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A few words.

28 April 2010

Mr Mike Buckley
General Manager
Network Regulation North Branch
Australian Energy Regulator

Email: nswactgas@aer.gov.au

JGN Access Arrangement 2010–2015 — Draft Decision and Jemena's revised proposal

Dear Mr Buckley,

Please find attached AGL Energy Limited's ("AGL") submission in relation to the Draft Decision released by the AER in February 2010 and the revised proposal submitted by Jemena Gas Networks on 19 March 2010.

AGL Energy, as the largest user of reference services provided by Jemena Gas Networks in NSW, is disappointed that Jemena have not elected to adopt the revisions put forth by the AER in its Draft Decision. On the whole, we are supportive of the Draft Decision and are of the view that it represents a sound basis for the terms and conditions applying to access and use of the NSW gas networks.

AGL's main concerns with the recently revised proposal released by Jemena are:

- Jemena are still proposing a 33.4% increase in their Volume Throughput Rate from 1 July 2010 to apply to V-Coastal sites, notwithstanding the AER's draft decision which would have resulted in a 3.73% increase. As we have argued previously when we were looking at a 34.3% increase based on the initial AA proposal, this is a major step change in the network distribution charge that can only result in significant price shock to end-use consumers if implemented from Day 1 of the new Access Arrangement. Whatever the eventual outcome, AGL argues for a smoothing of any material increase over the five years.

- The revised demand forecast for the tariff or volume market is not in line with what AGL sees. As was the case with the initial forecast, we are not convinced that a sufficient case has been demonstrated for the assumptions employed.

- Jemena's insistence on its self-appointed right to impose a different balancing regime on Users through the RSA is not tenable and is most concerning. This clause, if retained, would effectively nullify the STTM in the Sydney Hub and undo the efforts of governments and industry to usher in a new gas market.

- The revised terms and conditions, both in the Access Arrangement and in the Reference Service Agreement, are still contentious and do not align with the tenor and details of Use-of-System agreements that are currently in force in other States and that we work with on a daily basis. AGL seeks revisions in a number of key areas.

Should you have any queries in relation to our submission, please feel free to contact George Foley on (03) 8633 6239

Yours sincerely,

Alex Cruickshank
Head of Energy Regulation

AGL Submission: JGN Access Arrangement 2010–2015 — AER Draft Decision and Jemena's revised proposal

2010 volume tariffs

Jemena Gas Networks are proposing a 33.4% increase in their Volume Throughput Rate from 1 July 2010 to apply to V-Coastal sites, which is where the majority of NSW retail customers are located. This is a major step change in the haulage rate that can only result in significant price shock to end-use consumers if implemented from Day 1 of the new Access Arrangement.

Should JGN have complied with all aspects of the AER's Draft Decision, this increase would have been moderated to an acceptable level of 3.73%. Whatever the eventual outcome approved by the AER in the Final Decision, AGL would argue, as it did previously, that it is not in the interests of Users and end-use consumers to be faced with significant price shocks and that a smoothing of any approved increase that is deemed material over the five years would represent a better outcome.

Minimum demand bills

JGN has retained the minimum bill for demand customers, notwithstanding AER's Draft Decision requiring removal of the minimum demand bill. JGN adduces an "oversimplification of network pricing principles" and "simplified representation of the principles underlying efficient network tariff setting" on the Regulator's part to support its position. Nevertheless, no further detail on these principles (or complexity) is provided by the Service Provider in its revised proposal. The stepped increase may remove the initial price shock but after the 5 years the full shock will still be manifested. Furthermore, JGN's arguments seem to rely (solely) on the possibility that the STTM will deliver reduced costs in gas and make the transition to Demand worthwhile.

AGL suggests amendment in accordance with the AER's Draft Decision.

Alternative balancing arrangements

It is of great concern that Jemena persist in insisting on their rights to enforce, contractually via clause 7.4 in the RSA, an alternative balancing regime in the event that a gas balancing mechanism introduced by AEMO (i.e. the STTM) fails to meet the "operational requirements of the network". The first and obvious point to make here is that it is not AEMO imposing a different balancing regime in NSW but AEMO implementing STTM as required by the STTM amendments to the National Gas Law and National Gas Rules, changes which are part of the gas reform process endorsed by the MCE.

The stated reason for Jemena's stance on this issue is that the STTM leaves responsibility for the ongoing safe and reliable operation of the network in the hands of JGN. Jemena's assertion rests on the view that they alone are responsible for system security whilst the STTM, in particular the Market Operator Service (MOS), is merely a financial allocation. They draw a spurious distinction between financial balancing and physical balancing, without allowing for the interaction between financial drivers in a market and its impact on gas flows. There is no disputing the fact that JGN are responsible for system security. With that very much in mind, the market design for the STTM has adopted the concept of Contingency Gas (CG), which is based on the attributes of the NSW Gas Supply Continuity Scheme. Under the CG process, JGN are entitled to approach AEMO and ask for a conference to be convened if they have a view that gas supply in the days ahead may not be sufficient to meet expected demand. If AEMO agrees with this assessment, then AEMO is obliged to call on offers of additional supplies or voluntary curtailment, subject to availability on the day. JGN are in a position to call for their own voluntary curtailment from those who have accepted the Capacity 1st Response Tariff. If these measures are insufficient in JGN's view, they have the ability to initiate involuntary curtailment as per the load shedding tables.

It is therefore not the case that JGN have no alternative but to revert to the current balancing regime, including the regime of Operational Balancing Gas, when system security is, or is perceived to be, under threat. They have measures available to manage stresses on the network system. The STTM will encourage greater flexibility and innovation, such as intra-day renomination facilities on pipelines that hitherto locked down their nominations the day before. We are seeing this already in terms of new service offerings from pipeliners. Daily price signals and cash settlements introduced by the STTM will lead to behaviours by users and shippers which will contribute positively to the maintenance of system security. Commercial incentives are delivered by the STTM in the form of spot price deviation risks for Users that take a short market position. As we have seen in Victoria on quite a number of occasions, market prices do act as powerful signals to bring forth additional supplies in the short term.

AGL has publicly supported a discontinuation of the NSW Gas Supply Continuity Scheme as it expects the STTM to deliver strong commercial price signals that should mitigate a re-occurrence of the 2007 events that resulted in the establishment of the Scheme. One of the weaknesses of pre-STTM market arrangements in NSW is the absence of price signals, other than OBG (which is only invoked by the Network Operator only when the market as a whole is forecast to be short), to drive home to causers the consequences of inadequate nominations. The absence of price signals and cash settlements, coupled with the resolution of imbalances through forward nominations, allowed participants to be less than fully contracted. The day-to-day price signals and daily cashing out of positions in the STTM will provide the commercial drivers that are currently missing.

AGL considers that Users are left with a large operational liability and risk if this clause in the RSA is retained — Users require certainty as to how gas balancing will operate in the market. The STTM's MOS and CG provide market mechanisms by which both the financial and the physical flow of gas may be regulated by market processes (in line with the overarching market goals of the STTM). JGN would in all instances have recourse (and should be restricted) to involuntary curtailment in order to preserve the safety and minimum operational requirements of the network.

Demand forecasts

The revised gas demand forecast submitted by JGN has again been prepared with the assistance of NIEIR, consultants engaged by the network operator. AGL is disappointed to see that the numerous comments we provided in our first submission of 10 November 2009 have not been acknowledged and reflected in the revised set of forecasts — and therefore we believe that our earlier comments are still appropriate.

We are even more surprised that the improved economic outlook and changes to government programs and policy since the initial forecasts for JGN were prepared in early 2009, all of which ought to translate into further increases in gas volumes in NSW, have somehow not resulted in a revised forecast that aligns with generally accepted outlooks. At a high level, some of these changes are:

- Improvement in economic conditions;
- An increase in the current existing residential per customer usage since the previously quoted figure;
- An increasing trend in the residential usages which contradicts the projected decline; and
- Delay or cancellation of the ETS and home insulation schemes.

AGL has compared the old and new NIEIR reports and we offer the following comments and observations. As we have stated above, the comments provided in our earlier submission are still also relevant.

- NIEIR and JGN have now updated the average existing residential customer usage as being 21.5GJ in 2009/10, up from 20.8GJ in 2008/09 that was in the previous report. This is a 3.4% increase and contradicts their projected decline in average usage. This alone ought to lead to an increase of 3.4% in the tariff market volumes, without any change in assumptions.
- However, after acknowledging a higher average usage as a reference point, NIEIR and JGN go on to negate this impact by actually worsening their projected decline in average usage of existing customers. Previously they showed a drop of 2.2% pa, and now this rate of decline is up to 3.1% pa. AGL does not see any justification for the declining trend, let alone an increase in this rate of decline.
- NIEIR and JGN still quote the now defunct home insulation scheme as a driver for reduced residential usage.
- NIEIR and JGN show projected increases price increases of 28.1% between 2009/10 and 2014/15 for residential customers and 38.8% for business. The

only justification is an ETS ‘to be introduced by 2010-2011’. This does not seem credible, given recent developments. Furthermore, the projected prices are now shown to be higher than in the previous version.

- NIEIR and JGN note better economic performance than expected in the last few months, and economic growth in NSW has been revised upwards in 2009/10 and 2010/11. However forecast NSW growth has been revised downwards in 2012/13 and 2013/14, apparently due to stimulus effects winding down and to contractionary monetary policy. Overall the forecast economic growth is barely changed at 2.0% pa. AGL is surpised not to see a significant revision upwards in overall gas demand stemming from this revision to the economic underpinnings of the forecast.

- NIEIR and JGN have revised upwards the demand in the C&I market in 2010-2013. However they still show a C&I market declining by 0.8% pa. The stated reason for the decline is the price impacts. AGL would argue that an increase in line with economic growth would be more reasonable.

- Table 5.1 of the revised NIEIR report persists in excluding gas-powered generation (GPG) from JGN’s forecast gas consumption by sector. AGL queried this anomalous exclusion in its previous submission and, whilst acknowledging the difficulty in forecasting non-baseload GPG usage, argued that it is now a source of gas consumption in the network and should be included in overall industrial demand. As we stated previously, the absence of GPG seems questionable at best and can only exacerbate any downward trend that is being projected.

Capacity 1st response tariff

The discount was not reduced by JGN and stands at 50% of the reference demand tariff. JGN justify this on the basis of their own customer survey which suggests a low take-up at a 25% discount. The discount eligibility has been lifted from a minimum consumption rate of 100 GJ/hour to a rate greater than 350 GJ/hour. The modifications partially take into account the AER’s Draft Decision (and, as per the survey submitted, more incentive would seem to be required for take-up), the figures are still based on a forecast that is not assured or guaranteed (and JGN as always has recourse to its right of involuntary curtailment over and above any voluntary curtailment plans proposed).

AER, Users and customers should have as much certainty as possible which guarantees JGN’s forecasted take-up before JGN’s proposal is accepted.

Whilst AGL does support this innovative offer from JGN as a common sense move to increase the robustness of the Network Operator’s curtailment options, we did seek clarification and amplification on how the call-up for voluntary curtailment would be managed and how Users would be kept informed and the consequential impacts on billing arrangements, booth network and retail.

Reference Service Agreement (RSA)

The AER has required some modifications to the reference service agreement put forth by Jemena as part of the Access Arrangement and at the same time has set aside concerns raised by AGL and other Users. Whilst we did indicate at the outset that we are on the whole accepting of the Draft Decision, we are of the view that some of the issues in relation to the RSA need to be put back on the table.

We restate those issues, as well as some additional comments in relation to amended clauses, that we regard as significant from a User perspective.

Clause 5.6(b)

This clause which relates to Authorised Overruns is unamended and AGL repeats its previous comment: the indemnity is very broad and should be limited to damage caused by the User.

Clause 7.4

The clause, requiring a different regime for operational gas balancing at Jemena's assessment of the efficacy of the STTM, is not acceptable for reasons outlined earlier in this submission.

Clause 15.12

JGN should be liable for their own negligence or wilful misconduct. This is a fundamental principle at law.

Clause 17.1

Meter data provision is a big problem for any User. What format must Jemena provide the data in? What about standards in relation to data validation. AGL does not see why JGN do not indemnify Users where they are negligent or fail to comply.

Clause 17.5

This provision is improved, but it still would be equitable for JGN to indemnify the User against any loss when considered against all indemnities that a User has to provide JGN.

Clause 22.1

This relates to issuing of invoices and is a big issue for us. It should be no more often than monthly and the invoices should specify the charges for each Delivery Point so that the retailer can verify them and prove them to a customer or a court. AGL does not think it reasonable for invoicing frequency to be at the absolute discretion of the Service Provider. The timing should be by agreement and provide sufficient time to enable a User to run automated reconciliation processes prior to payment, for example no more than one per month.

Clause 22.6

A User should be able to withhold disputed amounts. This is standard practice in contractual arrangements. To give effect to this, AGL requests that the words ‘manifestly wrong’ within clause 22.6(c) be removed and replaced with ‘genuinely disputed’.

Clause 22.8

This new clause is as follows:

> (a) Where the Service Provider has:
>
> (i) undercharged or not charged a User, the User is not obliged to pay the correct amount pursuant to clause 22.8(b) to the extent the User is precluded by law from recovering those charges from its customers; and
>
> (ii) overcharged a User, the User may seek to recover the correct amount to the extent permitted by law and pass those charges through to its customers,
>
> *provided that the User has complied with the requirements of all applicable Laws and any relevant contracts and has used reasonable endeavours to recover the relevant charges in accordance with its rights at Law or under a relevant contract.*

AGL suggests the underlined words be deleted and the italicised words be moved to the end of sub-clause (i). If the Service Provider has overcharged a User, that User will have no basis on which to recover those charges from end-users.

Clauses 26.1(a)(vii) & (viii)

These exclusions, namely equipment breakdowns and native title claims, should be deleted as they are not Force Majeure events. They are within Jemena’s control.

Clause 28.2(b)

JGN’s argument and eventual reliance on clause 28.2(b) does not cover the concern (or explicitly address the allocation of risk and liability) set out in the AER’s Draft Decision. AGL suggests the inclusion of explicit wording in clauses 15.12(b) and 24.3(b) allocating JGN the liability related to JGN’s negligence in dealing with user requests and/or carrying out acts of decommissioning, disconnection or suspension.

Clause 28.4(b)

In relation to scope of liability, AGL argues that this should be reciprocal and should not apply where adequate insurance is not maintained.

Clause 30

There needs to be non-contentious triggers within thin clause describing the circumstances under which Jemena can drawn on credit support provided by a User. It should not be at the ‘absolute discretion of the Service Provider’.