

6 August 2007

Mr Chris Pattas
General Manager
Network Regulation South
Australian Energy Regulator
GPO Box 520
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BY EMAIL: chris.pattas@aer.gov.au

Dear Mr Pattas

**GASNET AUSTRALIA (OPERATIONS) PTY LTD
ACCESS ARRANGEMENT 2008-2012**

We are pleased to provide a submission on revisions lodged by GasNet Australia (Operations) Pty Ltd (GasNet) in respect of the GasNet's Access Arrangement for 2008 – 2012 (AA3).

It has come to our attention that GasNet is proposing major changes for AA3 relative to the previous Access Arrangement (AA2). In particular, GasNet is proposing the removal of several categories of prudent discount. These changes are likely to have a significant effect on our members. At least one member is now facing up to a 160 per cent increase for delivery costs associated with its gas use - from \$0.4 million per annum currently to over \$1.0 million in 2008.

In addition to the withdrawal of the 'prudent discount', the EUAA has a number of concerns about GasNet's proposed substantial capital works program and the manner in which GasNet has communicated these prospective changes to large gas customers. We are also concerned about the low level of information disclosure associated with these changes that has resulted in our members not being able to fully understand the rationale behind them.

REMOVAL OF THE PRUDENT DISCOUNT

Relevant for the GasNet review, Section 8.43 of the National Third Party Access Code for Natural Gas Pipeline Systems (the Gas Code) states (in effect) that if GasNet faces a credible bypass threat for a particular user, and the Reference Tariff would be higher than if calculated with regard to the alternative costs to a user, the regulator may approve a Prudent Discount. GasNet proposed a Prudent Discount for the four tariff zones in 2002, including the Latrobe zone; and this was accepted by the ACCC. As we understand it, this

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represented the continuation of tariff pricing practices that had existed for many years, and the formal proposal of the Prudent Discount was made in good faith. The removal of certain prudent discounts at the conclusion of the AA2 regulatory period has not previously been mentioned as a possibility by either GasNet or the ACCC.

In the case of the Latrobe Zone Tariff D, for example, GasNet now claims that there is a reduced threat of bypass from Latrobe zone customers based on (GasNet's estimates of) revised construction costs. However, in section 11.7.1 of the GasNet Access Arrangement Submission dated 14 May 2007, GasNet has indicated that bypass in this region remains credible and accordingly has foreshadowed the potential need to approach the ACCC / AER within the AA3 period to re-impose the Prudent Discount arrangement should a bypass threat emerge. It is not clear exactly what GasNet is proposing, other than a "re-opening" should a "bypass threat" emerge – as a form of an "each-way bet" that seeks to protect GasNet's interests without consideration of the impact on major customers.

GasNet claims that, according to its New Tariff Model, the threat of bypass is significantly reduced, to a degree sufficient to enable withdrawal of the Prudent Discount. However, GasNet has not provided the cost models and revenue model(s) used to support this analysis. This approach lacks transparency and is inappropriate, to say the least, given the magnitude of the change and cost impacts on affected major gas users.

The EUAA considers that, commensurate with the advantages of being allocated a regulated revenue stream, GasNet should release publicly – but as a minimum to all affected customers – all models relevant to its application to the ACCC. This already occurs in electricity transmission and distribution reviews and the EUAA sees no reason why similar arrangements should not be followed with gas transmission businesses subject to access arrangements.

CAPITAL WORKS PROGRAM

The EUAA also notes that GasNet is proposing to undertake a significant capital works program in AA3. In particular, GasNet proposes substantial capital expenditure of \$334.08 million over AA3 that includes augmentation capex of \$245.9 million, refurbishment and upgrade capex of \$88.19 million and \$63.71 million on the Brooklyn Lara (Corio) pipeline. This is a substantial increase above both the forecast and actual capex for AA2.

As a general principle, the EUAA would like to be assured (and see evidence) that the costs of the additional capital works are borne by the users that cause, or benefit from, those capital works, and not by users that do not cause a need for, or benefit from, those capital works. Because the models and calculations that lie behind the determination of tariffs are not publicly available, the EUAA is not in a position to assess whether the 'user pays' principle has been fairly applied in determining proposed tariffs.

The EUAA considers that this concern adds further weight to the call for the capital works and tariff models to be released.

MANNER OF THE REVIEW

Major users have also indicated to us that the manner in which GasNet has engaged with industrial customers has been totally unsatisfactory. To date, as far as we are aware,

GasNet has not written to or discussed with any other major end user the proposed Access Arrangement. GasNet has not, to our understanding, provided any major end user with an opportunity to discuss gas supply (or alternative supply) issues. This has left at least one major user with limited time to pursue alternative energy supply options, relative to the introduction of the increased tariffs. Clearly, this makes affected end users more susceptible to 'capture' by GasNet.

The EUAA considers that GasNet, with knowledge of the effects of its revised tariff model on major industrial end users, should have engaged with these end users in a commercially open, transparent and honest manner in exactly the same way that would be expected for any other supplier of its major customer.

WHAT THE EUAA IS SEEKING

As a result of discussions with GasNet, our membership and the ACCC / AER, the EUAA considers that:

- End users affected by the Prudent Discount issue should be given access to the tariff models, cost models and assumptions that have been used by GasNet to conclude that the Prudent Discount offered in respect of the La Trobe zone is no longer applicable.
- In assisting the ACCC / AER to reach a decision on whether the conditions under 8.43 of the Gas Code have been met, relevant stakeholders should be allowed to make a submission on whether a Prudent Discount should be allowed in respect of any particular service, consequent on receiving the models and information specified above; and
- As appropriate, the AER / ACCC should issue formal guidelines for the assessment of Prudent Discount issues so that this issue is determined in a reasonable, fair and transparent way should future Prudent Discount issues need to be resolved

As a matter of record, we also believe that GasNet needs to engage more with major end users to explain its proposals, demonstrate their soundness and ensure that GasNet is able to understand the impact of its proposals on its customers – and the options available to those customers. It would be helpful if the ACCC / AER made this known to GasNet.

Please contact Mr Jeremy Romanes, Manager - Policy & Regulation (on 03 9898 3900 and/or jeremy.romanes@euaa.com.au) if you have any questions or comments regarding this submission or any other related matters.

Yours sincerely



Roman Domanski
Executive Director