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27 October 2016

Dear Mr Anderson

ROMA (WALLUMBILLA TO BRISBANE PIPELINE ACCESS ARRANGEMENT 2012-2017)

QGC Pty Limited (QGC) (a member of the Shell Group) welcomes the opportunity to respond to the Roma to Brisbane Pipeline (RBP) proposed Revised Access Arrangement (**the Proposal**) submitted by APT Petroleum Pipelines Pty Limited (APTPPL) for the period 2012 to 2017. Our interest in this proposal is two-fold - the direct commercial implications for QGC as a shipper on the RBP and the linkages of this issue to the current review of the Coverage Test for pipelines and the implications for gas market policy.

We have observed that the regulated service under the current Access Agreement has not kept pace with customer requirements. We are now operating in a more dynamic market, which has altered the flows on the pipeline giving rise to new and additional services, which are not regulated. Furthermore, the pipeline has been extended through looping and unregulated services such as "backhaul" have been offered for some time. We have observed that these "unregulated" services are being utilised just as extensively (if not to a greater extent) as the regulated service and the pricing for these services does not reflect the outcomes that would be expected in a competitive market. While we recognise there are some updates in the forthcoming Proposal, further adjustments are necessary to ensure it meets the overarching objectives of the regulatory framework for covered pipelines. Our specific comments include:

- The RBP reference service definition should be expanded to including other services such as "as available", "interruptible" and possibly "park and loan" services (until capacity trading is introduced).
- Tariffs should be realigned to reflect the level of risk borne by the pipeline and the underlying supply-demand dynamics on the RBP rather than a general uplift in the firm price.
- Consideration should be given to segmenting the RBP for the purposes of pricing. Given the change in gas flows due to the current transformation of the gas market, this would provide improved alignment across usage, cost allocation and pricing.
- The proposed rate of return appears somewhat high and from our understanding above those applied in other regulated sectors.

Further details are contained in the Attachment.

More generally and in the context of the broader policy debate, we note access to competitively priced pipeline capacity is an essential feature of an effective and efficient liquid gas market enabling gas to flow to customers who value it most. In our experience, current pricing structures on the RBP (and other east coast pipelines) are impacting the efficient operation of the market.

The cost of transport on the RBP (and associated redirection and compression services) is limiting the level of liquidity and transparency at the Wallumbilla Gas Supply Hub (Wallumbilla). Parties are incentivised to trade bi-laterally and agree alternative delivery points to those offered at Wallumbilla to avoid these high costs. This is also making it difficult in transitioning to a single Wallumbilla Hub product, which was agreed to by the COAG Energy Council in 2015. This is in part due to the current RBP regulatory framework being out of date and not capturing shifts in customer requirements.

Shell does not necessarily support an immediate change in the Coverage Test. Consideration of the issues applying to RBP Access Agreement, however, demonstrates that changes may be necessary to the overarching regulatory approach that applies to existing covered pipelines and any that may fall under the coverage umbrella following any change in policy.

Overall, Shell supports the Australian Energy Regulator's (AER) active consultation on the APTPP Proposal for 2017 to 2022. We welcome any further enquires on the issues raised in this response and look forward to continuing our involvement in this process. Questions can be directed to me or Ms Erin Bledsoe (0409 877 116).

Yours sincerely,

A handwritten signature in black ink, reading "Tom Summers". The signature is written in a cursive, flowing style.

Tom Summers
Vice President Supply and Optimisation



1. *Reference service coverage and pricing*

We have observed that the regulated service under the current Roma to Brisbane Pipeline (RBP) Proposal is out of date and has not kept pace with the shift in customer requirements since the existing arrangements were approved by the Australian Energy Regulator (AER), which will continue until June 2017. We are now operating in a more dynamic market, which has altered the flows on the pipeline giving rise to new and additional services, which are not regulated. Furthermore, the pipeline has been extended through looping and unregulated services such as “backhaul” have been offered for some time. We have observed that these “unregulated” services are being utilised just as extensively (if not to a greater extent) as the regulated service and the pricing for these services does not reflect the outcomes that would be expected in a competitive market. In this regard,

- Shell welcomes the inclusion of the westbound service in the definition of the reference service reflecting changes in gas flows. Although operationally this gas would be typically “netted off” resulting in customers being charged for services where there is no actual physical flows.
- The inclusion of a short-term firm service indicates APTPPL’s recognition of the changing pipeline utilisation levels, however, we are not convinced this service is priced appropriately and it is unclear how extensively it will be utilised by the market - the “as available” service while not “firm” provides a very similar short-term service.

Furthermore, APTPP’s suggestion that this service is priced at 166 per cent above the long-term firm value is overly high and is, in part, driven by the assumption that all users have the same load factor, which is not necessarily reflective of actual usage.

- The reference service definition should be expanded to include other services such as “as available”, “interruptible” and possibly “park and loan” services and tariffs should be realigned to reflect the level of risk borne by the pipeline and the underlying supply-demand dynamics on the RBP for the service rather than an a general uplift in the firm price.
 - o We have some concerns with APTPPL’s rationale for the relationship between the pricing of long-term and short-term firm services and this is likely to be influencing the pricing structures of other short-term services (including non-regulated services such as “as available” and “interruptible”). APTPPL suggests this is to encourage shippers to enter into long-term firm contracts (to underpin investments) short-term capacity should be priced at a premium.

In our view, this is not necessarily the case and parties with long-term contracts for gas such as a retailers and or industrial loads are still incentivised to enter into a long-term Gas Transportation Agreement (GTA) that fixes the price and terms for a number of years.

While we appreciate that a short-term firm service may be priced at a higher value to long-term firm, this reflects the level of risk borne by the pipeline in the provision of the supply of the service and the benefit of flexibility awarded to customers. This clearly does not apply to an “as available service”, which does not carry this level of risk, but is typically priced at 180 per cent to the firm service.

- If efficient market principles were applied, we would expect that the “as available” and “interruptible” services would be priced below the short-run and long-run firm prices. If, however, the current price relativities are applied in the forthcoming regulatory period, these services would be more expensive.
 - o As available” and “interruptible” are inferior services (reflecting the overall level of risk to the pipeline and the shipper regarding availability).
 - o In an efficient market, “as available” services should be priced as a function of the supply and demand for capacity at the time it is required - not the underlying contract price for long-term firm capacity. This means, at times of high demand, the price may exceed the long-term contracted price and also be priced below this level when utilisation is relatively low.
- Overall, we consider that the introduction of the day-ahead capacity auction, agreed to by the COAG Energy Council, should address some of these concerns. The value of short-term capacity will be determined through the auction (or through secondary capacity trading) and it is our expectation that pricing will be below the firm price (except in very high demand periods). According to the Gas Market Reform Package Implementation timetable, the auction is unlikely to be introduced before 2019-20. Until such time, these concerns will continue and as such they should be addressed through the forthcoming Access Agreement.

1. Rate of return

The Proposed rate of return appears high and is above those applied in other regulated sectors such as electricity, which is in part driving the tariff increase in the reference service. The Proposal includes a post-tax cost of equity of 8.40 per cent, a pre-tax cost of debt of 7.26 per cent resulting in a post-tax vanilla Weight Average Cost of Capital of 7.72 per cent.

The rates of return determined by the AER recently for the electricity networks are significantly less than APTPP’s estimate and are below 7 per cent¹. It is unclear why a high WACC is applicable to the RBP relative to other regulated infrastructure and we suggest, if accepted, the AER provides detailed reasoning behind the decision.

¹ According to the AER Rate of Return Fact Sheet – October 2015 the rates applying to recent and preliminary AER decisions range from 6.01 per cent (Energy and Ergon Energy) to 6.12 per cent (United Energy). While we note these apply to 2015-16, we would not expect these to have moved substantially from 6 per cent to 7.72 per cent in the last twelve months.