



Attention: Mr Sebastian Roberts
General Manager
2012 Victorian Gas Access Arrangement Review
Australian Energy Regulator

By email: VicGAAR@acc.gov.au

15th June 2012

Dear Mr Roberts

RE: APA GasNet Access Arrangement Submission 1 January 2013 to 31 December 2017, March 2012

Australian Power and Gas ("APG") welcomes the opportunity to provide comment on the above Access Arrangement proposal. APG is a national retailer of gas, electricity and green electricity products to the domestic energy market. We have both gas and electricity licenses in Victoria, New South Wales, Queensland, ACT and South Australia. We currently have in excess of 300,000 customers in Victoria, New South Wales and Queensland. As a Market Participant on the Victorian Transmission System ("VTS") and as an active and growing retailer in Victoria, APG takes particular interest in ensuring this 4th Access Arrangement is fair, equitable and in the best interests of our customers.

Though in general we support market based solutions as the most efficient and effective mechanism, we recognise that regulatory oversight and price setting of services provided by natural monopolies such as APA GasNet, is an imperative to uphold the National Gas Objective for Victoria. Where competition does not exist, regulation allows rates and prices to be set fairly and equitably and services to be provided in a non-discriminatory and efficient manner. It is with these principles in mind we make comments on the proposal submitted by APA GasNet for the 4th Access Arrangement ("AA4") of the VTS.

We wish to address the following specific issues and further detail is attached.

Capital Expenditure:

We note the extraordinary large Capital Expenditure (Capex) forecast and seek that adequate scrutiny is given to its validity given the demand requirements over the AA4 period.

Extensions and Expansions:

We maintain that extensions and expansions should ultimately recognise the existing regulatory framework and investments should eventually be rolled into the capital base once the overall economic benefits become positive. This is in the long term interests of customers.

Authorised Maximum Daily Quantity Credit Certificates (AMDQCC):

We hold the view that AMDQCC should form part of the Reference Service. However in absence of such, be formally recognised as part of the Rebateable Services, with rebates on tariffs clearly visible to the market.

Annual Tariff Adjustments:

Annual adjustments should not be uncertain and unresolved prior to pass through. It is unworkable to have unapproved or temporary adjustments passed through to customers. Hence we oppose the inclusion of an automatic pass through of annual adjustments should the AER delay approval.

Terms and Conditions:

We note that many terms and conditions have been changed to reflect a consistent format of the Amadeus Access Arrangement. However, we argue that this should not deteriorate the position of Market Participants, particularly with regards to prudential arrangements.

If you have any queries in relation to our comments or issues, please contact Libby Hawker, Market Development Manager on 03 8621 3709.



Shelley Reed
General Manager Wholesale Gas & Carbon

Detailed Submission

Forecast capital expenditure

We note that APA GasNet proposal contains a rather ambitious Capex program funded by an extraordinary requirement of \$346.4 million over the AA4 period. Whilst we do not discount the need to ensure system security and appropriate planning to alleviate current or future capacity constraints, we ask that the Regulator undertakes adequate scrutiny to ensure the Capex is not excessive and justifications are sound against the standards defined in clause 79 of the National Gas Rules (“NGR”). We also seek that the Regulator prudently weighs up the capex against the demand requirements, as to us, trends do not show a clear case for warranting such levels. Furthermore we question whether such an ambitious program will realistically be fulfilled or will simply lead to over recovery in the AA4 period.

Extensions & Expansions

We note in the proposal that “APA GasNet can elect for incremental capacity associated with that non-conforming capital expenditure not to be covered by the access arrangement”¹. It is unclear how exactly expansions and extensions related investments would be considered *non-conforming capital expenditure* and we believe this needs to be clearly articulated, particularly how this interacts with rule 83 & 84 of the NGR.

We are of the view that APA GasNet’s proposal of electing to derive a new tariff zone relevant to the extension and have associated revenue excluded from the target revenue calculation needs to be carefully considered on its impact to customers. We are uncertain as to the reasons why extension derived incremental revenue warrants different treatment and should not be included in Target Revenue under Schedule D of the AA4. This could potentially price out customers from gas services in particular zones, with tariffs set at levels beyond which would be fair and equitable.

APG strongly believes that any investment for expansion or extension should ultimately recognise the existing regulatory framework. We understand the Transmission Capacity Working Group established by AEMO looked extensively at the issues surrounding transmission investment and developed market design solutions that could address the issues. Although these solutions are being progressed via the Declared Wholesale Gas Market Consultative Forum, we believe that the investment incentives defined by this AA should be flexible so as not to preclude the adoption of these solutions agreed by the industry.

We believe that consideration should be provided to shift excluded pipelines into regulated assets at a future date when overall market benefits become positive. We suggest any determination made by the AER on 7.1 or 7.2 should take into

¹ APA GasNet – Access Arrangement Revision Proposal Submission – March 2012 page 25

consideration whether a positive economic benefit can be identified in the future, at which point the investment would be included in the regulated asset base and AMDQ or AMDQ CC (as defined in the NGR) would be transferred to market participants. This may need to involve a subsequent review date to the decision surrounding 7.1 and 7.2 that considers market power and identifies market benefits of the investment at a prescribed future time.

Treatment of AMDQ credit Certificates

Australian Power and Gas holds the view that AMDQ CC should be considered part of the Reference Service. The AMDQ CC mechanism is essentially a supplement service for transmission, whereby preferential rights allow participants to manage the risks associated with use of the pipeline. It is a facility that is widely used, evident by the significant contracting of ADMQ CC by participants. We support the AERs proposed rule change (currently at Final Decision stage with the AEMC) to ensure the AER has flexibility in defining Reference and Rebateable Services under the NGR. We see the proposed changes to *both* definitions as a small step to provide greater clarity to defining AMDQ CC, as well as other pipeline services that are currently ambiguous, or fall outside of regulatory treatment when they clearly should not.

In the absence of AMDQ CC explicitly considered a reference service, any rebates resulting from AMDQ CC that APA GasNet alleges to make against tariffs should be clearly defined and identifiable to the market. In its response to the AEMC Draft Rule Determination in respect to Reference and Rebateable Services, we note APA GasNet considers that any additional revenue from unused AMDQ credit certificates contract capacity is returned as a rebate against all tariffs². Besides the obvious issue of a blanket rebating approach against all tariffs regardless of the level of cover of AMDQ CC taken by participants, the extent to which this occurs or has occurred is not transparent to the market. We do not believe AMDQ CC revenues are appropriately dealt with in this way and argue for at least greater scope to formally define AMDQ CC rebates in the tariff calculation.

Tariff Controls & Adjustments

Cap and Collar Mechanism

We note that APA GasNet has submitted for the removal of the current cap and collar mechanism which limits revenue risk arising from the deviation of actual volumes from forecasts. Our comments in relation to this are that price certainty is extremely important and we see the current mechanism removing the chance of large deviations, limiting both upside and downside risk to APA GasNet and indeed prices movements to Participants and ultimately customers. In this way the current

² APA GasNet submission letter to the AEMC Draft Rule Determination on definition of Reference and Rebateable Services, page 2, dated April 26th 2012.

model shares equally, the potential upside and downside volume risk and the subsequent impact on tariffs.

We are unconvinced of the arguments presented by APA GasNet that they are unfavourably treated by the arrangement, and noted this was indeed a mechanism proposed by them as an alternative to eliminate volume risk in the last AA. In determining the appropriateness of removing such bounds, we hope the Regulator gives scrutiny and due consideration to the accuracy of forecasting undertaken by APA Gasnet.

X Factor

We seek clarification as to the justification behind the increase in the x factor to 3 % as it is unclear in the proposal supplied by APA GasNet.

Automatic mechanism for annual tariff adjustments

We do not support the automatic adjustment mechanism proposal as detailed in clause 4.7.5 whereby if an approval to a tariff adjustment is not forthcoming from the AER by 1 January, tariffs may be increased irrespective. Retailers would have no option but to pass the unauthorised and potentially temporary tariff increase through. It is unreasonable and impractical to have a potentially unresolved tariff increase passed through to customers. Further, such a mechanism may add to administrative costs with repealing the adjustments should increases not be subsequently approved.

We believe that Clause 4.7.2 (a) poses similar issues of price uncertainty in which further adjustments could arise. The words “or will be incurred” should be restricted to carbon cost events as this is the only event that should have an element of estimated cost. All other pass through events’ should be realised costs for pass through to be considered.

With respect to the timeframe of annual tariff adjustments, retailers must have a clear understanding of changes as soon as possible prior to the end of the year, ideally in November and no later than 1st December. This allows for regulatory requirements such as the gazettal of prices at least one month in advance, notifications to customers and to accommodate billing system changes in time for the annual tariff adjustment period from the 1st January.

Carbon Costs

With respect to carbon costs, we note that emission liability for pipelines will be under two elements; that is, for fugitive emissions and combustion emissions. Combustion emissions are the liability of the natural gas supplier, unless an Obligation Transfer Number “OTN” is in place³. We understand that both AEMO and

³ AEMO has proposed a Rule change to transfer title to metered operational gas from injecting participants to withdrawing participants so that withdrawing participants will be the natural gas suppliers in this case.

APA GasNet are seeking clarity as to the party that has operational control of the Declared Transmission System, and therefore potential liabilities under the Clean Energy Act. At the time of this submission, this remains unresolved. As liability on the operational controller (facility) at this point is identified as pertaining to fugitive related emissions we believe that carbon costs under this AA should distinctly be categorised as fugitive emission related carbon costs only.

Terms and Conditions

F.2 Billing & Payment

Recovery of additional amounts clause (c).

With respect to invoices to recover additional amounts, we believe that this should be restricted to revised amounts as issued by AEMO as per the previous AA, with a similar invoice period of two business days after issuing the revised amounts. We believe this should be limited as any other legitimate recovery will be contemplated under the cost pass through provision; that is, F3. However, in the case of recovery of additional amounts that specifically pertain to errors, there should be reference to the last paragraph where a time limitation applies.

F.4. Prudential Requirements

It is our experience that prudential requirements in the energy sector have a history of being onerous and can form a barrier to participants' market entry and expansion. We are disappointed that clause F4. leaves scope to continue this theme. We have always maintained that provision of credit support should be commensurate with the level of risks associated with payment default and balanced to recognise the costs that the arrangements impose on participants.

We are very concerned that clause (a) suggests that credit support arrangements are to be solely at the discretion of APA GasNet. The drafting lacks reference to any consistent calculation methodology in determining the quantum, or criteria for determining the type of this support. In our opinion, the clause as worded may produce an arrangement that is unfair, risks being discriminatory against smaller unrated participants and is susceptible to over-provision. It is therefore unacceptable.

We maintain that participants should be given flexibility to provide credit support in a low cost manner, commensurate with the risk of payment default and with consideration to that participant's risk profile. Credit support should be flexible to participants for provision upfront but also to maintain the arrangement. We believe forms such as cash deposits, bank guarantee or indeed a mix should be available. Where participants are not officially rated by an agency, assessments of profiles according to models such as Dunn & Bradstreet should be sufficient.

F.10. Assignment

APG believes the provisions for change of control should be removed. These clauses provide that in circumstances where there is a change in control of a party (affected party) the Deed cannot be enforced until consent has been obtained from the other party. Further, the other Party may terminate the Deed if consent under paragraph (d) is not obtained within 60 Business Days of the earlier of the date on which the Affected Party first notifies the other Party of the Change in Control and the date on which the other Party becomes aware of the Change in Control. We stipulate that 'change in control' may be beyond the immediate control of the parties (as in the case of a publically listed company) and in effect, a subsequent trigger that the Deed is not enforced until consent is obtained from the other party maybe an unreasonable disruption to continuing business. Further we see this potential disruption as inconsistent with the application of the NGO with regards to reliability and security of supply.

F11 Confidentiality

We believe this clause should make provision for disclosure to any financiers or prospective financiers of a party, as exceptions to consent requirements (in addition to those already specified as a lawfully required by an authority). Further, we believe there should be explicit provision for disclosure due to adherence of rules of a stock exchange, again as an exception to consent requirements under this clause F11.