



19 December 2011

Mr Warwick Anderson
General Manager
Network Regulation Branch
Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

By email: rbb@aer.gov.au

Dear Mr Anderson

APT PETROLEUM PIPELINE LIMITED 2012-17 ACCESS ARRANGEMENT PROPOSAL FOR THE ROMA TO BRISBANE PIPELINE

Origin Energy (Origin) welcomes the opportunity to comment on APT Petroleum Pipeline Limited's (APTPPL's) proposed revisions to its Access Arrangement for the Roma to Brisbane Pipeline (RBP) to apply from 12 April 2012 to 30 June 2017 (the Proposed Access Arrangement).

Where possible, Origin supports the use of markets rather than regulation to deliver efficient and effective outcomes. A prerequisite for this, however, is the presence of workable competition. When there is an absence of effective competition, regulation may be necessary to address the risks associated with monopoly powers. This is the case for the RBP: it is a natural monopoly asset with no alternative competing pipelines to transport gas into the Brisbane market.

Consequently, Origin supports the continued full regulation of the RBP. Under the fully regulated framework, the Access Arrangement governs the arrangements under which users can gain access to the RBP. As such, the Access Arrangement must address the needs of users and ensure that all revenue requirements, associated tariffs and charges, and non-price terms and conditions are reasonable, justifiable, cost-reflective and transparently determined. Such outcomes are in the long-term interests of consumers and promote the National Gas Objective.

The lack of supporting detail and explanations in the Proposed Access Arrangement makes it difficult to determine whether or not its terms and conditions meet the above criteria around transparency and reasonableness. As such, this submission raises a number of questions and concerns, particularly around the:

1. reference tariff price path;
2. proposed changes to other reference service charges;
3. future extensions and expansions;
4. new auction process; and
5. capacity trading arrangements.

We recommend that the AER focus on these aspects of the Proposed Access Arrangement when preparing its Draft Decision.

1. Reference tariff price path

Origin does not understand what is driving the proposed significant increases in the reference tariff rate. Consistent with the current 2007-11 RBP Access Arrangement, the Proposed Access Arrangement defines a single reference service: a non-interruptible service for the receipt, transportation and delivery of gas through any length of the RBP in the direction from Wallumbilla or Peat to Brisbane.¹ The reference service continues to be provided at the reference tariff, which is the sum of the capacity charge and the throughput charge. The reference tariffs are then adjusted annually by a Consumer Price Index and X factor (CPI-X) price adjustment mechanism.

While the CPI-X methodology may remain appropriate, APTPPL proposes substantial X factors of -17.8% in 2012/13 and -13% each year from 2013/14 to 2016/17. This translates into a CPI+17.8% increase in the reference tariff rate in the first year and then a CPI+13% increase in each of the subsequent years.² There is little explanation, however, around changes to APTPPL's cost structure that would warrant such substantial increases each year. For example, over the five-year period of the Proposed Access Arrangement, APTPPL has forecasted:

- zero demand growth;
- zero capital expenditure for expansions or extensions;
- only a small increase in stay-in-business capital expenditure;
- relatively steady increases in operating expenditure; and
- a falling capital base.

Given this, we do not see the justification for such a significant escalation in the reference tariff price path.

Setting the reference tariff at the appropriate level is important to more than just those who have reference tariff contracts.³ The reference tariff sets the base for negotiating all other RBP services and their rates. Having the reference tariff and its associated price path set using a robust and transparent process provides customers with a more confident and informed negotiating platform. This can facilitate more effective and equitable contract negotiations between APTPPL and its customers, particularly helping to address the potential information asymmetries between the counter-parties.

A key principle for regulated asset owners is that they should be limited in their ability to over-recover their costs for providing their services. As these services are monopoly services, adhering to this principle ensures effective competition and equity of access for pipeline users. Removing information asymmetries and promoting transparency are important when setting tariffs in order that they are reasonable and cost-reflective. This reduces the potential for the service provider to double recover through earning both reference services and negotiated services, particularly for new capacity.

2. Proposed changes to other reference service charges

APTPPL has proposed changes to a number of other charges pursuant to the reference service. These are summarised in the table below.

¹ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, p. 4

² APTPPL 2011, *Access Arrangement Submission*, October, p. 107

³ At the AER's public forum in Brisbane on 30 November 2011, APTPPL commented that currently there are only two small contracts for the RBP that are at the reference tariff.

Table: Comparison between 2006-11 Access Arrangement and Proposed Access Arrangement⁴

Charge	2006-11 (ACCC approved)	2012-17 (proposed)
Authorised overrun rate	120% of capacity tariff	120% of capacity tariff + throughput tariff
Unauthorised overrun rate	300% of capacity tariff	250% of capacity tariff + throughput tariff
Imbalance rate	250% of capacity tariff	250% of capacity tariff + throughput tariff
Imbalance allowance	N/A*	5% (either positive or negative) of the sum of MDQ for all delivery points
Daily variance rate	120% of capacity tariff	250% of capacity tariff + throughput tariff
Daily variance allowance	10% (either positive or negative) of the MDQ for the applicable delivery point or receipt point	5% (either positive or negative) of the MDQ for the applicable delivery point or receipt point

* The Access Arrangement acknowledges that despite APTPPL and users' reasonable efforts, minor imbalances will occur as a result of the inability to precisely match nominations and quantities received and delivered. APTPPL shall not be entitled to make any charges as a result of the minor imbalance.

As can be seen from the table, APTPPL proposes tightening the imbalance and daily variance allowances, as well as increasing the daily variance rate. We support the flexibility and tolerances reflected in the current arrangements. If a change is proposed, it should be supported by robust cost-benefit analysis to explain why the proposed arrangement delivers better value and more efficient outcomes. APTPPL has provided no such analysis or commentary. Given this, we ask that the AER examine closely the proposed changes.

3. Future extensions and expansions

We are unclear what APTPPL's intentions are around the delivery of future extensions and expansions. APTPPL proposes that where the Access Arrangement applies to the incremental services provided by an extension or expansion, it will elect whether access to the associated incremental services will be operated as part of the reference service or as a negotiated service. The policy also states that reference tariffs in the Access Arrangement period will not be affected by any extension or expansion made.⁵

This implies that all extensions or expansions going forward would be through negotiated services.

Origin supports extensions or expansions being undertaken as a negotiated service to deliver new capacity for commercial ventures; for example, to supply fuel to a new gas-fired generator. This allows for APTPPL and its counter-parties to negotiate a commercial tariff separate from the reference tariff. Those users paying the existing reference tariff are therefore not adversely or unfairly affected through variations to their reference tariff rate as a result of a new party changing the overall demand for gas on the RBP.

⁴ APTPPL 2007, *2007-11 Access Arrangement*, 28 February and APTPPL 2011, *2012-17 Proposed Access Arrangement*, October

⁵ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, pp. 35-36

There are also occasions where an extension or expansion needs to be regulated and form part of the reference service. The most relevant case is expanding capacity to meet organic growth in the retail mass market. In markets with Full Retail Contestability, retailers do not have a financial incentive to invest in pipeline extensions and expansions that support that market. Competitive dynamics that promote customer choice and churn mean that retailers, for example, are not guaranteed to earn the necessary return to justify the investment given their customer base may change. As a result, a regulated service provider needs to invest to meet any increase in mass market demand and continue to promote effective competition. These new services would then be included in the reference service.

Applying this logic on the RBP means that any future augmentation requirements in the Brisbane metro sector need to be delivered through regulated investment. This would then be included as a reference service. In its supporting Access Arrangement submission, APTPPL signalled that the capacity of the metro sector is expected to constrain the capacity of the RBP at some point in the future. The required looping to alleviate this constraint is expected to cost approximately \$50 million and may be required “late in the upcoming Access Arrangement period or early in the following period”.⁶

Given that this significant investment is forecast in the next 5-10 years, it is important to clarify APTPPL’s policy on future extensions and expansions. Origin seeks clarification from the AER on how to interpret APTPPL’s extensions and expansions policy and the policy’s application to the RBP metro sector investment.

4. New auction process

The Proposed Access Arrangement outlines a new auction process for existing and developable capacity. This new process is to replace the current first-come, first-served methodology.⁷ The Proposed Access Arrangement provides some detail around the steps and timeframes for this auction process.

While Origin supports the principle of the auction process and the level of transparency of the process itself, there are a few cases where we need to understand its practical application on the RBP. We also support APTPPL detailing its auction process in the Access Arrangement, but would like to understand better the AER’s views on how best to enforce the timelines and notice periods.

However, it is unclear whether the auction process would apply to negotiated service capacity as well as reference service capacity. This is an important distinction for pipeline users when making decisions around their participation in any auction process. For example, one scenario where the role of an auction is unclear is where a user is willing to underwrite the investment necessary for the developable capacity. The Proposed Access Arrangement stipulates that APTPPL may conduct negotiations with prospective users or hold an auction to determine the allocation of developable capacity following receipt of expressions of interest for that capacity.⁸ Private investors value certainty and as a result, an auction may not be the most suitable approach to progress with the new development. It is important that the incentive for private investment is retained because without that incentive, it may prove more difficult for future developments to occur.

For developable capacity, the Proposed Access Arrangement outlines a requirement that APTPPL’s auction notice specifies:

- the approximate developable capacity to be built;

⁶ APTPPL 2011, *Access Arrangement Submission*, October, p. 44

⁷ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, pp. 26-34

⁸ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, p. 31

- an indication of the tariff or range of tariffs that may apply; and
- the date the service may be available.⁹

It is unclear to prospective pipeline users how APTPPL determines the value of the tariff. There is an information asymmetry that leaves prospective users unable to sufficiently evaluate tariff information, which places them in a poor negotiation position for that capacity. We ask that the AER consider how the auction process section of the Access Arrangement could be enhanced to alleviate any potential asymmetries between the information held by APTPPL and prospective users. Clarity and transparency around how APTPPL sets the tariff level could greatly improve user understanding of how a suggested tariff reflects the costs of a new development. This promotes efficient tariff outcomes, as we have discussed above.

A suggested amendment to improve the transparency of the auction process is to specify timeframes in terms of business days. For example, the Proposed Access Arrangement states that users must be provided at least 30 days to lodge bids after the notice of auction is released.¹⁰ The actual timeframe to prepare bids depends on when in the year APTPPL releases its notice. Reporting the timeframes in business days provides participants with confidence around the minimum amount of time they have to respond. We recommend converting 30 days into at least “20 business days”.

5. Capacity trading

Origin supports more flexible arrangements around transferring or assigning RBP capacity to others and to different delivery and receipt points. The Proposed Access Arrangement maintains a requirement that a user must obtain consent from APTPPL to substitute all or part of an existing receipt or delivery point MDQ for another receipt or delivery point (respectively) on the RBP. In response to this application, APTPPL has the authority to withhold consent on or make its consent subject to “reasonable commercial and technical grounds”.¹¹ These grounds allow APTPPL excessive discretion to reject substitution requests as there is no clear definition of what constitutes reasonable commercial and technical grounds.

Greater flexibility to change receipt and delivery points enables user to utilise better their current capacity. Origin recommends that the Access Arrangement include a guideline on how APTPPL assesses a user’s application to substitute delivery and receipt points.

6. Further discussions

Should you have any questions or would like to discuss this submission further, please contact Hannah Heath (Manager, Regulatory Policy) on (02) 8345 5500 or hannah.heath@originenergy.com.au.

Yours sincerely



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⁹ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, p. 32

¹⁰ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, p. 32

¹¹ APTPPL 2011, *2012-17 Proposed Access Arrangement*, October, p. 25