

Issues Paper



Revisions lodged by GasNet Australia (Operations) Pty Ltd for the Victorian Principal Transmission System

24 May 2007



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Abbreviations and glossary

AA1	the access arrangement approved in 1998 at which the initial capital base was set
AA2	the first scheduled revision of AA1 covering the period 2003–07
AA3	the second scheduled revision of AA1 proposed to cover the period 2008–12
ACCC	Australian Competition and Consumer Commission
access arrangement	an arrangement for third party access to a covered pipeline provided by a service provider and approved by the relevant regulator in accordance with the Code
access arrangement information	information provided by a service provider to the relevant regulator pursuant to section 2 of the Code
access arrangement period	the period from when an access arrangement or revisions to an access arrangement takes effect (by virtue of a decision pursuant to section 2) until the next revisions commencement date
AER	Australian Energy Regulator
AMDQ	authorised maximum daily quantity
APA Group	APA Group includes Australian Pipeline Trust, Australian Pipeline Ltd and APT Investment Trust
CAPM	Capital Asset Pricing Model
Code	National Third Party Access Code for Natural Gas Pipeline Systems
covered pipeline	a pipeline to which the provisions of the Code apply
CGS	Commonwealth Government securities
CPI	Consumer Price Index
DPI	Victorian Department of Primary Industries
GasNet	GasNet Australia (Operations) Pty Ltd
GJ	gigajoule (one thousand million joules)

GNS	GasNet System, also referred to as Principal Transmission System (PTS)
IDC	interest during construction
km	kilometre
linepack	refers to the amount of gas in a pipeline. Linepack is a function of pipeline size (length and diameter) and pressure
LNG	Liquefied Natural Gas
MSO Rules	Market System and Operational Rules
MVP	Murray Valley Pipeline
NPV	net present value
PJ	petajoule (one thousand terajoules)
PTS	Principal Transmission System, also referred to as the GasNet System
queuing policy	a policy for determining the priority that a prospective user has, as against any other prospective user, to obtain access to spare capacity
RBA	Reserve Bank of Australia
reference service	a service which is specified in an access arrangement and in respect of which a reference tariff has been specified in that access arrangement
reference tariff	a tariff specified in an access arrangement as corresponding to a reference service.
reference tariff policy	a policy describing the principles that are to be used to determine a reference tariff
SEA	service envelope agreement between GasNet and VENCORP
service provider	a person who is the owner or operator of the whole or any part of the pipeline or proposed pipeline
SWP	South-west pipeline
SWZ	system withdrawal zones

TJ	terajoule (one thousand gigajoules)
tariff D	users with consumption greater than 10,000 GJ per annum or a maximum hourly demand greater than 10 GJ
tariff V	users with consumption less than 10,000 GJ per annum
VENCorp	Victorian Energy Networks Corporation
WACC	weighted average cost of capital

Summary

Access arrangements for GasNet Australia (Operations) Pty Ltd (GasNet) and the Victorian Energy Networks Corporation (VENCorp) were first approved by the Australian Competition and Consumer Commission (ACCC) in 1998 (referred to as AA1). The ACCC subsequently approved revisions to AA1 in 2003 from 1 January 2003 to 31 December 2007 (referred to as AA2).

GasNet lodged substantial revisions documents with the ACCC on 30 April 2007, inclusive of a proposed access arrangement and related information (accompanied with an access arrangement submission) to cover the period 1 January 2008 to 31 December 2012 (referred to as AA3). The purpose of this issues paper is to highlight a number of issues to facilitate public consultation as part of the ACCC's assessment of GasNet's proposed access arrangement.

The issues paper does not attempt to replicate, and should be read in conjunction with, GasNet's proposed access arrangement and supporting information. Submissions to this issues paper close Friday 29 June 2007.

Key features of GasNet's proposal

- 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.¹ This is a significant increase from AA2.
- Substantial increases in operating expenditure as a result of its proposed capital program over AA3 and anticipated business scope changes.
- A real increase in its average tariff between 2007 and 2008 of approximately 30 per cent and a real tariff increase of 11.6 per cent over AA3.
- Modifications to the average revenue yield tariff control to limit GasNet's exposure to volume risk.
- The introduction of a single postage stamp tariff for all tariff V (small) users and the removal of specific asset group costs from tariff zones for tariff D (large) users.
- The introduction of new withdrawal zones for tariff D users and the removal of a number of prudent discounts.
- Injection tariffs levied on actual volumes injected during the winter period (currently it is levied on the ten peak injection days over the winter period).

¹ In June 2006 in accordance with s. 8.21 of the Code, the ACCC approved the Corio Loop to be included as forecast capex in AA3. The Corio Loop satisfied s. 8.16 of the Code for inclusion in GasNet's capital base. The ACCC will include the Corio Loop in the capital base for AA3 subject to the costs of the project being less than the approved amount and the project undertaken is the same as the approved project: see ACCC, *Final Decision: Major System Augmentation—Corio Loop*, June 2006.

- GasNet proposes to have the discretion on whether an expansion at Culcain for withdrawals above the current capacity of 17 TJ/day in AMDQ is to be covered by the access arrangement.

The issues paper

The ACCC has released this issues paper to guide interested parties in preparing submissions to assist the ACCC in its assessment of GasNet's proposed revised access arrangement. It contains and outlines:

- how to make a submission
- background, scope and issues for assessment
- key matters on which the ACCC seeks comment, information and supporting evidence.

This issues paper identifies a number of issues relevant to the ACCC's assessment of the proposed revised access arrangement. It is not intended to be exhaustive or to replicate the proposals by GasNet Australia (Operations) Pty Limited. This issues paper should be read in conjunction with the GasNet's proposed access arrangement, access arrangement information and supporting information.

Key inquiry dates

Provision of revised access arrangements	30 April 2007
Release of issues paper	28 May 2007
Due date for submissions	29 June 2007
Draft decision	September 2007
Due date for submissions on the draft decision	October 2007
Final decision	December 2007

If you wish to obtain a hard copy of this issues paper or to be notified of developments concerning the ACCC's assessment of GasNet's proposed access arrangement, please phone (03) 9290 1436; fax (03) 9290 1457; or email gns@acc.gov.au.

Any other inquiries should be directed to Blair Burkitt, Director, Network Regulation South Branch on (03) 9290 1442.

How to make a submission

Interested parties are invited to make submissions to the ACCC on any issues raised by this paper, or any other issues they consider relevant, by 29 June 2007. The ACCC is not obliged to consider submissions received after this date.

Interested parties are not restricted to comment only on matters raised in this issues paper. Any information which interested parties consider relevant to this assessment will be considered by the ACCC. Copies of the proposed revised access arrangement, access arrangement information and supporting information are available on the Australian Energy Regulator's (AER) website at www.aer.gov.au.²

After considering these submissions, the ACCC will issue its Draft Decision. Following consideration of further submissions, and any amendments to the proposed revised access arrangement, the ACCC will issue its Final Decision.

All public submissions received will be placed on the AER website and the public register held by the Code Registrar. Any information considered to be of a confidential nature should be clearly marked as such, and the reasons for seeking confidentiality be provided. The ACCC will not disclose confidential information where it is of the opinion that undue harm or prejudice is likely to result to the legitimate business interests of a user or service provider.

Submissions should be supplied in electronic format compatible with Microsoft Word to the e-mail address gns@acc.gov.au.

In addition, one original signed document together with a completed submission cover sheet should be mailed to the address below.

Mr Chris Pattas
General Manager
Network Regulation South Branch
Australian Competition and Consumer Commission
GPO Box 520
Melbourne VIC 3001

² The enabling legislation to transfer the ACCC's current functions under the Code to the AER has yet to be enacted. For administrative simplicity, all ACCC documents relating to its functions under the Code are available on the AER website.



Submission cover sheet

Please complete and submit this form with your submission to:

Mr Chris Pattas
General Manager
Network Regulation South Branch
Australian Competition and Consumer Commission
GPO Box 520
Melbourne VIC 3001

Organisation:.....

Street address:.....

Suburb/City..... **State & Postcode**.....

Postal address.....

Suburb/City..... **State & Postcode**.....

Principal contact..... **Phone**.....

Position..... **Fax:**.....

Email address:..... **Mobile**.....

Please indicate if your submission:

- contains NO confidential material
- contains SOME confidential material (clearly marked and provided under a separate submission cover sheet)
- contains confidential material and the whole submission is provided 'IN CONFIDENCE'

1 Introduction

1.1 Background

This assessment is the second scheduled review by the ACCC under the *National Third Party Access Code for Natural Gas Pipelines* (the Code) of GasNet Australia (Operations) Pty Ltd's (GasNet) access arrangement initially approved in 1998.

The purpose of this issues paper is to outline the access arrangement assessment for GasNet and to highlight a number of issues to facilitate public consultation. This issues paper is to be read in conjunction with the proposed access arrangement, access arrangement information and supporting information provided by GasNet (refer to www.aer.gov.au).

1.2 The Principal Transmission System

The Principal Transmission System (PTS) (also known as the GasNet system) is the primary system for the transmission of natural gas at high pressure in Victoria. For the purpose of tariff recovery, the PTS comprises of gas injection pipeline assets and gas withdrawal pipeline assets. Injection tariffs are charged for the costs attached to usage of injection pipeline assets. Withdrawal tariffs recover the costs attached to usage of the system for transmission of gas from injection pipelines to users, i.e. primarily those costs incurred in the usage of withdrawal pipelines. In some tariff zones, users receive a discount for withdrawing off an injection pipeline prior to the gas using all the pipeline and then entering into the withdrawal pipeline system. The main injection and withdrawal pipelines are shown in figure 1.1.

The PTS is not a traditional point to point transmission pipeline as there are a number of injection points. As set out in GasNet's submission, the PTS has the following five main injection zones:

- Longford, comprising injection points at the site of the ESSO/BHP Billiton processing facility; VicHub (the interconnection with the Eastern Gas Pipeline);
- Culcairn, the NSW interconnection with the Moomba-Sydney gas pipeline system;
- Port Campbell, comprising the injection point for the Western Underground Gas Storage facility and local fields; an interconnection with the SeaGas Pipeline and Minverva processing facility;
- Dandenong, the site of the LNG facility; and
- Pakenham injections, for gas sourced from the Yolla gas field.

Since the start of AA2 there has been an increase in the number of injection points. This coincides with an observable reduction in the reliance on Longford injections and the development of new gas fields and new gas production facilities.

Table 1.1 sets out the change in gas sources for the PTS between 2003 and 2006.

Table 1.1: Gas sources for the PTS (PJ)

Period	Source of gas supply						
	Longford	VicHub	BassGas ^a	Iona	SeaGas ^b	Culcairn	Dandenong LNG Facility
Sep 02– Sep 03	89.9%	4.3%	n/a	5.8%	n/a	–0.2% ^c	0.1%
Sep 05– Sep 06	84.9%	4.4%	1.4%	5.8%	3.5%	0.9%	0.1%

Source: VENCORP, *Gas Annual Planning Report 2006*, section 2.4; VENCORP, *Gas Annual Planning Report 2004*, p. 13.

^a BassGas was commissioned in June 2006.

^b SeaGas was commissioned in January 2004.

^c The negative injection percentage reveals a greater amount of gas withdrawn (exported) from the PTS than injected into the PTS from the connected Moomba to Sydney Pipeline.

Whilst Longford injections remain the primary source of gas, supplies from other sources are increasing over time. GasNet forecasts this trend of gas supply, which places less reliance on the Longford injection zone, to continue in AA3.

Gas injected into the PTS is primarily delivered into Victoria’s gas distribution system, however some large customers are directly connected to the transmission network. A small amount of gas injected into the PTS is exported out of the system to:

- the separately owned Carisbrook to Horsham pipeline transmission pipeline in Victoria;
- South Australia via the SeaGas pipeline; and
- NSW via Culcairn and the VicHub.

The PTS provides, along with distribution pipelines, a large part of the infrastructure necessary to facilitate both wholesale and retail competition in natural gas. As table 1.1 details, gas is increasingly sourced from a variety of fields. Diversity of ownership within these fields has been increasing along with the diversity of retail offerings to customers. The ACCC’s final decision and access pricing decisions on the PTS must be sensitive to potential impacts on competition in both the wholesale and retail gas market.

1.3 Allocation of responsibilities between GasNet and VENCORP

Under the Code, both GasNet and VENCORP are service providers (for AA1 and AA2). Their access arrangements allocate responsibility between them for complying with the obligations imposed by the Code.

Under the market carriage capacity management system operating in Victoria, users currently pay tariffs to both the system owner, GasNet, and the independent system operator, VENCORP. GasNet as the owner of the PTS is responsible for the extensions and expansions policy (s. 3.16 of the Code) and VENCORP is responsible for the

queuing policy (ss. 3.12–3.15). VENCorp’s obligations in respect of queuing are contained in the *Market System and Operational Rules* (MSO Rules) under the *Gas Industry Act 2001* (Vic).

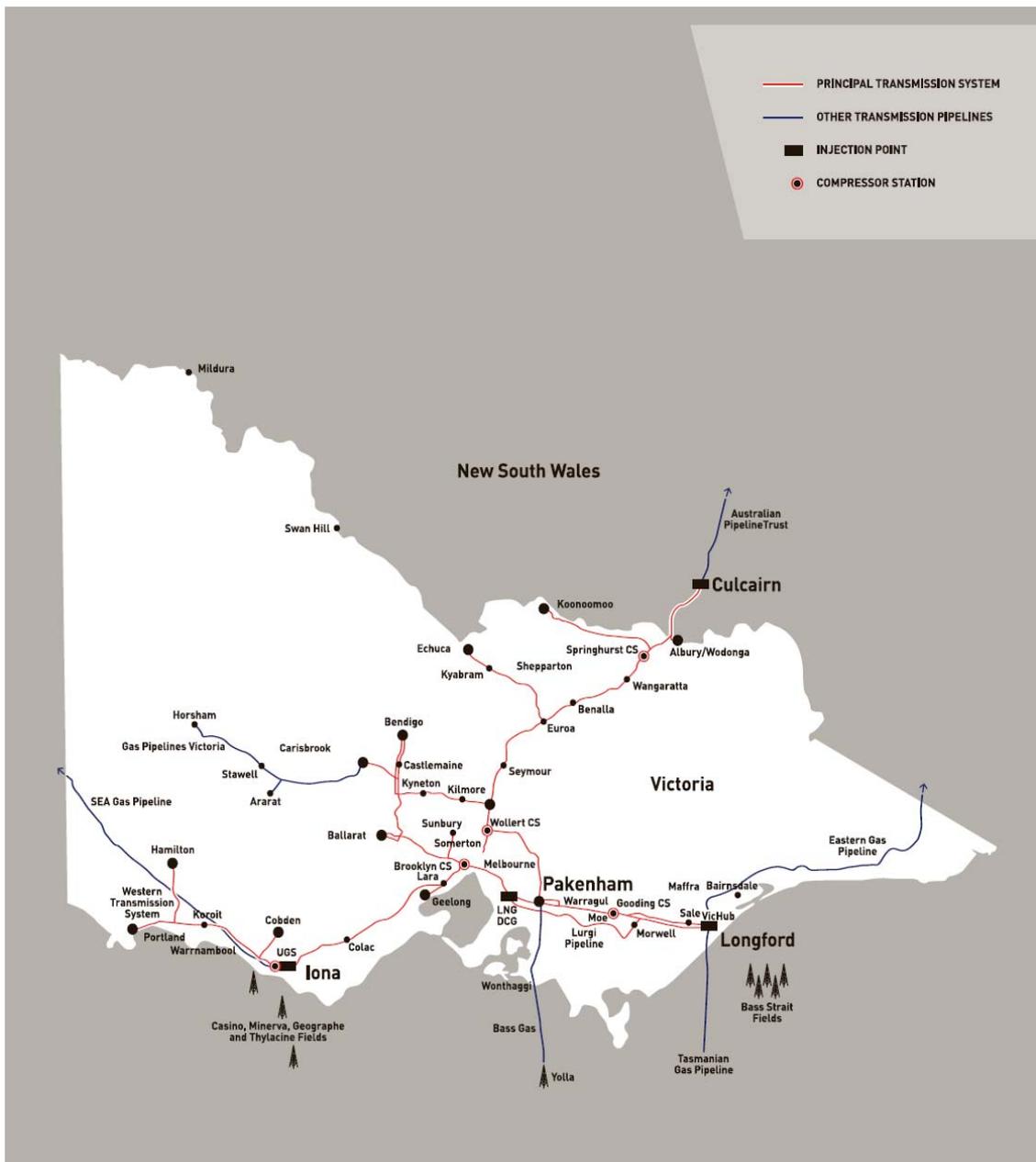
The Victorian Government has accepted the recommendations of a statutory review of VENCorp’s functions that VENCorp no longer be required to submit an access arrangement under the national gas access regime. In its place, the review recommended VENCorp’s costs and revenues be regulated on an annual basis by the AER under explicit provisions in the National Gas Law when it is enacted.

Under the Victorian Government’s proposals, VENCorp’s obligations in respect of the queuing policy for the PTS will remain under the MSO Rules. It is expected that the rule making functions in respect of the MSO Rules will transfer to the Australian Energy Market Commission.

Under the existing regulatory arrangements, GasNet makes the PTS available to allow VENCorp to operate the pipeline. VENCorp has a direct relationship with, and enters into gas transportation deeds with, the users of the PTS. The Victorian Minister for Energy has indicated that if necessary legislation will be introduced so VENCorp is no longer an intermediary between GasNet and the users of GasNet’s transportation service. Instead, there will be a direct contractual relationship between GasNet and pipeline users.

VENCorp requested an extension of its revisions submissions date on the basis that the AER will approve the costs and revenues of VENCorp’s reference services under the new regulatory arrangements. The ACCC approved this extension request on 28 March 2007. Accordingly, this issues paper only covers GasNet’s proposed revisions and the processes for approving GasNet’s revised access arrangement.

Figure 1.1: Map of the Principal Transmission System



Source: VENCORP, *Gas Annual Planning Report 2006*.

2 Key issues in GasNet’s proposed revised access arrangement

2.1 Demand and supply forecasts

As contemplated under the Code, GasNet has chosen to base its total revenue and reference tariffs on the basis of forecast demand and supply volumes. Forecast volumes will be critical to GasNet’s overall revenue recovery and the apportionment of that recovery across pricing zones and across tariff D and tariff V users. The accuracy of demand forecasts is particularly important to GasNet given its proposed Reference Tariff Control Formula Approach. Under this proposed formula, deviations in actual volumes from above (below) forecast, which are not associated with EDD related weather risk will allow GasNet to recover additional revenue (less revenue) during AA3. This may provide an incentive to GasNet to submit biased forecasts (i.e. low forecasts). Significantly, since GasNet propose to adopt VENCORP’s medium economic growth scenario demand forecasts and also its Gas Powered Generation forecasts, the accuracy of these forecasts will be crucial as to whether GasNet recovers more or less revenue under its proposed average revenue control. GasNet proposes the following forecasts for AA3.

Demand forecasts

GasNet’s proposes to base its peak and annual demand forecasts on the medium economic growth scenario forecasts in VENCORP’s *2006 Gas Annual Planning Report*. However, GasNet proposes a number of adjustments to VENCORP’s forecasts. The adjustments GasNet includes to support its tariff setting approach are outlined in table 2.1. The table sets out GasNet’s annual and peak demand forecasts.

Table 2.1: Annual and peak demand forecasts

	2008	2009	2010	2011	2012 ^(a)
<i>Annual (PJ)</i>					
VENCORP	219.2	219.6	220.7	221.8	224.1
Inclusive of gas generator component	6.8	6.8	6.7	6.8	6.8
Less notional compressor fuel	-0.4	-0.4	-0.4	-0.4	-0.4
Culcairn Export	2.5	3.8	5.0	5.0	5.0
VicHub Export	0.3	0.3	0.3	0.3	0.3
WUGS/LNG refill	0.8	0.8	0.8	0.8	0.8
Total	222.5	224.1	226.5	227.6	229.9
<i>Peak (GJ)</i>					
VENCORP(exclusive of GPG)	1168	1174	1183	1192	1205
GPG forecast	50	50	50	50	50
Less notional compressor fuel	-4	-4	-4	-4	-4
Culcairn Export	17	17	17	17	17
VicHub Export	1	1	1	1	1
WUGS/LNG refill	0	0	0	0	0
Total	1233	1239	1248	1256	1270

Source: GasNet, *Access Arrangement 2008–12 Submission*, p. 87

(a) GasNet have included 2012 forecasts in its AA which incorporate further additional volume forecasts supplied by VENCORP.

(a) *VENCorp forecasts*

These annual withdrawal forecast volumes are supported by assumptions in VENCORP's forecast as to the annual effective degree days (EDD) for the 2007-2011 planning period³. Notably, GasNet proposes to accept VENCORP's volumes on the basis of a constant EDD of 1,340 over AA3⁴. For AA2, the ACCC approved an annual declining EDD value. GasNet has also chosen to use VENCORP's 1 in 2 peak day volume forecasts.⁵

VENCORP's annual volume forecasts are based on an inclining temperature sensitivity (TJ/EDD) forecast over the period. This implies that the effect of a change in the EDD will have an increasingly larger effect on total gas usage into the future, consistent with the assumption that base gas usage will increase over time, as reflected in table 2.2.

Table 2.2: VENCORP annual volume forecasts

	2007	2008	2009	2010	2011
Medium economic growth scenario forecast volumes (TJ)	217.2	219.2	219.6	220.7	221.8
Number of EDDs	1340	1340	1340	1340	1340
EDD sensitivity, EDD/TJ	44.5	44.8	45.2	45.5	45.9

Source: VENCORP, *Gas Annual Planning Report 2006*.

(b) *Gas-fired power generator (GPG) forecasts*

GasNet has adopted VENCORP's annual GPG forecasts. GPG demand has shown significant variability over the last few years: over 12 PJ in 2004, 11 PJ in 2005 and around 6 PJ in 2006. The ACCC observes that to date GPG volumes for 2007 are in the order of 12 PJ, in comparison to less than 7 PJ for the whole of 2006.⁶ A significant factor behind this divergence is understood to be the drought and reduction in hydro-electric generation.⁷

³ See VENCORP, *Review of the Effective Degree Day Weather Standards: Final Report*, September 2006.

⁴ *ibid.* The yearly forecast of the number of EDDs (1340) represents a forecast of the likely coldness of weather over the year. For each day of the year an actual positive EDD figure will be recorded when weather conditions are such that the temperature recorded falls below a threshold level of 'coldness'. VENCORP notes the precise calculation and the temperature of 18 degrees within the formula represents a threshold for residential gas heating which is a fairly common standard internationally.

⁵ VENCORP, *Gas Annual Planning Report 2006*, Appendix A. Appendix A sets out the assumptions behind annual and peak injection forecasts.

⁶ VENCORP, *Gas Annual Planning Report 2006*, p. 6. VENCORP measures GPG usage yearly from October to September each year.

⁷ See VENCORP, *Gas Annual Planning Report 2006*, p. 11 for other assumptions underpinning GPG forecasts into the future including, increased supply from Basslink and wind farms.

GasNet has provided its own GPG peak day forecast of 50 TJ/day over the period. The access arrangement submission submits this forecast is based on historical analysis and previous statements from VENCORP.⁸

(c) *Culcairn*⁹

GasNet projects Culcairn volumes to increase during AA3 from 2.5 PJ in 2008 to 5 PJ in 2012. However, these forecasts depend on the:

- proposal to discount the export tariff on the basis that there are competing pipelines and that the proposed tariff still exceeds the long run incremental costs of supply;
- proposed capital expenditure for the Northern zone;¹⁰
- the volume of imports through the Interconnect; and
- any associated operating condition restrictions.

In relation to the operating conditions VENCORP notes in its *Gas Annual Planning Report 2006* (2006 Gas APR) that under existing pipeline operation boundaries, export operations have limited flexibility when there is a need to switch from imports to exports on a daily basis or within-day basis. It states that import to export mode changes require advanced planning of a day or more, providing time for adequate pressurization to enable exports.¹¹

Supply forecasts

GasNet submits there are no independent sources of information for injection volume forecasts. However, GasNet has used historical VENCORP monthly data as a basis for forecast winter four month volumes at each injection zone across AA3. Table 2.3 sets out GasNet’s proposed injection forecasts.

Table 2.3: Injection forecasts

	2008	2009	2010	2011	2012
<i>Annual (PJ)</i>					
a. Longford	150	150	150	150	150
b. Port Campbell	49.2	51.8	55.2	56.7	59
c. Culcairn	3.0	2.0	1.0	0.5	0.5
d. Pakenham	20	20	20	20	20
e. Dandenong	0.3	0.3	0.3	0.3	0.3
Total	222.5	224.1	226.5	227.6	229.9
<i>Winter 4 month (PJ)</i>					

⁸ *ibid.*

⁹ VENCORP does not forecast these volumes for the purpose of its planning report, whereas GasNet forecasts these volumes as it recovers part of its system costs through tariffs over these volumes.

¹⁰ The ACCC understands that other forecasts may be based on the assumption of an approval of its proposed forecast capital expenditure over AA3.

¹¹ VENCORP, *Gas Annual Planning Report 2006*, p. 34.

a. Longford	66	66	66	66	66
b. Port Campbell	25.7	27.1	28.9	29.7	30.9
c. Culcairn	2.4	1.6	0.8	0.4	0.4
d. Pakenham	7	7	7	7	7
Total	101.1	101.7	102.7	103.1	104.3
<i>Peak (TJ)</i>					
a. Longford	830	830	830	830	830
b. Port Campbell	272	289	303	315	328
c. Culcairn	34	23	18	15	15
d. Pakenham	67	67	67	67	67
e. Dandenong	30	30	30	30	30
Total	1223	1239	1248	1256	1270

Source: GasNet, *Access Arrangement 2008–12 Submission*, pp. 89, 90.

(a) *Longford and Port Campbell*

GasNet forecasts significant increases in all injection flows (annual, peak and winter) from Port Campbell for AA3 as compared to AA2.

The ACCC understands GasNet’s injection forecasts are in part based around general industry information as to the likely gas availability from various competitors producing and sourcing gas in the Gippsland and Otway basins. In addition to commercial conditions, however, GasNet’s gas injection forecasts also appear to be particularly sensitive to actual operating conditions imposed. That is, particularly for peak injection forecasts, consideration must be given to the likely manner in which the system will be operated. VENCORP discusses in the 2006 Gas APR that upon the completion of the Corio Loop (anticipated for April 2008):

- injections would increase to 307 TJ/d on the basis of the lower operating boundary consistent with lower operating pressures on the pipeline to take account of PTS operational issues; however
- it also notes a maximum modelled injection volume at Iona of 347 TJ/d based on an assumption of pressures up to the pipeline’s maximum allowable operating pressure of 10,000 kPa.¹²

GasNet’s forecasts for 2011 and 2012 fall between these figures of 307 TJ/d and 347 TJ/d.

However, GasNet is proposing a Stonehaven augmentation (to be commissioned in 2012 as discussed in section 2.13 of this issues paper), which if built would likely lift the operational capacity of the SWP above GasNet’s forecast peak volumes for 2012.¹³

¹² See VENCORP, *Gas Annual Planning Report 2006*, chs. 4 and 5.

¹³ See VENCORP’s Network Planning Report on Stonehaven.

(b) *Culcairn*

GasNet forecasts that as export volumes increase and gas trading activity increases, Culcairn hub injection volumes will fall (for both annual and peak). GasNet's forecasts of import volumes are sensitive to assumptions underpinning its forecasts of export volumes as discussed above.

(c) *Pakenham and Dandenong*

GasNet forecasts the annual supply from Pakenham and Dandenong of 20 PJ via BassGas, which appears to be consistent with the VENCORP's 2006 GAPR. GasNet proposes an annual injection volume from Dandenong which is marginally higher than historical averages.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- the demand forecasts GasNet proposes are reasonable for the determination of reference tariffs and revenues, in particular for:
 - annual volume forecasts;
 - peak volume forecasts;
 - GPG forecasts;
 - compressor fuel forecasts; and
 - export and refill forecasts.
- the supply assumptions and forecasts for each injection source (annual, winter and peak) for the proposed access arrangement period are reasonable;
- the assumptions of a constant EDD of 1,340 and increasing EDD/TJ sensitivity over AA3 are reasonable.

2.2 Services policy

As required by the Code, an access arrangement must include a services policy which describes one or more services that the service provider will make available to users and prospective users. The policy must contain one or more services likely to be sought by a significant part of the market (a reference service) and any service or services that, in the regulator's opinion, should be included in the services policy.

GasNet proposes the same services policy as in AA2. In particular, GasNet proposes a single reference service to make the PTS available to VENCORP on the same terms as those set out in the Service Envelope Agreement (SEA)¹⁴. Under this arrangement

¹⁴ The SEA is available on the AER's, VENCORP's and GasNet's websites.

VENCorp enters into Gas Transportation Deeds with users which direct users to pay GasNet directly for the gas transportation service. The service GasNet proposes is to make the PTS available to VENCorp to provide for gas transportation services.

GasNet proposes a services policy which reflects its existing policy in its access arrangement. As discussed in section 1.3 of this issues paper, the ACCC understands the Victorian Government will amend the relevant code and legislative provisions to remove VENCorp's obligation to submit a revised access arrangement under the code. The Victorian Government has advised that as VENCorp will not be required to submit a revised access arrangement, users will be required to enter into bilateral contracts for the gas transportation service with GasNet instead of VENCorp. Under these new arrangements, GasNet will provide gas transportation service directly to users as well as making the PTS available to VENCorp. As a result, GasNet's proposed services policy for AA3 may not reflect the relationship between VENCorp and GasNet recently foreshadowed by the Victorian Government.

At this stage there is still some uncertainty about the specific provisions that will apply under the amended Victorian legislation to in relation to arrangements between VENCorp and GasNet. GasNet has therefore not as yet made modifications to its services policy to reflect the proposed new arrangements. The ACCC will review GasNet's proposed services policy in the context of any changes to the relationship between GasNet and users following the introduction of Victorian legislation.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- GasNet's proposed reference service will meet users' anticipated needs during AA3;
- there are any other services likely to be sought by a significant segment of market participants that should be included in the services policy;
- there are any issues in terms GasNet's proposed services policy resulting from the Victorian Government's proposals to require GasNet to provide the gas transportation service directly to users.

2.3 Reference tariffs

GasNet proposes around a 30 per cent increase in its real average tariff between 2007 and 2008—the first year of AA3. GasNet also proposes a real increase in its average tariff of 11.6 per cent over AA3.

GasNet submits, however, that the current reference tariffs are approximately 15.5 per cent below the level that would have applied had the forecast tariff path under AA2

been followed. GasNet comments that this was a result of the delay in Yolla gas coming on-stream and the consequential effect on its revenue control model¹⁵.

Tariff structure

GasNet proposes a separate injection tariff for each of its four injection points levied on actual volumes injected during the winter period June to September (currently it is levied on the ten peak injection days over the winter period at each injection point). The matched injection tariffs will be maintained but levied on actual volumes during the winter period.

GasNet will continue to charge withdrawal tariffs on the basis of actual annual gas withdrawals and to maintain V and D tariff classes. However, GasNet proposes to remove its withdrawal zones for its less than 10TJ per annum tariff V users (currently there are 16 withdrawal zones) and apply a single postage stamp tariff to all tariff V users. This means that tariff V users will pay the same tariff regardless of their location and usage.

Withdrawal zones for tariff D users (greater than 10TJ/annum or a maximum hourly demand greater than 10GJ) are maintained, but with the addition of a proposed new Geelong zone and the separation of Warrnambool and Koroit as separate withdrawal zones from the current Western Zone. This results in 19 withdrawal zones for tariff D users compared to the current 16 withdrawal zones.

Proposed cost allocation and tariff setting

(a) Withdrawal tariffs

GasNet has proposed significant changes to its tariff formulation and associated cost allocation approach in its AA3 application. To better understand these changes, it is useful to first outline the approach approved by the ACCC in its previous (AA2) decision.

In GasNet's AA2, the direct capital costs (return on and return of capital) associated with pipeline, regulator and compressor assets are apportioned among 28 pipeline segments (asset groups) based on the optimised replacement cost of the assets within the asset group. Asset groups are defined by the physical characteristics of the pipeline (i.e. pipeline diameter, looping).

¹⁵ Under GasNet's revenue control model, GasNet is allowed to earn a maximum average tariff per annum. (Under this type of control actual volume mix, rather than total volume is the important influence. Total actual volume may be less than forecast in one year and hence less total revenue is earned than anticipated, but the actual volume mix between tariff zones and tariff V and D may result in a higher average return per GJ). The delay in Yolla gas coming on-stream meant that less gas than anticipated was injected at Pakenham and consequentially more gas injected on other pipelines with higher injection tariffs. This change in volume mix produced a higher actual average tariff than allowed under GasNet's revenue control model and meant that over the period GasNet was required to reduce its tariffs in order to achieve the allowed average tariff (average tariff per GJ).

Direct operating costs are allocated to each asset group according to the pipeline length and whether the pipeline is located in a metropolitan or rural area. Direct operating costs associated with city gates, regulators and compressors are allocated directly to the relevant asset group. Indirect operating costs are allocated on a postage stamp basis (i.e. a set amount per gigajoule transported).

To assign direct costs (capital and operating) to tariff zones, GasNet calculates an annual and a peak \$/TJ-km unit rate for each of the asset groups and uses this to assign direct costs first to each off-take based on the flow of gas from injection point to withdrawal off-take and then, by grouping the off-takes, to each tariff zone. 45 per cent of direct costs is allocated according to peak flows and 55 per cent according to annual flows.

The zonal tariffs are found by summing the cost allocations for each off-take in the zone and then dividing by the total volume withdrawn by each off-take in the zone. The average of the costs for all meters for both V and D volumes within a tariff zone represents the charge against direct costs at the zonal level. GasNet defines its tariff zones by grouping off-takes to achieve a balancing between tariffs and to maintain cost reflectivity. Some tariff zones have been particularly defined to avoid the threat of bypass.

As a result of GasNet's current cost allocation procedure, the direct capital cost component of the tariff zones depends on the distance from the injection source and the consequent cost allocated to each asset group through which gas flows to the off-take (i.e. the direction of gas flow) and the volume utilisation.

For AA3 GasNet proposes to retain the current allocation of indirect costs on a postage stamp basis, but to replace the cost allocation methodology for direct costs. The proposed changes include:

- direct capital and operating costs will no longer be allocated to individual asset groups, as per the existing general cost allocation methodology, to calculate peak and annual \$/TJ-km direct cost unit rates for each asset group;
- a single system wide average peak and average annual \$/TJ-km unit rates will be applied to all asset groups; and
- to calculate the average peak and annual unit rates, 65 per cent of direct costs is averaged according to peak volumes and 35 per cent according to annual volumes.

For withdrawal tariff D users, GasNet proposes that the system wide average direct cost unit rate is used to assign direct costs to withdrawal pricing zones based on the volume-distance from injection source to withdrawal zone. This proposed cost allocation methodology for AA3 has the effect of removing specific asset group costs from the tariff zones, and makes volume-distance from injection point to withdrawal off-take the only influence on the final zonal tariff for D users.

For withdrawal tariff V users, GasNet proposes the removal of all tariff pricing zones. To achieve this GasNet aggregates its zonal tariffs to a single average tariff to apply across all zones. Accordingly, GasNet's proposed cost allocation methodology removes

the volume-distance effect on the tariff for V users as all users are levied the same tariff. GasNet submits that a simple tariff structure for V users will promote retail gas competition which outweighs the relatively small economic efficiency benefits of a complex zonal tariff structure for tariff V users. GasNet also submits that most retailers amalgamate the PTS transmission pricing zones for the purposes of marketing gas in order to save administrative costs.

(b) *Injections tariffs*

To calculate final injection tariffs GasNet proposes to use an average peak and annual (\$/TJ-km) rate to allocate direct costs to the injection pipelines. These average rates are derived by allocating 35 per cent of direct costs on the basis of forecast annual flows and 65 per cent on the basis of forecast 1 in 2 peak flows. This cost allocation methodology differs from the current access arrangement where direct costs associated with a pipeline are assigned directly to the pipeline and tariffs are based 100 per cent on peak flows on the top 10 peak days.

In GasNet's proposed model, the direct cost to be recovered from each injection zone is calculated on the basis of distance of the injection pipeline and the average peak and annual \$/TJ-km direct cost unit rates. This process allows the direct costs to be allocated to each pipeline based on both the distance of the pipeline and the peak and annual flows of the pipeline (instead of assigning actual costs directly to the pipeline as is the case for AA2). Once the direct cost recoveries are allocated accordingly to each pipeline, GasNet is able to divide this cost recovery by the forecast winter volume (June to September) to obtain final injection tariffs. This change in methodology results in significantly reduced tariffs, but the respective tariff is applied over a longer peak period.

Matched injection rebates are calculated in the same manner for offtakes which do not use the full length of the injection pipeline and are proportional to the length of the pipeline not used.

GasNet's proposal reduces the influence of specific asset costs associated with each injection pipeline on the final injection tariffs. Under the proposed cost allocation methodology, the difference between tariffs for each injection pipeline is the result of the length of pipeline and the winter volumes associated with the pipeline only. The implication of GasNet's proposal is that any increase in capital expenditure associated with a particular injection pipeline will no longer be recovered directly by the associated injection tariff.

Other changes

(a) *New withdrawal zones*

GasNet proposes to introduce a new Geelong withdrawal zone for tariff D users by separating it from the current Metro zone. GasNet also proposes to separate Warrnambool and Koroit from the current Western Zone and to set the tariffs for these two zones at a lower level than the Western zone tariff instead of applying a prudent discount to the Western zone as was the case for AA2.

(b) *Peak and annual flows cost allocation*

In allocating costs to users there is a question of how usage is defined. Under its current access arrangement GasNet defines peak injection flows as the top 10 peak injection days for each injection point during the winter period and allocates 100 per cent of the direct costs associated with each injection pipeline according to these peak flows. For AA3, GasNet proposes to allocate direct costs associated with injection pipelines such that 65 per cent of direct costs are allocated on the basis of 1 in 2 peak flows and 35 per cent on the basis of annual volume flows.

GasNet also proposes to change the allocation of direct costs associated with withdrawal assets such that 65 per cent of the direct costs will be allocated according to peak flows (currently 45 per cent) and 35 per cent allocated according to annual flows (currently 55 per cent).

GasNet's proposal of allocating 65 per cent of direct costs on the basis of peak usage and 35 per cent on the basis of annual usage associated with both injection and withdrawal assets is a change from 60 per cent of all direct costs being allocated according to peak usage in AA2¹⁶.

The implication of allocating more of the direct costs on the basis of peak flows, for withdrawal tariffs (65 instead of 45 per cent) is to change the relativities between tariff V and --tariff D. The allocation of more direct costs on the basis of peak flows will increase the tariff for tariff V users (and lower the tariff for tariff D users) because tariff V users tend to have peakier demand. However, by allocating 65 per cent of direct costs to injection assets on the basis of peak flows (instead of 100 per cent) the peak injection charge is reduced.

(c) *South-west pipeline*

GasNet proposes to revert to the standard real straight line depreciation profile for the South-west pipeline (SWP), instead of the partially deferred depreciation profile approved in AA2.

In AA2, the ACCC included 50 per cent of the SWP in GasNet's capital base in accordance with the economic feasibility test and 50 per cent under the system-wide benefits test under s. 8.16 of the Code. At the time the ACCC considered, in relation to the sustainability of charges on the SWP, tariffs on the SWP should be approximately 10 per cent higher than those on the Longford to Pakenham Pipeline.

Under GasNet's proposed methodology for allocating direct costs to pipelines based on average peak and annual \$/TJ-km unit rates means that 50 per cent of the costs associated with the SWP are averaged across all injection pipelines rather than allocated directly to the SWP as per the ACCC's 2002 decision. The result of GasNet's

¹⁶ In AA2 the effect of allocating 45 per cent of direct withdrawal asset costs on the basis of peak usage and 100 per cent of direct injection asset costs on peak usage resulted in 60 per cent of total direct costs being allocated on the basis of peak usage.

proposed methodology for injection pipelines is that the injection tariff for the SWP is now less than the injection tariff for the Longford to Pakenham pipeline.

(d) *Interconnect pipeline*

GasNet's proposed cost allocation methodology for calculating injection tariffs has implications for the ACCC's earlier decision to allocate part of the direct costs associated with the interconnect pipeline on a standalone basis and the rest on a system wide basis.

Other tariff elements

(a) *Matched withdrawals*

GasNet proposes to maintain its matched withdrawal tariffs for the northern zones (North Hume, Murray Valley, Interconnect and Wodonga) for injections from Culcairn and for the Metro South East zone for injections from Pakenham. However, GasNet proposes that this will be applied only to tariff D users for AA3.

(b) *Prudent discounts*

GasNet proposes in AA3 that:

- no prudent discounts be applied to tariff V users as a single tariff V is proposed for all V users;
- to remove prudent discounts for tariff D users in the Latrobe and Wodonga zones on the basis of a re-evaluation of bypass risk;
- a separation of the Western zone into two new withdrawal zones for tariff D users: Warrnambool and Koroit (negating the need for a prudent discount to apply in the Western zone); and
- to maintain a prudent discount for tariff D customers at Pakenham (the Pakenham bypass tariff is implemented as an injection tariff at Pakenham, determined as a proportion of the Longford Injection Tariff, pro-rated by distance from Pakenham to Dandenong, and a discounted withdrawal tariff in the Metro south east zone).

(c) *Murray Valley incremental tariff*

In AA2, the ACCC approved the inclusion of the Murray Valley pipeline (MVP) in GasNet's capital base on the basis that it satisfied the economic feasibility test under s. 8.16 of the Code. The economic feasibility test for part of the MVP imposes a requirement of the cost recovery to be on a stand alone basis. As a result, users of the MVP are charged a tariff that consists of two components. The first component recovers the cost of withdrawal pipeline usage up to Chiltern Valley, noting that a lower tariff applies for gas sourced from Culcairn (being closer to the Murray Valley) than for gas sourced from Longford. The second component the incremental tariff is designed to recover is the costs (stand alone costs) associated with the \$15.6 million MVP. In the current access arrangement the Murray Valley tariff is charged to both tariff V and tariff D users.

For AA3 GasNet proposes to remove the incremental component of the Murray Valley tariff and include the recovery of costs of the MVP across all users, consistent with its proposed general cost allocation methodology. As a result, the cost of the MVP is averaged across the system and is recovered from all tariff V and tariff D users.

(d) *Tariff recovery—Corio Loop*

The ACCC's 2006 decision approved the Corio Loop project under s. 8.16(a) of the Code on the basis that it is a prudent investment and satisfies the 'system-wide benefits test'. GasNet proposed that it would recover a portion of the Corio Loop costs from users of the Southwest Pipeline by maintaining the Southwest Pipeline tariff at the tariff that would prevail in the absence of the Loop. This portion of the recovery would be determined on the basis that the investment is expected to generate some additional revenue as a result of increased volume along the Southwest Pipeline. GasNet proposed that it expected to recover somewhere between 5 per cent and 10 per cent of the incremental costs of the Corio Loop directly from increased flows on the Southwest pipeline. The remainder of the costs would be recovered from PTS users through an uplift in the anytime tariff applying to all users. However, the ACCC indicated that the recovery of these costs and the tariff structure would be considered in the context of GasNet's revised access arrangements.

For AA3, GasNet proposes to allocate 100 per cent of the costs associated with Corio Loop under the system-wide benefits test. This means that all the costs associated with Corio Loop are to be recovered from all tariff V and tariff D users. The ACCC indicated that the recovery of these costs between users would be considered in the context of GasNet's revised access arrangements.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- GasNet's proposed changes are consistent with the tariff design principles in chapter 8 of the Code, including GasNet's proposal to levy a postage stamp tariff for V users;
- retailers presently amalgamate PTS transmission costs for the purpose of marketing gas in order to save administrative costs;
- GasNet's proposed tariff-V structure will:
 - lead to less administrative costs for retailers and the degree of any likely savings;
 - reduce 'barriers to entry' and encourage new entrants and small retailers to enter the market;
 - lead to consumer benefits from increased retail competition;

- the different usage characteristics of tariff D users and tariff V users justifies GasNet’s proposed separate cost allocation methodologies;
- the introduction of a new Geelong zone is appropriate;
- GasNet’s proposal to allocate costs on the basis of 65 per cent peak volume and 35 per cent annual volume is appropriate;
- GasNet’s proposed changes to the peak injection tariffs are likely to dampen peak pricing signals and reduce the efficiency and effectiveness of the tariff structure;
- GasNet’s proposed peak charging structure for injection tariff is consistent with where congestion is likely to be experienced on the system in the future;
- GasNet’s proposed removal of some prudent discounts on the basis that bypass risk has reduced;
- GasNet’s proposed tariffs enable users to better identify the cost impact of their usage decisions than the current arrangements. In particular, are peak pricing signals identifiable and would users respond to these signals;
- GasNet’s proposed changes to the cost allocation methodology for deriving the injection tariff for the SWP, and Interconnect and for the Murray Valley withdrawal Pipeline are appropriate;
- GasNet’s proposed recovery of the Corio Loop project costs across all tariff V and tariff D users is appropriate; and
- GasNet’s proposed recovery of augmentation expenditure on the basis of the Code’s system integrity test is consistent with its proposed tariffs for users.

2.4 Reference tariff methodology—modified revenue yield control

GasNet proposes to continue to set its revenue requirement in accordance with a cost of service approach where total revenue is calculated on the basis of a return on the capital base, depreciation of the capital base; and other operating, maintenance and non-capital costs incurred in providing the reference service.

Section 4.3 of GasNet’s proposed access arrangement states that transmission tariffs may vary on the basis of a Reference Tariff Control Formula Approach, consistent with s. 8.3 of the Code.

However, GasNet now proposes to remove the existing average revenue yield control and introduce a modified average revenue yield control. GasNet submits that these modifications will remove its exposure to weather related volume risk and retain an exposure to some economic risks on volumes. In contrast, under the average revenue yield control applying to AA2, GasNet has been exposed to volume risk and earns more (less) revenue where total actual volumes are more (less) than total forecast volumes.¹⁷

¹⁷ Under the average revenue control GasNet is not exposed to any differences in average revenue resulting from differences between forecast and actual product mix. Product mix refers to the balance of usage between Tariff V and Tariff D customers within zones, the balance between zones

For AA3, GasNet proposes an alternative control which it regards as a price path approach. Under this approach tariffs are determined for the initial year of the access arrangement and then move in accordance with the price control formula contained in Schedule 4 of GasNet’s proposed access arrangement. GasNet considers the use of an adjusted price path constitutes an incentive mechanism and exposes GasNet to cost risk and some limited volume risk.

As part of a risk sharing procedure between GasNet and users, the target revenues approved at the commencement of the access arrangement period will be adjusted up or down to reflect non EDD-related movements in gas withdrawals. That is, GasNet intends to bear no revenue risk due to deviations between forecast and actual volumes associated with differences between forecast and actual EDDs (certain types of weather risk).

GasNet submits that it will still be subject to volume risk in respect of variations in economic activity (eg. housing and construction demand) and energy efficiency activity. Additionally, however, the ACCC notes that other weather and environmental factors not related to EDD could impact on total volumes through the PTS. For example, there may be more GPG usage than forecast because of the continued drought and/or if there are higher than average temperatures for an extended period.

GasNet proposes that both positive and negative adjustments to target revenues received within the AA period will be limited by upper and lower bounds of 5.5 per cent. If actual (weather normalised) volumes are greater than target volumes in any given year, GasNet proposes a positive adjustment to revenue and vice versa if total actual (weather normalised) volumes are less than target revenue. In addition, these proposed revenue adjustments will be symmetrical in terms of any positive and negative adjustments for differences between target volumes and actual volumes.

Issues for consideration

The ACCC seeks comments and supporting evidence whether:

- the proposed changes to GasNet’s average revenue control tariff methodology (to reduce exposure to weather related risk) is appropriate;
- the proposed treatment of weather factors not related to EDD (i.e. adjustments for fuel gas volumes) and GPC volumes is appropriate.

and the balance between peak and anytime demand. A change (between forecast and actual) in the proportions of any of these categories will affect the average revenue achieved.

2.5 Terms and conditions

GasNet submits the terms and conditions on which it will offer its reference service are set out in the MSO Rules.

2.6 Extensions and expansions policy

Section 3.16 of the Code requires the extensions and expansions policy of an access arrangement to set out the method used to determine whether extensions and expansions will be treated as part of the covered pipeline and, if covered, how they will affect reference tariffs.

The extensions and expansions policy GasNet proposes is set out in section 5 of its proposed access arrangement. GasNet proposes to:

- continue the current arrangement whereby it is solely responsible for extensions and expansions on the PTS; and
- allow itself the discretion to decide whether an expansion at Culcairn for withdrawals above the current capacity of 17 TJ/day in AMDQ is to be covered by the access arrangement.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether it is appropriate for GasNet to have discretion over whether the expansion at Culcairn for withdrawals above 17 TJ/day should be covered.

2.7 Capacity management policy

GasNet proposes that the PTS continue to be a Market Carriage Pipeline under s. 3.7 of the Code as is the case for AA2.

2.8 Queuing policy

The purpose of a queuing policy is to deal with surplus demand and facilitate the timely provision of new capacity.

GasNet did not submit a queuing policy as VENCORP is responsible for the queuing policy for the PTS. GasNet refers to the MSOR in its proposed access arrangement as the queuing policy under which the PTS will be operated.

2.9 Opening capital base

Chapter 8 of the Code sets out a number of Reference Tariff Principles. The overarching requirement is that when reference tariffs are determined and reviewed, they should be based on the efficient cost (or anticipated efficient cost) of providing the Reference Services. GasNet proposes a cost of service approach as outlined below.

GasNet proposes to roll forward for AA3 its inflation-adjusted capital base at the start of AA2 by adding new facilities investment and subtracting forecast depreciation and redundant capital. Table 2.4 summarises the proposed roll-forward calculation.

Table 2.4: GasNet’s proposed roll forward of the capital base (\$ nominal million)

	2002	2003	2004	2005	2006	2007
Opening capital base	496.92	496.18	487.97	479.70	473.88	485.73
Depreciation allowance	-16.89	-20.61	-21.60	-22.81	-23.92	-24.41
Capital expenditure	0.31	0.50	0.70	3.62	20.69	48.08
Disposals/redundancies	0.00	0.00	0.02	0.00	0.00	0.00
Inflation	15.84	11.90	12.64	13.37	15.08	14.97
Closing capital base	496.18	487.97	479.70	473.88	485.73	524.36

Source: GasNet, *Access Arrangement 2008–12 Information*, p. 3; GasNet PTRM.¹⁸

In calculating its capital base at the beginning of the AA2 period, GasNet provided a best estimate of \$0.66 million for capex in 2002. GasNet indicates that actual capex for 2002 was \$0.31 million and states the capital base has been adjusted to account for this underspend. However, the higher forecast capex amount was incorporated into the capital base for the AA2 period and GasNet has therefore earned a return on and of this amount over the period. GasNet does not propose to pass back the value of the return on this underspend to network users through a reduction in its revenue requirement for the AA3 period. The return of this amount was provided to GasNet in the depreciation allowance for AA2, which has been deducted from the opening capital base for AA3.

GasNet used an inflation estimate of 0.54 per cent for the December quarter 2002 in calculating its capital base as at the beginning of the AA2 period. GasNet has adjusted the capital base to incorporate actual inflation for this period of 0.72 per cent. In effect, this underestimate of inflation resulted in GasNet’s capital base being slightly undervalued for the AA2 period, resulting in the returns on capital being similarly lower than they would otherwise have been.

Issues for consideration

The ACCC seeks comments on whether:

- GasNet’s proposed roll-forward of the capital base is consistent with the requirements of the Code;

¹⁸ GasNet’s post tax revenue model submitted to the ACCC.

- GasNet should be allowed to retain the benefit of the return on capital underspend in 2002 that was provided over the AA2 period;
- there should be an adjustment to revenues to correct for the lower returns on capital associated with the underestimate of inflation for the December quarter 2002.

2.10 Actual capital expenditure

The ACCC approved a forecast capital expenditure allowance of \$47.72 million to be incurred during AA2. Although the approved forecast projects have largely proceeded as planned (some projects will be completed later than expected), GasNet has spent \$35.42 million of capital expenditure on non-forecast projects, exceeding its approved forecast allowance by \$19.86 million.

Table 2.5: Actual capital expenditure (\$2006 Dec million)

	2003	2004	2005	2006	2007	Total
Forecast projects						
Gooding compressor refurbishment	-	-	-	-	16.03	16.03
Lurgi pipeline refurbishment	-	-	-	2.82	-	2.82
City gate upgrades and heaters	-	-	-	-	5.38	5.38
Wollert compressor station automation	-	-	-	-	2.76	2.76
Gas chromatographs	0.27	0.19	-	-	-	0.46
Other maintenance capex	0.21	0.30	1.09	0.70	2.38	4.70
Total	0.48	0.50	1.09	3.52	26.57	32.16
Non-forecast projects						
Brooklyn compressor redevelopment	-	-	-	3.00	14.46	17.46
South Melbourne cut in	-	-	-	2.98	-	2.98
Wollert compressor station (miscellaneous)	-	0.17	0.83	-	1.15	2.15
Pig traps	-	-	-	-	0.72	0.72
Safety and security	-	-	-	-	0.79	0.79
Iona Cooler upgrade	-	-	-	-	0.70	0.70
Regulators work	-	-	-	-	0.42	0.42
Corporate restructuring	-	-	-	8.84	-	8.84
Total	0.00	0.17	2.20	14.82	18.23	35.42

Source: GasNet, *Access Arrangement 2008–12 Information*, p. 12.

GasNet proposes that its total actual capital expenditure be included in its rolled-forward capital base in accordance with ss. 8.16 and 8.20–8.22 of the Code.

Inclusion in the capital base

Section 8.16 of the Code allows the capital base to be increased by the actual cost of the new facilities investment provided the amount incurred is not more than would be invested by a prudent service provider acting efficiently (acting in accordance with accepted good industry practice to achieve the lowest sustainable costs of delivering services) and provided one of the following conditions is satisfied:

- (i) the anticipated incremental revenue exceeds the costs incurred (the economic feasibility test—s. 8.16(a)(ii)(A) of the Code); or
- (ii) the new facility has system-wide benefits that justify a higher tariff for all users (the system-wide benefits test—s. 8.16(a)(ii)(B) of the Code); or
- (iii) the new facility is necessary to maintain the safety, integrity or contracted capacity of services (the system integrity test—s. 8.16(a)(ii)(C) of the Code).

GasNet submits that all of its actual capital expenditure incurred in AA2 satisfies s. 8.16 of the Code, in particular the system integrity test as the capital expenditure incurred was of a maintenance nature and did not augment or increase the capacity of the PTS.

The ACCC will assess the actual capital expenditure GasNet submits it incurred in AA2 and include that which satisfies s. 8.16 of the Code in GasNet's capital base.

Corporate restructuring costs

GasNet proposes to capitalise corporate restructuring costs incurred in 2006 as a part of the APA Group's takeover of GasNet and include these costs in the capital base.

GasNet submits the costs of corporate restructuring total \$10 million, of which \$8.84 million is allocated to the GasNet's regulated business. GasNet indicates that these costs include payments to legal advisers, evaluation experts and strategic consultants for strategic advice and a break fee.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- GasNet's actual capital expenditure in AA2 is reasonable and prudent;
- GasNet's actual capital expenditure in AA2 satisfies the system integrity test;
- the proposed inclusion of capital expenditure incurred in relation to corporate restructuring in the capital base satisfies s. 8.16 of the Code, or whether these costs should be classified as non-capital costs; and
- the allocation of \$8.84 million of the \$10 million corporate restructuring costs to the regulated business is appropriate.

2.11 Inclusion of interest during construction for AA2 and AA3

GasNet proposes that its capital expenditure be included in the capital base on an 'as-commissioned' basis, which does not recognise the timing or value of actual

expenditures incurred prior to capitalisation. In this context GasNet proposes to capitalise the costs of interest during construction (IDC) for each asset constructed during AA2 and forecast in AA3.

In calculating IDC amounts, GasNet has modelled monthly expenditure profiles for four types of assets. Expenditure on pipelines, compressors, pressure regulators and heaters is assumed to occur over a 22 month period with commissioning occurring at the end of the 19th month. Expenditure on ‘other’ assets is assumed to occur over three months with commissioning at the end of the third month.

GasNet calculates IDC as the amount of expenditure required at the asset commissioning date that is equal, in net present value terms, to the value of the assumed monthly expenditures. In other words, GasNet has assumed that IDC on forecast expenditure accrues at a rate which is equal to its proposed weighted average cost of capital.

Tables 2.6 and 2.7 outlines the ACCC’s estimate of forecast IDC per asset class using GasNet’s assumptions.

Table 2.6: Estimate of IDC incurred over AA2 period (\$2006 Dec million)

	2003	2004	2005	2006	2007
Pipelines	-	-	0.1	1.1	0.3
Compressors	0.0	0.0	0.1	0.3	2.8
City Gates & Field Regulators	-	-	-	0.0	0.1
Odourant Plants	-	-	-	-	0.0
Gas Quality	0.0	0.0	-	-	0.0
Other	0.0	0.0	0.1	0.6	0.0
General Building	-	0.0	0.0	-	0.0
Total	1.3	0.0	0.3	2.0	3.2

Source: ACCC estimates from GasNet RAB model.

Table 2.7: Estimate of forecast IDC for AA3 (\$2006 Dec million)

	2008	2009	2010	2011	2012
Pipelines	1.7	0.6	1.5	0.0	0.3
Compressors	0.1	3.4	-	0.4	0.9
City Gates & Field Regulators	0.2	0.0	0.0	0.0	0.0
Odourant Plants	-	-	-	0.0	-
Gas Quality	0.0	-	-	0.0	-
Other	0.0	0.0	0.0	0.0	0.0
General Building	0.0	-	-	0.0	-
Total	2.0	4.1	1.6	0.4	1.3

Source: ACCC estimates from GasNet RAB model.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- the proposed allowance for interest during construction is prudent and efficient;
- these costs should also be included with new facilities investment over the AA2 period and included in the capital base.

2.12 Revenue proposal

Table 2.8 sets out the revenue requirements proposed by GasNet under the building block methodology, and its components, for each year of AA3. It also shows the smoothed forecast revenue for each year.

Table 2.8: Components of the revenue requirement, forecast revenue (\$2006 Dec million)

<i>Components of revenue requirement</i>	<i>2008</i>	<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>
Return on capital	32.42	37.63	41.86	42.42	42.43
Depreciation	22.53	25.79	28.09	28.58	29.40
Non-capital costs	27.37	26.25	26.03	27.59	29.40
Total revenue requirement	82.30	89.68	95.98	98.59	101.23
Forecast revenue	86.18	89.77	93.79	96.87	100.55

Source: GasNet, Access Arrangement 2008–12 Information, pp. 11–12 (converted to \$2006 December).

Reflecting the capital-intensive nature of gas transmission services, the return on capital is the largest component of the revenue requirement. Similarly, return of capital (depreciation) represents a substantial component of revenue.

In the AA2 access arrangement GasNet, in calculating its total revenue, assumed that all cash flows except for capex take place at the end of the year. It was assumed that capex occurs in the middle of each year and is rolled into the regulatory asset base at the end of the year. The return on capital was calculated from the opening regulatory asset base value and paid at the end of the year and so did not incorporate a return on capex for the half year period from when assets are commissioned to when they are rolled into the regulatory asset base. The ACCC has previously argued against providing a half-year return on capex on the basis that the end-of-year modelling assumptions over-compensate GasNet. For example, revenues are actually recovered evenly throughout the year rather than at the end of the year as assumed in the modelling.

GasNet proposes to amend its revenue model in AA3 to provide for a half-year return on capex in the year when assets are commissioned. In doing so GasNet calculates a simplified monthly cash-flow model for AA3 using benchmark payment cycles for revenues, opex and capex for several asset types, with values that correspond to the yearly forecasts in its submission. This model contains adjustments (including to opex and revenue) to equate the present values of monthly and yearly cash flows. GasNet

uses this model to compare the presence and absence of an additional half-year return on capex. The result is that the additional return would result in an over-recovery of revenues, in present value terms, by an estimated 0.4 per cent, compared to an estimated under-recovery of 1.9 per cent where this return is not provided. It should be noted, however, that these results do not appear representative of GasNet's proposal which does not envisage the amendments related to the timing of opex and revenues that feature in its monthly model. More generally, GasNet's proposed amendment would seem to create an inconsistency between the timing assumptions for capex (middle of the year) and those for opex and revenues (end of the year).

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- an amendment to GasNet's revenue model to include a half-year return on capex is necessary to provide an opportunity to recover the efficient costs of providing the Reference Service; and
- GasNet should adjust all of its cash flows, namely opex, revenues and capex, such that they are all assumed to occur at the same time.

2.13 Forecast capital expenditure

GasNet proposes a substantial capital expenditure program in AA3 which incorporates augmentations, refurbishment and upgrades to the PTS of \$334.08 million. This is approximately 64 per cent of the value of GasNet's proposed the 2007 rolled-forward RAB and is some five times the amount that was invested by GasNet under AA2. Table 2.9 sets out GasNet's proposed capital expenditure program.

GasNet submits the proposed capital expenditure program is necessary to address the increasing load growth in Victoria and the anticipated constraints from 2007/08 onwards as identified in VENCORP's 2006 Annual Planning Review.

Table 2.9: Forecast capital expenditure (\$2006 Dec million)

	2008	2009	2010	2011	2012
Augmentations					
Northern zone	-	79.03	-	-	-
Sunbury loop	-	-	-	-	12.46
Ballarat loop	-	-	29.03	-	-
Warragul loop	-	4.84	-	-	-
Pakenham	-	1.22	-	-	-
Stonehaven compressor	-	-	-	-	26.19
Carisbrook loop	-	-	24.05	-	-
Brooklyn Lara (Corio) pipeline	63.71	-	-	-	-

Brooklyn Wollert easements	-	-	5.37	-	-
Total augmentations	63.71	85.12	58.45	0	38.63
Refurbishments and upgrades					
Gas heating facilities	7.22	1.99	-	-	-
City gate works	6.68	-	-	-	-
Pipeline upgrades	2.45	4.13	0.89	1.29	0.89
Safety and security systems	3.41	0.84	-	-	-
Brooklyn compressor station	-	37.76	-	11.81	-
Wollert compressor station	-	1.58	-	-	-
Other compressor stations	1.34	-	-	-	1.62
Other	1.76	0.36	0.43	0.82	0.93
Total refurbishments and upgrades	22.87	46.65	1.32	13.92	3.43
Total capital expenditure	86.57	131.77	59.76	13.92	42.06

Source: GasNet, *Access Arrangement 2008–12 Information*, table 3-10.

Proposed augmentation projects

GasNet submits the proposed augmentations are necessary to increase the capacity of the PTS to meet growing demand and avoid breaches of minimum system pressure obligations in accordance with VENCORP's system security guidelines and distribution business connection deeds.

As detailed in table 2.9, GasNet proposes a total of \$245.91 million in augmentations, through the upgrade of compressors and pipeline looping to address the growing demand on parts of the network. In particular, major augmentation is planned for the Wollert to Wodonga pipeline, involving both new compression capacity and looping to accommodate higher forecast demand. The major looping project on the Brooklyn to Lara (Corio) pipeline was approved by the ACCC in June 2006.¹⁹ Other major looping is planned for the pipelines to Sunbury, Carisbrook and Ballarat. A new compressor station at Stonehaven on the South West pipeline is planned for 2012.

GasNet submits the network timing and planning reports prepared by VENCORP support the proposed forecast capital expenditure.²⁰

Refurbishment and upgrades

GasNet submits the proposed refurbishments and upgrades of \$88.19 million in AA3 are necessary to maintain the service potential of existing facilities as they age and deteriorate.

The largest refurbishment project GasNet proposes is the Brooklyn Compressor Station, which involves significant upgrading of compressor units in addition to other major work involving control systems and the installation of a fire suppression system. In particular, GasNet proposes two larger Centaur compressors to replace the four

¹⁹ See ACCC, Final Decision: Major System Augmentation—Corio Loop, June 2006.

²⁰ VENCORP has requested that these reports not be publicly released until the VENCORP Board has approved release. At See section 4.6 of this issues paper.

existing Saturn units. The current wet-seal compressors are to be replaced with dry-seal compressors to prevent ingress of oil into the pipeline.

GasNet also proposes significant work for a number of city gates including the replacement of ageing regulators and the installation of water bath gas heaters (which GasNet submits are required, inter alia, to avoid hydrocarbon liquid condensation with the advent of gas supplies from new sources). GasNet proposes these water bath gas heaters for Lara, Dandenong, Brooklyn, Wandong, Clonbinane and North Laverton.

GasNet notes the compressor strategy supports the proposed refurbishment and upgrade capital expenditure.²¹

Inclusion of forecast capital expenditure in the capital base (s. 8.20 of the Code)

In accordance with s. 8.20 of the Code, reference tariffs may be determined based on forecast capital expenditure (or new facilities investment) for the forthcoming access arrangement period if it is reasonably expected to pass the requirements of s. 8.16 of the Code (for inclusion in the capital base) when the investment is forecast to occur.

In this regard GasNet submits:

- all of the proposed projects satisfy the prudent investment test as they reflect a level of investment prudent to achieve the service standard in a technical and engineering sense, and each project will be put to tender to find the most efficient and lowest cost solution (i.e. will satisfy the prudent investment test)
- all of the proposed projects (with the exception of the Stonehaven compressor) satisfy the system integrity test as they are necessary to maintain the safety, integrity or contracted capacity of services and
- the Stonehaven compressor augmentation satisfies the system-wide benefits test as there are sufficiently substantial system-wide benefits associated with this augmentation.

Issues for consideration

The ACCC seeks comments and supporting evidence on:

- the necessity of the proposed augmentations GasNet proposes to meet growing demand and avoid breaches in minimum system pressure requirements;
- GasNet's proposed recovery of augmentation expenditure on the basis of the Code's system integrity test is consistent with its proposed tariff structure for tariff V users;

²¹ See GasNet, *Proposed Access Arrangement Submission*, Attachment C, which includes GasNet's compressor strategy. The compressor strategy is a review of the status and redevelopment plans for its compressor facilities.

- the necessity of the proposed refurbishment and upgrades to maintain the service potential of existing facilities;
- whether the proposed capital expenditure is consistent with the other assumptions in the proposed access arrangement (e.g. peak demand forecasts); and
- the nature and extent of oil ingress into the pipeline supports GasNet’s compressor upgrade strategy.

2.14 Weighted average cost of capital

GasNet proposes a nominal post-tax weighted average cost of capital (WACC) of 9.01 per cent. This incorporates a post-tax nominal cost of equity which rises from 11.40 to 11.85 per cent. However, the real post-tax real vanilla WACC falls from 6.62 to 5.74 per cent.

Table 2.10 sets out the WACC parameters as approved by the ACCC for AA2 and those GasNet proposes for AA3.

Table 2.10: AA2 WACC parameters and AA3 proposed WACC parameters

<i>WACC parameter</i>	<i>Current (AA2)</i>	<i>GasNet proposal (AA3)</i>
Real risk-free interest rate	3.33%	2.68%
Nominal risk-free interest rate	5.57%	5.85%
Bond maturity period	10 years	10 years
Expected inflation	2.16%	3.09%
Debt margin	1.71%	1.14%
Debt raising costs		0.125%
Credit rating		BBB
Cost of debt	7.28%	7.12%
Market risk premium	6.00%	6.00%
Gearing ratio	60.00%	60.00%
Value of imputation credits	50.00%	50.00%
Equity beta	0.973	1.00
Return to equity	11.40%	11.85%
Nominal Vanilla WACC	8.93%	9.01%
Real Vanilla WACC	6.62%	5.74%

Source: GasNet, Revised Access Arrangement Information, 1 January 2005, cl. 3.2.

In particular the ACCC notes GasNet’s proposals reflect:

- an increase in the expected inflation rate from 2.16 to 3.09 per cent (see discussion below);
- a reduction in the debt margin and the cost of debt; and
- an increase in the equity beta from 0.973 to 1.00.

Forecast inflation rate

The accepted approach the ACCC adopts to estimate the forecast inflation rate is to apply the yields on 10 year indexed Commonwealth Government securities (CGS) and 10 year nominal CGS to the Fisher equation.

GasNet considers the nominal and index-linked CGS yields may currently reflect a downwards bias due to the limited supply of index-linked bonds in the market. GasNet claims applying these yields into the Fisher equation lead to a biased estimate of the inflation rate, and in turn an underestimation of the true WACC.²²

To offset this possible bias, GasNet proposes that in the ACCC's AA3 final decision, if the approved forecast inflation rate:

- exceeds the target band of 2 to 3 per cent used by the Reserve Bank of Australia (RBA), the forecast inflation rate be capped at 3 per cent as this would evidence the pricing of a premium for the risk that the RBA will not be successful in meeting its monetary targets; or
- is less than 3 per cent, an appropriate adjustment be made to the risk-free rate as this would evidence a possible bias in the nominal and indexed bond rates.

Issues for consideration

The ACCC seeks comments and supporting evidence on GasNet's proposed WACC bearing in mind the WACC set in AA2 and in particular:

- on the alleged downwards bias of nominal and index-linked CGS yields; and
- whether other proposed changes in GasNet's proposed access arrangement will affect the WACC (e.g. changes to the average revenue control model).

2.15 Depreciation

GasNet proposes to determine its depreciation allowance using a real straight-line methodology over AA3. GasNet also proposes the following technical lives, which are listed against those used in AA2 in table 2.11.

²² In support of this claim GasNet has lodged a report prepared by Synergies Economic Consulting. See GasNet, *Proposed Access Arrangement Submission*, Appendix F.

Table 2.11: Technical life per asset category

<i>Asset category</i>	AA2	AA3
Compressor stations	30	30
Heaters	20	20
Regulators	30	30
Pipelines	60	60
Telemetry	5	10
Buildings	60	60
Land	n/a	n/a
Office equipment	5	5

Source: GasNet, Access Arrangement 2003–07 Information, p. 6; Access Arrangement 2008–12 Information, p. 6.

For AA3, GasNet proposes the economic lives of these assets be equal to their technical lives, with the exception of pipeline assets. GasNet proposes that the economic life of new pipelines be set at 55 years. Table 2.12 illustrates the different lives per pipeline group used in AA2 and those GasNet proposes for AA3.

Table 2.12: Current and proposed economic lives for pipeline groups

<i>Pipeline Group</i>	AA2	AA3
Longford	2023	2023
SWP	2052	2052
Murray Valley	2033	2054
Lurgi	2016	2033
Other existing pipelines	2033	2033
New pipelines	55 years	55 years

Source: GasNet, Access Arrangement 2003–07 Information, p. 7; Access Arrangement 2008–12 Information, p. 6.

GasNet proposes to depreciate the Longford pipeline completely by 2023 as per the economic life approved in AA2. The ACCC approved the shortening of the life of the Longford pipeline in the context of GasNet’s legitimate business interests in accordance with s. 2.24(a) of the Code, noting that it may reassess this decision in light of future studies relating to reserves in the Gippsland Basin or other factors impacting on the pipeline’s useful life.

Consistent with that approved for AA2, GasNet proposes to depreciate the SWP over a period of 50 years, with its useful life ending in 2052. In approving the depreciation for the SWP in AA2, the ACCC noted that the use of a longer asset life would result in a lower tariff in the initial years of the pipeline’s life and therefore assist the development of its market. The ACCC also noted that it would reassess the life of the SWP in the future as provided for under s. 8.33 of the Code. Table 2.13 outlines the depreciation allowance GasNet proposes.

GasNet proposes to extend the economic life of the Murray Valley pipeline. GasNet’s proposal would extend the economic life of this pipeline to 56 years, which is in line with the 55 year life assumed for all new pipelines.

GasNet has not indicated that it proposes to retain the assumed economic life of the Lurgi pipeline, implying that it proposes to treat this asset as per the remaining pipelines whose lives extend to 2033.

Table 2.13: Proposed depreciation allowance by asset category (\$million, Dec 2006)

<i>Asset category</i>	<i>2008</i>	<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>
Pipelines	15.4	16.3	17.1	17.7	17.8
Compressors	4.7	6.6	8.1	8.2	8.9
City gates and field regulators	1.2	1.5	1.5	1.5	1.5
Odourisation	0.0	0.0	0.0	0.0	0.0
Gas quality	0.1	0.1	0.1	0.1	0.2
General land and building	0.8	0.8	0.8	0.5	0.5
Other	0.4	0.5	0.5	0.5	0.5
Total	22.5	25.9	28.1	28.7	29.4

Source: GasNet Access Arrangement 2008–12 Information, p. 7, converted to Dec 2006 dollars.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- GasNet’s proposed depreciation methods and proposed asset lives is consistent the Code requirements; and
- there is any need to reassess the assumed economic life of the Longford pipeline and SWP.

2.16 Non-capital costs

GasNet proposes forecasting operating and maintenance expenditure for AA3 in accordance with the methodology outlined in s. 7.2(h) of its AA2 access arrangement. This requires GasNet to:

- (ii) take into account the actual operating costs in 2006, adjusted for the change in operating costs between 2006 and 2007 and to avoid doubt, not taking into account the efficiency gain (loss) made in 2007;
- (iii) take into account forecast changes in workload, taxes, regulatory events, insurance premiums and other relevant costs between 2006 and each year of the Third Access Arrangement Period; and
- (iv) take into account a percentage trend factor.

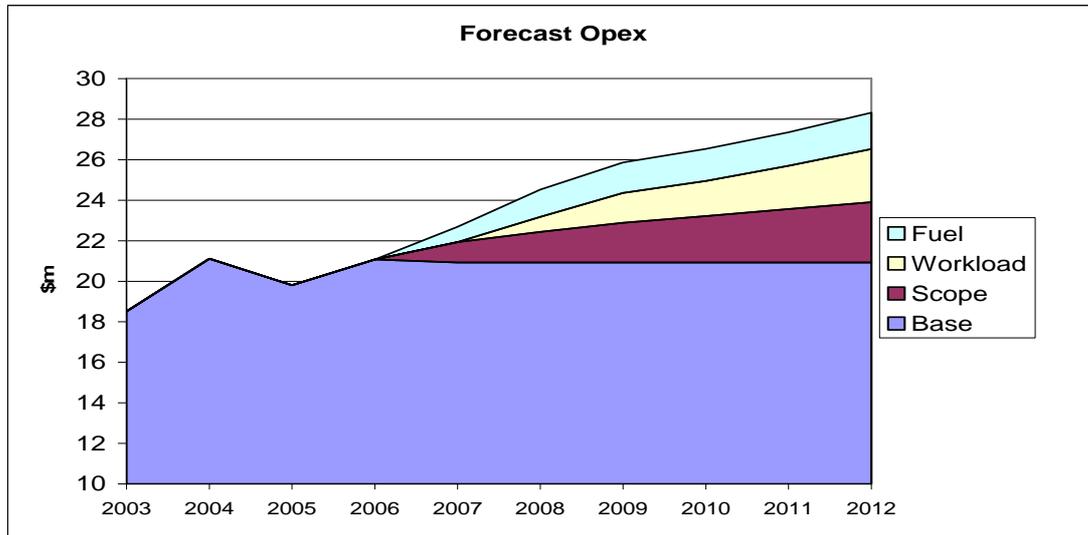
GasNet proposes a real increase in operating and maintenance costs of 31 per cent over AA3 from AA2 due to:

- increased operating costs associated with GasNet’s proposed capital expenditure program over AA3 (referred to as ‘workload’ changes); and

- increased operating costs associated with ‘operating scope’ changes on direct operating costs and corporate overheads.

The breakdown of the operating and maintenance expenditure GasNet proposes is shown in figure 2.1.

Figure 2.1: Actual and forecast operating costs (\$m 2006 Jun)



Source: GasNet, *Access Arrangement 2008–12 Submission*, p. 72.

GasNet proposes the workload cost increases on the basis of:

- increased operating costs driven by the greater length of the PTS pipeline from the construction of a number of proposed pipeline loopings;
- increased operating costs driven by the proposed increase in compressor, inline regulator and heater costs, resulting of increased compressor capacity in the PTS from a number of proposed upgrades; and
- additional growth of fuel gas usage and an assumed increase in fuel gas costs of up to 10 per cent costs.

GasNet submits the drivers of its proposed scope increases as new technical and safety legislation and economy wide exogenous factors, which include increases in the real cost of labour.

Productivity changes

GasNet submits the gas industry is now facing a period of rising costs and productivity gains to be made as a result of privatisation have been exhausted.

Issues for consideration

The ACCC seeks comment and supporting evidence on whether:

- the actual 2006 operating and maintenance expenditure is a reliable basis to forecast from over AA3;
- GasNet's proposed 'workload and scope change' operating costs for AA3 are efficient and prudent;
- the forecast increase in fuel gas costs of 10 per cent is reasonable; and
- there are likely to be scope for efficiency improvements arising from GasNet's proposed capital expenditure for the refurbishment and upgrade of assets.

2.17 Incentive mechanisms

As contemplated by s. 8.44 of the Code, GasNet's AA2 access arrangement incorporated incentive mechanisms enabling GasNet to retain certain returns from transmission tariffs during AA2.

A rolling carryover incentive mechanism for operating costs was incorporated as part of GasNet's access arrangement in AA2 as a fixed principle. The fixed principle permitted GasNet to keep certain efficiency gains and losses from AA2 in AA3.

GasNet proposes to keep a share of the efficiency gains (losses) over AA2 in accordance with the benefit sharing allowance. However, GasNet also proposes the following amendments to the fixed principle:

- the removal of fuel gas costs; and
- the Regulator be allowed to exercise discretion in determining how any accrued negative carryover amount at the end of an access arrangement period should be treated.

Issues for consideration

The ACCC seeks comments and supporting evidence on whether:

- fuel gas costs should be removed from the carry-over mechanism;
- the Regulator should be allowed to exercise discretion in determining negative carryover amounts.

2.18 Information

The Code requires a proposed access arrangement to be supported by access arrangement information. Section 2.6 of the Code specifies that the access arrangement information must contain such information that in the opinion of the regulator would enable users and prospective users to understand the derivation of the elements in the proposed access arrangement and to form an opinion as to the compliance of the access arrangement with the provisions of the Code. Section 2.7 of the Code states the access arrangement information may include any relevant information but must include at least the categories of information described in attachment A to the Code which provides a guide detailing examples of minimum disclosure obligations.²³

GasNet provided extensive documentation in support of its revisions. This includes the system planning reports prepared by VENCORP in support of GasNet's capex augmentation program, which GasNet has subsequently claimed confidentiality over on following an instruction from VENCORP. The ACCC understands that confidentiality is sought on the grounds that these reports are not approved VENCORP reports for public release at this stage. VENCORP requested that the ACCC delay the public release of the reports until the VENCORP Board has formally approved these reports.

The ACCC is concerned that given that GasNet has submitted these reports as supporting information in regard to its proposed capital expenditure program, that interested parties have timely access to these reports. Given the timing of the ACCC's proposed draft decision, in the absence of VENCORP Board approval, the ACCC will release these reports on its website no later than 8 June 2007.²⁴ This will allow interested parties to consider these reports in submissions to the ACCC on GasNet's application.

At this stage only information over which confidentiality has been claimed has not been disclosed. These reports will be available on the AER's website at www.aer.gov.au no later than 8 June 2007.

GasNet provided detailed financial modelling information to the ACCC on 30 April 2007 to assist its assessment.

GasNet's proposed access arrangement information includes forecasts of costs and demand which are reproduced elsewhere in this issues paper. It also describes GasNet's pricing proposal. GasNet's submission contains additional information, including the revenue requirement. As envisaged by section 2.9 of the Code, the

²³ Attachment A to the Code is reproduced in appendix 1 to this issues paper.

²⁴ It should be noted that the ACCC is empowered to consider any confidentiality claims on their merits and determine whether any commercially sensitive information is of such significance that its release is justified in the public interest. In this case, however, there do not appear to be any material commercial sensitivity concerns, but rather the issue relates to the internal timing processes of VENCORP. Accordingly, the ACCC does not consider there are any substantive matters associated with the public release of this information.

ACCC will review the access arrangement information provided by GasNet and determine whether changes need to be made.

GasNet provides in its access arrangement information two key performance indicators (KPIs) which are:

- opex as a percentage of ORC; and
- opex per km.

In both cases GasNet falls within the middle of the range.

Issues for consideration

The ACCC seeks comments on:

- the issue regarding the capital program planning reports aside, does the access arrangement satisfy the requirements of ss. 2.6 and 2.7 of the Code, or a changes necessary; and
- are the KPI's provided and the benchmarks chosen the most appropriate ones, and has GasNet correctly interpreted the results.

2.19 Any other matters

The issues raised in this issues paper are not intended to restrict or influence submissions lodged by interested parties. Submissions are welcome on any matter associated with GasNet's proposed access arrangement including any issues which may have been omitted from the proposed access arrangement, access arrangement information and submission and this issues paper.

Appendix 1

ATTACHMENT A INFORMATION DISCLOSURE BY A SERVICE PROVIDER TO INTERESTED PARTIES

Pursuant to Section 2.7 [of the Code] the following categories of information must be included in the Access Arrangement Information.

The specific items of information listed under each category are examples of the minimum disclosure requirements applicable to that category but, pursuant to Sections 2.8 and 2.9 [of the Code], the Relevant Regulator may:

- allow some of the information disclosed to be categorised or aggregated; and
- not require some of the specific items of information to be disclosed,

if in the Relevant Regulator's opinion it is necessary in order to ensure the disclosure of the information is not unduly harmful to the legitimate business interests of the Service Provider or a User or Prospective User.

Category 1: Information Regarding Access & Pricing Principles

Tariff determination methodology

Cost allocation approach

Incentive structures

Category 2: Information Regarding Capital Costs

Asset values for each pricing zone, service or category of asset

Information as to asset valuation methodologies - historical cost or asset valuation

Assumptions on economic life of asset for depreciation

Depreciation

Accumulated depreciation

Committed capital works and capital investment

Description of nature and justification for planned capital investment

Rates of return - on equity and on debt

Capital structure - debt/equity split assumed

Equity returns assumed - variables used in derivation

Debt costs assumed - variables used in derivation

Category 3: Information Regarding Operations & Maintenance

Fixed versus variable costs

Cost allocation between zones, services or categories of asset & between regulated/unregulated

Wages & Salaries - by pricing zone, service or category of asset

Cost of services by others including rental equipment

Gas used in operations - unaccounted for gas to be separated from compressor fuel

Materials & supply

Property taxes

Category 4: Information Regarding Overheads & Marketing Costs

Total service provider costs at corporate level

Allocation of costs between regulated/unregulated segments

Allocation of costs between particular zones, services or categories of asset

Category 5: Information Regarding System Capacity & Volume Assumptions

Description of system capabilities

Map of piping system - pipe sizes, distances and maximum delivery capability

Average daily and peak demand at "city gates" defined by volume and pressure

Total annual volume delivered - existing term and expected future volumes

Annual volume across each pricing zone, service or category of asset

System load profile by month in each pricing zone, service or category of asset

Total number of customers in each pricing zone, service or category of asset

Category 6: Information Regarding Key Performance Indicators

Industry KPIs used by the Service Provider to justify "reasonably incurred" costs

Service provider's KPIs for each pricing zone, service or category of asset