the rebate on offer in 2028 as per the ERA scheme) are sufficient to drive the reference tariff down by 20 percent to \$1.92, a 15 percent premium on this produces an overrun charge of \$2.21. Effectively, what the ERA has done is produced a penalty price which is lower than the efficient price of the reference service in the ERA's regulatory model. It is unclear how this represents an efficient outcome; shippers will very quickly realise that inefficient actions on their part can lead to prices lower than would prevail if they continue to operate efficiently.

The only solution to this impasse is to either set the overrun charge at some level unrelated to reference tariffs, say \$3.00 per GJ, and escalate it by CPI or, if some markup is to be used, set it at a markup over the reference service price in the first year of AA6 (and then escalate it by CPI), rather than the reference service price in each year of AA6. Either approach will mean that the overrun charge is not affected by overrun volumes and would avoid the perverse outcome where the penalty charge ends up being lower than the expected efficient price formed at the start of AA6.

Estimation of net overrun revenues

The ERA's proposal for "net overrun revenues" uses the regulatory model fuel curve to estimate SUG costs for overrun. That is, the ERA applies the fuel curve in the regulatory model to the volumes of overrun. As we point out in our response to the ERA's Draft Decision, actual SUG volumes when the pipeline is operating inefficiently (which it is when overrun is happening; by definition we cannot plan for efficient provision of overrun) are vastly different from what the fuel curve suggests. This is likely to give rise to a significant underestimate of our costs, and therefore a significant over-estimate of net overrun revenues. In many cases, it may mean that we suffer losses from allowing shippers to overrun, due to the costs on a given day being very different from what the fuel curve suggests they might be.

There is a relatively simple solution:

- Take the actual SUG for a given day (A).
- Use the fuel curve to estimate the SUG for all reference and non-reference services (B).
- Subtract B from A to give an estimate of the amount of SUG used on that day for overrun.
- Multiply this by the cost of SUG in the regulatory model to determine the operating costs for the purpose of calculating net overrun revenue.

This maintains the ERA's basic structure for calculating net overrun revenue, but avoids the downward bias that comes from estimating costs for overrun based on a fuel curve that is not designed to capture the extremes of SUG represented by overrun volumes. We note that this does not include all of our costs, such as more maintenance and more frequent compressor overhauls. These would need to be added in over time. For the moment, and given the unduly tight timeframe for providing comments, we have focussed on fixing the more egregious issue of an incorrect starting point for the calculation.

Substantial unintended consequences

The Overrun revenue received by DBP represents a problem - it is a symptom of behaviour by shippers that is inconsistent with efficient, reliable and secure pipeline operations and presents challenges for DBP to manage the pipeline. The ERA's proposed 'solution' will only make this problem worse by reducing the disincentive on shippers to engage in this behaviour, sending the wrong signals to shippers and limiting DBP's levers for achieving efficient, reliable and secure operations. Rather, a solution is required that encourages shippers to contract appropriately for their flexible needs in a way that enables foreseeability of capacity use for the Operator and accordingly better efficiency, security and reliability of supply for all users.

We have reviewed the ERA's proposal and find it unworkable. We set out below, some preliminary comments explaining our concerns. We are still working on developing a better understanding of how the overrun charge position could impact different shippers and their interactions with each other and will respond on this as part of our comments on drafting.

General comments

The below provide further general commentary in relation to the proposed changes to overrun charges.

Inconsistency with National Gas Objective

As recognised by the ERA, the delivery of Overrun Gas is not a Pipeline Service.

Overrun is the use of Gas Transmission Capacity by a shipper which is beyond the amount that the shipper is entitled to use under its shipper contracts. If a shipper takes Gas in an amount in excess of the aggregate of its contracted quantities under all of its Capacity Services (i.e. Overrun Gas), this will result in a (uncontracted for) reduction in the capabilities of the pipeline intended to be made available to support other shippers' contracted quantities.

Overrun is often taken at times when Gas Transmission Capacity is under most demand. Therefore, the unauthorised use of Gas Transmission Capacity (i.e. Overrun) increases the probability of the Operator curtailing other shippers' contracted quantities.

Obviously, this is inefficient, unfair and should not be encouraged - shippers enter into, and undertake obligations under, contracts which commit to certain contracted quantities as part of their long term strategy to ensure energy security for their long term, and gas shortage vulnerable, projects. These long term contracts, and long term reservations of available Gas Transmission Capacity, should not be undermined by regulatory changes which make it more palatable for a shipper to take Overrun Gas, which is not efficiently scheduled taking into account demand from other reference and non-reference services, and interferes with the Operator's ability to deliver T1 Service.

The effect of Overrun 'freeloading' on Contracted Capacity, and its effect on the pipeline operations, is inconsistent with the promotion of safety, reliability and security of supply of natural gas. The ERA's proposal with respect to rebating 100% of the net revenue received from Overrun Charges will decrease the disincentives for shippers to take Overrun Gas (knowing that they will not bear the full burden of Overrun Charges due to their future rebate by way of reduction of tariffs). In the result, this will make the pipeline operate less efficiently, to the detriment of all shippers. So that the Gas Transmission Capacity can be efficiently utilised by all shippers on a fair and equitable basis, shippers should be incentivised to contract for a service that better aligns with their requirements and provides better foreseeability and certainty to DBP.

For completeness, AGIG notes that, pursuant to clause 15.5(d), each shipper has constant access to CRS information to manage its gas flows and has various options to adjust its usage of gas transportation services, gas demand requirements and contracted capacity levels (including by increasing its access to Capacity Services) to manage its need for, and take of, Overrun Gas.

Accordingly, the ERA's proposal appears to be inconsistent with the National Gas Objective. The ERA's proposal is concerned only with price and is not consistent with efficient operation and use of natural gas services for the long-term interests of consumers of natural gas with respect to quality, safety, reliability and security of supply of natural gas.

Apparent pseudo rebateable service

It appears that the effect of the ERA's proposal is an overrun rebate which operates as though overrun was a Rebateable Non-Reference Service (but with a 100% rebate (net of costs)). It is unclear to us why this is necessary.

Existing approach

We consider that all the changes proposed by the ERA are unnecessary and confusing. We note the regulator, shippers and DBP have historically agreed (by way of SSCs and Reference Services terms and conditions) that the Other Charges are genuine pre-estimates of the unavoidable additional costs, losses and damages borne by the Operator.

While the ERA may be of a mind to change the reference service terms and conditions in this respect, Shippers contracted to SSC's have agreed that with the genuine pre-estimate, adjusting the reference tariff will contradict this position agreed in the SSC.

The Clause 20.4(c) of the Reference Contract already provides: *"To the extent that the Other Charges are in excess of the costs, losses and damages actually incurred by the Operator as a result of the conduct giving rise to the Other Charges, the Operator will distribute such additional revenue annually in equal proportions amongst the shippers"*

Inconsistency with revenue and pricing principles

The ERA's proposal is inconsistent with the revenue and pricing principles in section 24 of the of the National Gas Law (as applicable to Western Australia). For example:

- a) the ERA's approach (by reducing the disincentives for a shipper taking Overrun Gas) sends price signals which undermine the efficient investment in connection with the pipeline. Most (but not all) long term projects rely on security of gas transmission. On the DBNGP, security of gas transmission is primarily contracted through T1, P1 and B1 Services. Overrun increases the probability that, by other shippers taking more than their contractual entitlement, the integrity of the T1, P1 and B1 Services will be impacted, meaning a reduction of the security of supply under T1, P1 and B1 Services. This reduction in the utility of T1, P1 and B1 Services places downward pressure on the demand for these services, which undermines the economics of the pipeline and places upwards pressure on tariffs.
- b) the ERA's proposal does not appear to have regard to the economic costs and risks of the potential for over utilisation of the pipeline – to the contrary, it appears to us that the ERA's proposal encourages over reliance on overrun by returning Overrun Charges to the shippers whose behaviour caused the relevant over reliance.
- c) As noted above, depending on the level of the Overrun Charge and the volume of Overrun Gas taken by shippers, the impact of reducing the Reference Tariff by 'Net Overrun Revenue' could result in a circumstance whereby the cost of taking Overrun Gas is lower than what the ERA asserts in its Final Decision is the efficient price for Reference Services.

Demand uncertainty fixed principle

Notwithstanding the issues of constrained timing and materiality raised above, in the case of the demand uncertainty fixed principle, we consider the mechanism should allow for consideration of adjustments within AA6. This is consistent with the approach the ERA has proposed in respect of overrun and also the current approach to rebateable services.

We are concerned that an accumulated variance, whether high or low, has the potential to cause significant mismatch in AA7 between the calculated costs to operate the pipeline and the revenue that will be allowed to be recovered. We therefore consider a better approach may be to consider application of an true-up throughout AA6.

Conclusions

As noted above, we have three major concerns in respect of the proposed overrun charges being the link between the charge and current prices, the way net revenues are determined and, more substantively, the unintended consequences of the mechanism the ERA proposes. The first two, as we outline above, can potentially be solved, but the latter cannot, which is why we consider that the issues should be addressed as part of AA7, rather than rushed through AA6 when neither we nor shippers have been given time to consider the ramifications of the ERA's approach. In respect of the demand uncertainty fixed principle, we accept this in principle, but not the mechanism whereby the unders and overs are applied in the first (and to a limited extend second) year of AA7.

In respect of both the overrun mechanism and the demand uncertainty fixed principle, we have some concerns in respect of the ERA's drafting of the relevant clauses, which is inconsistent in many places and could cause confusion. We will provide as soon as possible what we consider to be more robust drafting, as one week is insufficient time for us to undertake a proper legal review. These drafting points apply to both the overrun and the demand uncertainty mechanisms.

If you would like to discuss any aspects of this submission, please do not hesitate in contacting either myself or Peter Bucki – Group Head of Regulation.

Yours sincerely



Roxanne Smith
Executive General Manager Corporate and Regulation