

Draft Decision

Victorian Energy Networks Corporation access arrangement revisions for the Principal Transmission System

14 August 2002

Preface

The Victorian Energy Networks Corporation (VENCorp) lodged proposed revisions to its access arrangement with the Australian Competition and Consumer Commission (the Commission) on 28 March 2002. The Commission approved this access arrangement in 1998.

This Draft Decision sets out the Commission's draft assessment of VENCORP's proposed revised access arrangement in accordance with the provisions of the *National Third Party Access Code for Natural Gas Pipeline Systems* (the Code).

Under the terms of the Code the Commission may only approve VENCORP's proposed revised access arrangement if it is satisfied that it complies with the provisions of the Code. The Code specifies that an access arrangement must contain certain elements and be consistent with a range of principles.

The Commission proposes not to approve VENCORP's proposed revised access arrangement for the PTS, which incorporates the Western Transmission System, in its current form. This Draft Decision sets out the amendments (or nature of the amendments) which would have to be made to the revisions for the Commission to approve them. The Commission will consider submissions from interested parties and amended revisions from VENCORP (if submitted) before issuing its Final Decision.

Written submissions are requested on the Draft Decision and should be received by the Commission no later than 13 September 2002.

Copies of VENCORP's proposals and related information are available from the Commission's website at www.accc.gov.au (under 'Gas').

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Abbreviations and glossary

Access arrangement	An arrangement for third party access to a 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
BOM	Bureau of Meteorology
Code	National Third Party Access Code for Natural Gas Pipeline Systems
Commission	Australian Competition and Consumer Commission
Contract carriage	A system of managing third party access whereby the service provider normally manages its ability to provide services primarily by requiring users enter into a contract that specifies a particular quantity of service
Covered pipeline	A pipeline to which the provisions of the Code apply
CPI	Consumer Price Index
GasNet	GasNet Australia (Operations) Pty Limited
GIA	Gas Industry Act
GNS	GasNet System
GPAL	Gas Pipelines Access Law
Market carriage	A capacity management system where the service provider does not normally require users to commit to a contract. Instead charges are based on actual usage
MSOR	Market System and Operations Rules
NCC	National Competition Council
NIEIR	National Institute of Economic and Industry Research
Prospective user	A person who seeks or who is reasonably likely to seek to enter into a contract for a service (including a user who seeks or may seek to enter into a contract for an additional service)

PTS	Principal Transmission 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
Reference service	A service which is specified in an access arrangement and in respect of which a reference tariff has been determined
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
Revisions commencement date	The date upon which the next revisions to the access arrangement are intended to commence
Revisions submissions date	The date upon which the service provider must submit revisions to the access arrangement
Service envelope agreement (SEA)	An agreement between VENCorp and GasNet whereby GasNet makes the Gas Transmission System available to VENCorp
Service provider	A person who is the owner or operator of the whole or any part of the pipeline or proposed pipeline
Services policy	A policy detailing the service or services to be offered
VENCorp	Victorian Energy Networks Corporation
WTS	Western Transmission System

Executive Summary

1. Introduction

The Commission is currently conducting its first scheduled review of the Victorian Energy Networks Corporation (VENCorp) access arrangement, which it approved in 1998. GasNet owns the Victorian Principal Transmission System (PTS) and Western Transmission System while VENCorp is the independent system operator for the PTS. The two service providers submitted proposed revised access arrangements and access arrangement information to the Commission on 28 March 2002. While the revisions are subject to two separate regulatory processes (see also the Commission's Draft Decision on GasNet's revisions) this document also refers in part to the proposed GasNet revisions where appropriate. In addition, VENCorp submitted in May 2002, an application for re-authorisation of the Market System and Operation Rules (MSOR).

VENCorp's proposal would largely maintain the status quo. VENCorp's proposed tariff structure is designed to provide expected real price reductions of over 10 per cent for the next access arrangement period, using a five year price path for commodity and registration tariffs. This proposed tariff structure is aimed at providing greater certainty as an aid to industry confidence and investment decisions.

In order to facilitate VENCorp's revised access arrangement, some changes are required to parts of the MSOR. These minor changes are needed to give effect to the changes in tariff design that VENCorp is proposing as part of the revisions to the access arrangement. VENCorp submitted proposed drafting of these changes with its revised access arrangement.¹

2. Key Issues

2.1 Five year tariff proposal

VENCorp released an Issues Paper in October 2001 requesting input into the review of its access arrangement for the PTS. One clear response by industry was the desire for greater certainty in respect to tariffs for gas transmission. Therefore, VENCorp has constructed forecasts covering the second access arrangement period that incorporate fixed registration and commodity tariffs for five years. The Commission will continue to review all revenues and expenses as part of its annual consultation process on its budget.

VENCorp's proposal mitigates the potential for annual fluctuations that are likely under the current annual approval process for registration and commodity tariffs. The Commission considers that the proposal has merit.

¹ VENCorp submitted to the Commission proposed changes to the MSOR as a separate document on the 28 March 2002. These changes are Attachment 1 Clauses 2.6 & 2.7 and, Attachment 2 proposed definitional changes.

2.2 LNG system security

The Commission received a number of submissions from interested parties in regards to the regulation of the system security reserve provided to VENCorp by GasNet's LNG facility. Some interested parties submitted that GasNet is in a position to exercise market power in the supply of LNG services in relation to the PTS, in particular with regard to the system security reserve. Certain provisions of the Victorian Tariff Order, under which the Commission currently regulates LNG storage, are scheduled to cease to have effect after 31 December 2002.

There are limited alternative sources of peak gas, as WUGS is not seen as a full substitute for the Dandenong reserve at this time because of factors such as slower response times and the amount of capacity likely to be available.

The majority of submissions from interested parties suggested that the Commission should continue to regulate the LNG reserve under the provisions of the Code and the *Gas Pipeline Access Law* (GPAL). However, it is uncertain whether the Commission has the power to regulate the LNG system security reserve.

2.3 Information provisions and key performance indicators

BHP Billiton argued that users take a 'bundled' service from GasNet and VENCorp, thus costs should be aggregated for both services and ENERGEX Retail submitted that GasNet and VENCorp should be compelled by the Commission to submit a combined revised access arrangement. However, the Code allows GasNet and VENCorp to make separate applications.

BHP Billiton suggested that VENCorp should benchmark its costs against NEMMCo, which has a similar role to that of VENCorp. However, against this the Energy Users Association of Australia (EUAA) and the Department of Natural Resources and the Environment (DNRE) argue that VENCorp is a unique service provider and that the governance arrangements place strong incentives on VENCorp to efficiently deliver services to industry.

The Commission considers that the cost of developing benchmark or performance indicators needs to be considered in the context of the magnitude of VENCorp's costs and potential efficiency gains as VENCorp's costs represent only 1 to 1.5 per cent of the delivered price of gas. Importantly, VENCorp's proposal is designed to provide expected real price reductions of over 10 per cent for the second access arrangement period.

Accordingly, the Commission proposes to accept VENCorp's key performance indicators at this time.

2.4 Demand forecasts

GasNet and VENCorp have arrived at different demand forecasts for the second access arrangement period. Both GasNet and VENCorp use the demand forecasts from VENCorp's Annual Planning Review (APR) in 2001, however GasNet has made an additional adjustment for greenhouse and 'urban heat island' effect.

The difference is not significant in the context of total expected gas demand and uncertainty in forecasting. However, the view expressed by the majority of interested parties is that the forecast volumes should be the same across the two access arrangements. The Commission

supports this view. It prefers that multiple service providers adopt a consistent approach when proposing revised access arrangements.

As this has not occurred, the Commission has assessed the approach of both GasNet and VENCORP. VENCORP's APR forecasts have formed a sound basis for the demand forecasts that will be used to derive the tariffs to apply for the second access arrangement period. However, GasNet commissioned a report by the CSIRO that supports a comparatively small adjustment to these estimates that VENCORP considers is not material.

On balance, the Commission proposed to accept GasNet's demand forecasts. Accordingly, it has proposed an amendment to VENCORP's access arrangement. However it will consider further submissions before making its Final Decision.

3. Conclusion

A number of outstanding issues relating to both the GasNet and VENCORP proposed revised access arrangements need to be addressed prior to the release of the Final Decision. There are changes required in GasNet's revised access arrangement, in regards to its services policy, that need to be changed for VENCORP's revised access arrangement to be approved. Other issues for VENCORP include prudent discounts and its services policy. These issues are discussed further in the body of this report.

4. Draft Decision

Pursuant to section 2.35(b) of the Code, the Commission proposes not to approve VENCORP's proposed revised access arrangement in its current form. This Draft Decision sets out the amendments (or nature of the amendments) which would have to be made to VENCORP's proposed revised access arrangement for the Commission to approve them. The Commission will consider submissions from interested parties and amended revisions from VENCORP (if submitted) before issuing its Final Decision.

5. Proposed amendments

Proposed amendment 1

VENCORP must remove the fifth dot point of clause 5.2.2 (a) (i) that provides for VENCORP to introduce a new commodity tariff in the form of a prudent discount.

Proposed amendment 2

VENCORP must amend its total annual demand forecasts in Table 23 and Table 24 of its revised access arrangement information so that they are consistent with those proposed in section 7 of GasNet's revised access arrangement information.

Proposed amendment 3

VENCORP must clarify Clause 5.1.1 of its revised access arrangement that VENCORP provides to users, not only VENCORP Reference Services, but also the transportation of gas through the PTS via the Market Carriage system under the MSOR.

1. Introduction

1.1 Access arrangement revisions

In accordance with the provisions of its access arrangements, the Victorian Energy Networks Corporation (VENCorp) submitted a proposed revised access arrangement and revised access arrangement information to the Commission on 28 March 2002 and also submitted an application for MSOR re-authorisation on 17 May 2002.

Under the market carriage capacity management system operating in Victoria, users pay tariffs to both the independent system operator, VENCorp and to GasNet, the system owner. Approximately 15 per cent of the total tariffs are paid to VENCorp. GasNet has also submitted a proposed revised access arrangement to the Commission that is the subject of a separate approval process.

An access arrangement describes the terms and conditions on which a service provider will make access available to third parties. The initial access arrangement period ends on 31 December 2002. The second access arrangement period is scheduled to commence on 1 January 2003 and is proposed to end on 31 December 2007. However, service providers have the discretion to submit revisions earlier than a scheduled review.

Under the Code, the Commission is required to:

- inform interested parties that it has received the proposed revisions to the access arrangements and the associated access arrangement information (parties were notified by letter on 5 April 2002);
- publish a notice in a national daily paper which at least; describes the covered pipelines to which the access arrangements relate; states how copies of the documents may be obtained; and requests submissions by a date specified in the notice (the notice was inserted in the *Australian Financial Review* and the *Age* on 8 April 2002). The Commission also released an Issues Paper on 17 April 2002.
- after considering submissions received, issue a Draft Decision which either proposes to approve the revisions or proposes not to approve the revisions and states the amendments (or nature of the amendments) which would have to be made to the revisions in order for the Commission to approve them;
- after considering additional submissions, issue a Final Decision that either approves or does not approve the revisions (or amended revisions) and states the amendments (or nature of the amendments) which have to be made to the revisions (or amended revisions) in order for the Commission to approve them; and
- if the amendments are satisfactorily incorporated in amended revisions, issue a *Final Approval*. If the Commission is satisfied that the amended revisions either substantially incorporate the amendments specified or otherwise address to its satisfaction the matters which led it specifying the amendments in its Final Decision, it must either approve or not approve the amended revisions. In any other case, the Commission must draft and approve its own revisions.

1.2 Criteria for assessing revisions to access arrangements

The Commission may approve revisions to an access arrangement only if it is satisfied that the access arrangement as revised contains the elements and would satisfy the principles set out in sections 3.1 to 3.20 of the Code, which are summarised below. Revisions to an access arrangement cannot be opposed solely on the basis that the access arrangement as revised would not address a matter that section 3 of the Code does not require it to address. Subject to this, the Commission has a broad discretion in accepting or opposing revisions to an access arrangement.

An access arrangement, or a revised access arrangement, must include the following elements:

- a policy on the service or services to be offered which includes a description of the service(s) to be offered;
- a reference tariff policy and one or more reference tariffs. A reference tariff operates as a benchmark tariff for a particular service and provides users with a right of access to the specific service at the specific tariff. Tariffs must be determined according to the reference tariff principles in section 8 of the Code;
- terms and conditions on which the service provider will supply each reference service;
- a statement of whether a contract carriage or market carriage capacity management policy is applicable;
- a trading policy that enables a user to trade its right to obtain a service (on a contract carriage pipeline) to another person;
- a queuing policy to determine users' priorities in obtaining access to spare and developable capacity on a pipeline;
- an extensions/expansions policy to determine the treatment of an extension or expansion of a pipeline under the Code;
- a date by which revisions to the arrangement must be submitted; and
- a date by which the revisions are intended to commence.

The Code (section 10.2) provides that, where there is more than one service provider in connection with a covered pipeline, with one the owner and the other the operator, responsibility for complying with the obligations imposed by the Code is allocated among them by their access arrangement(s) and each service provider is responsible for complying with the responsibilities allocated to it.

In considering whether a revised access arrangement complies with the Code, the Commission must take into account the provisions of the access arrangement as it currently stands and, pursuant to section 2.24 of the Code, the following factors:

- the legitimate business interests and investment of the service provider;
- firm and binding contractual obligations of the service provider or other persons (or both) already using the covered pipeline;

- the operational and technical requirements necessary for the safe and reliable operation of the covered pipeline;
- the economically efficient operation of the covered pipeline;
- the public interest, including the public interest in having competition in markets (whether or not in Australia);
- the interests of users and prospective users; and
- any other matters that the Commission considers are relevant.

Appendix C to this Draft Decision sets out the access arrangement information that a service provider must disclose to interested parties (Attachment A to the Code).

1.3 Public consultation

Interested parties are invited to make written submissions to the Commission on its Draft Decision by Friday 13 September 2002. In addition, if requested and time permits, a public forum will be held on the issues raised in this decision and the Commission's proposed approach. After considering further submissions, the Commission will issue its Final Decision.

Submissions are made available from the Commission's website (www.accc.gov.au). They are also placed on the public registers held by the Commission and the Code Registrar. Submissions should be supplied in electronic format compatible with Microsoft Word to the review e-mail address below. In addition, one original signed document should be mailed to the postal address below. Any information considered to be of a confidential nature should be clearly marked as such, and the reasons for seeking confidentiality should be provided. Under the terms of the Code, the Commission must not disclose such information unless it is of the opinion that disclosure would not be unduly harmful to the legitimate business interests of the service provider, a user or prospective user.

The Commission's e-mail address for this review is victoriangasreview@acc.gov.au. Hard copies of submissions should be forwarded to:

Ms Kanwaljit Kaur
General Manager
Regulatory Affairs – Gas
Australian Competition and Consumer Commission
PO Box 1199
Dickson ACT 2602

Copies of the revisions applications and associated documents are available from the Commission's website. Copies of this Draft Decision may also be obtained from the Commission by contacting Ms Rebecca Khair telephone (02) 6243 1233, fax (02) 6243 1205, e-mail rebecca.khair@acc.gov.au. Copies of the revisions applications on computer disk can also be obtained from Ms Khair.

Any other inquiries should be directed to Mr Luke Griffin on (02) 6243 1059.

2. Background

The PTS and the WTS were both owned by the Victorian Government entities Transmission Pipelines Australia Pty Ltd and Transmission Pipelines Australia (Assets) Pty Ltd at the time the Commission approved the PTS and the WTS access arrangements in 1998. Ownership of these pipelines subsequently passed to GPU GasNet Pty Ltd and then to GasNet Australia (Operations) Pty Ltd (GasNet). VENCORP remains the independent system operator of the PTS.

The Victorian Government enacted the Gas Pipelines Access (Victoria) Law, effective 1 July 1997, which brought the *National Third Party Access Code for Natural Gas Pipeline Systems* (the Code) into force in Victoria (though certain provisions of the Victorian Code were grandfathered until the first scheduled review).

2.1 Victorian gas industry structure and regulatory framework

Relevant aspects of the Victorian gas industry structure include:

- GasNet owns the PTS in Victoria, which until recently solely transported gas supplied from the Esso-BHP Billiton fields in the Gippsland Basin. VENCORP is the independent system operator of the PTS. The recent completion of the Interconnect Pipeline and the Southwest Pipeline also allows Cooper Basin and Otway Basin gas to be supplied via the PTS;
- GasNet also owns the Western Transmission System (WTS), which until recently solely transported gas, supplied from the on shore Otway Basin gas fields. Since completion of the Southwest Pipeline, Gippsland Basin gas has been supplied via the WTS. The TXU owned Western Underground Storage (WUGS) facility provides a source of peak gas flows via the Southwest Pipeline. GasNet proposed that the WTS and the Southwest Pipeline be included from the start of the second access arrangement period in a single access arrangement for the PTS;
- since July 1998 the Interconnect Pipeline has linked the PTS with the Moomba to Sydney Pipeline (MSP) which is operated by East Australian Pipeline Ltd (EAPL). This section of the Interconnect Pipeline from Barnawartha to Culcairn forms part of the PTS, and is owned by GasNet, and operated VENCORP. EAPL owns and operates the remainder of the Interconnect from Culcairn to Wagga Wagga. It allows southward flows of gas supplied by the Cooper Basin producers to Victoria and northward flows of Gippsland Basin gas to NSW;
- Duke Energy International (DEI) owns and operates the Eastern Gas Pipeline (EGP) which commenced operations supplying Gippsland Basin gas to customers in NSW in 2000. In 2002, DEI commenced construction of a pipeline that will deliver Gippsland Basin gas to Tasmania; and
- a number of new gas sources, located primarily in the Otway Basin, are expected to commence supply to the GasNet system and to SA customers in the short to medium term.

The main legislation and relevant documents regulating access to the Victorian gas transmission industry are:

- the Code, under which transmission service providers are required to submit access arrangements and revised access arrangements to the Commission for approval;
- the *Gas Pipelines Access (South Australia) Act 1997*; and
- the *Gas Pipelines Access (Victoria) Act 1998*.

In addition, certain provisions of the Victorian Code under which the Commission approved the PTS access arrangement in December 1998 have been grandfathered. Sub-section 24A(3) of the Gas Industry Acts (Amendment) Act 1998 provides that access arrangements approved under the Victorian Code (such as the access arrangements for the PTS and WTS) continue to be subject to sections 3 and 8, and 9 (so far as it applies to sections 3 and 8) and to sections 2.33 and 2.48A of the Victorian Code.

These sections are not subject to the corresponding provisions of the Code until the first scheduled review of the access arrangements under section 2 of the Code. The convention has been adopted in this Issues Paper of identifying relevant Victorian Code provisions where they differ from current provisions of the Code.

The Code and appeals bodies in Victoria with respect to transmission pipelines are:

- the Commission – regulator and arbitrator;
- the National Competition Council – Code advisory body;
- the Commonwealth Minister – coverage decision maker;
- the Federal Court – judicial review; and
- the Australian Competition Tribunal – administrative appeal.

Reflecting institutional arrangements imposed by the Victorian Government at the time of its reform and privatisation of the formerly Government owned integrated gas supply business in 1998 and 1999, parts of a number of regulatory instruments are currently included in the access arrangements. As noted earlier, while GasNet owns the PTS and the WTS, the Victorian Government gave VENCORP the role of independent system operator for the PTS. Under the terms of the Code, both GasNet and VENCORP are service providers. Their access arrangements allocate responsibility between them for complying with the obligations imposed by the Code.

2.2 The initial access arrangement assessment

On 16 December 1998, the Commission approved the following Victorian gas transmission access arrangements under provisions of the Victorian Code with initial access arrangement periods ending on 31 December 2002:

- access arrangement by Transmission Pipelines Australia Pty Ltd and Transmission Pipelines Australia (Assets) Pty Ltd for the Principal Transmission System (PTS);

- access arrangement by Transmission Pipelines Australia Pty Ltd and Transmission Pipelines Australia (Assets) Pty Ltd for the Western Transmission System (WTS);
- access arrangement by Victorian Energy Networks Corporation (VENCorp) for the PTS.

2.3 Issues common to VENCorp and GasNet

This section outlines the key issues that have been raised by interested parties that are common to VENCorp and GasNet.

2.3.1 LNG system security

The role of the LNG system security reserve is to allow the maintenance of adequate system pressures in the event of a major emergency requiring complete shutdown of the system so that customer load can be disconnected safely. VENCorp currently pays GasNet \$1.4 million a year for LNG storage under the Victorian tariff order. In turn, VENCorp charges users through a commodity based tariff. Provisions under which the Commission currently regulates LNG storage for system security purposes are scheduled to cease to have effect after 31 December 2002.

Interested parties submitted that GasNet may be in a position to exercise market power in the market for the supply of LNG services, in particular, via the system security reserve. This is of concern to users because VENCorp passes through the cost incurred in the contract of reserving storage space of 3000 tonnes in GasNet's LNG facility. Accordingly, as part of its Draft Decision for GasNet the Commission has considered suggestions that it continue to regulate these services in terms of the provisions of the Code and the Gas Pipeline Access Law (GPAL).

Section 2.3.2 of the Commission's Draft Decision for GasNet's revised access arrangement outlines the Commission's consideration of this matter. The Commission does not propose to regulate the LNG system security reserve once the relevant provisions of the Tariff Order cease to have effect.

2.3.2 Demand forecasts

Demand forecasts represent a critical element in most access arrangements. The relevance of reasonable demand forecasts is that a service provider will earn greater (less) than forecast revenue if actual demand is greater (less) than that forecast. The service provider therefore has a strong incentive to understate forecasts in order to be able exceed them.

GasNet and VENCorp have based their demand forecasts on those published in the VENCorp Annual Planning Review (APR). However, GasNet has adjusted these estimates to account for a warming trend in Melbourne which it says arises from a combination of enhanced greenhouse effect and an urban heat island effect. There is a preference by interested parties for VENCorp's forecasts to be adopted for both proposed revised access arrangements.

VENCorp's demand forecast volumes were based upon independent econometric analysis by the National Institute of Economic and Industry Research (NIEIR). However, the Commission notes that the Essential Services Commission (ESC) has proposed to accept demand projections from three Victorian gas distribution businesses' access arrangements, which are consistent with GasNet's approach.

The Commission's preference is for multiple service providers to adopt a consistent approach. The Commission considers that the VENCORP APR forecasts have been determined through a transparent process involving public consultation, and form a sound basis for the demand forecast that will be used to derive the tariffs to apply for the second access arrangement period. However, the Commission notes that the CSIRO report commissioned by GasNet supports a comparatively small adjustment to these estimates, and that VENCORP considers the differences immaterial. Further, GasNet submits that no credible critique has been provided of the CSIRO report.

On balance, the Commission proposes to accept GasNet's demand forecasts. Accordingly, it has proposed an amendment to VENCORP's access arrangement.

2.3.3 Services policy

Sections 3.1 and 3.2 of the Code requires an access arrangement to include a policy on the service or services that the service provider will make available to users or prospective users.

VENCORP has outlined the reference services it will provide to users or prospective users of the PTS in section 5.2 of its proposed revised access arrangement. However, VENCORP's ability to provide its reference services is dependent upon GasNet making the PTS available to operate in accordance with the MSOR. Despite sections 3.1 and 3.2 of the Code, GasNet has proposed not to include a reference service in its revised access arrangement.

The view of many interested parties is that there needs to be certainty as to the relationship between GasNet and VENCORP over who provides services for the PTS. Section 11.1.5 of the Commission's Draft Decision for GasNet's revised access arrangement requires GasNet to amend its revised access arrangement to include a reference service for the services it provides to VENCORP. Also, VENCORP's proposed revised access arrangement does not acknowledge that it is the entity that supplies the whole service to retailers. Accordingly, the Commission requires VENCORP to make an amendment to clarify that it is VENCORP that provides to users, not only VENCORP reference services, but also the transportation of gas through the PTS via the Market Carriage system under the MSOR.

3. Reference tariffs

3.1 Reference tariff policy

3.1.1 Code requirements

Section 3.3 of the Code specifies the reference tariff elements that an access arrangement must include:

An Access Arrangement must include a Reference Tariff for:

- (a) at least one Service that is likely to be sought by a significant part of the market; and
- (b) each Service that is likely to be sought by a significant part of the market and for which the Relevant Regulator considers a Reference Tariff should be included.

Further, the Code outlines the requirement of an access arrangement to include a policy describing the principles that are to be used to determine a reference tariff. Section 3.5 states:

An Access Arrangement must also include a policy describing the principles that are to be used to determine a Reference Tariff (a Reference Tariff Policy). A Reference Tariff Policy must, in the Relevant Regulator's opinion, comply with the Reference Tariff Principles described in section 8.

Section 8.1 of the Code sets out the objectives that a reference tariff and reference tariff policy should be designed to achieve. Subject to these requirements, section 8.3 states the form of regulation in which a reference tariff may vary within an access arrangement period, though implementation of the reference tariff policy is within the discretion of the service provider.

For example, a reference tariff may be designed on the basis of:

- (a) a "price path" approach, whereby a series of Reference Tariffs are determined in advance for the Access Arrangement Period to follow a path that is forecast to deliver a revenue stream calculated consistently with the principles in this section 8, but is not adjusted to account for subsequent events until the commencement of the next Access Arrangement Period;
- (b) a "cost of service" approach, whereby the Tariff is set on the basis of the anticipated costs of providing the Reference Service and is adjusted continuously in light of actual outcomes (such as sales volumes and actual costs) to ensure that the Tariff recovers the actual costs of providing the Service; or
- (c) variations or combinations of these approaches.

3.1.2 VENCORP'S PROPOSAL

VENCORP'S reference tariff policy provides for a combination of 'price path' and 'cost of service' approaches consistent with section 8.3(c) of the Code. VENCORP proposes to apply charges to market participants for its services. These are information services, market and system operational services, meter data management services and a system security service.

VENCorp proposes that the recovery of costs associated with information and market and system operational services will be on a cost recovery basis over the access arrangement period.² Derivation of the cost of each reference service is described in Table 3.1.

Table 3.1: VENCorp’s cost structure for determining its Reference Services

Reference Service	Reference Tariff	How is the cost of the service derived	How is the Tariff applied
Information Services	Registration Tariff	Fixed costs associated with provision of Information Services. ³	Fixed Tariff of \$/day/Registered Market Participant
Market and System Operational Services	Tariff V	Based upon historical demand and scenario analysis, 70 per cent of common costs are allocated to Tariff V. ⁴	A flat rate for each GJ withdrawn daily for low-use customers.
	Tariff D	Based upon historical demand and scenario analysis, 30 per cent of common costs are allocated to Tariff D. ⁵	A flat rate for each GJ withdrawn daily for high-use customers.
Meter Data Management Services	Meter Data Management Tariffs	Direct recovery, on a per meter basis, of an allocation of VENCorp’s meter data handling costs between transmission and distribution meters. ⁶	A fixed \$ per day for each delivery point, both transmission and distribution for which metering data is managed by VENCorp.
System Security Service	System Security Tariffs	Pass through of external costs incurred through the contracted costs of reserving storage space of 3000 tonnes in GasNet’s LNG facility. ⁷	A fixed \$ per GJ for the 2002/03 financial year.

Source: VENCorp Access Arrangement Information 28 March 2002 p.6-13

To calculate tariffs, VENCorp’s forecast expenditures are divided by its gas demand forecasts (see Table 3.3) to derive the initial tariffs, that are either \$/participant, \$/meter or \$/GJ.

Table 3.2 sets out the initial tariffs proposed by VENCorp.

² VENCorp Access Arrangement 28 March 2002, p.9

³ VENCorp Access Arrangement Information 28 March 2002, p.10

⁴ VENCorp Access Arrangement Information 28 March 2002, p.9

⁵ Both Tariff V and D are structured so as to comply with section 8.1 (d) of the Code that states a Reference Tariff and Reference Tariff Policy should be designed with the view of not distorting investment decisions in Pipeline transportation systems or in upstream or downstream industries. As such, high-use customers are charged a lower average \$/GJ than low use customers.

⁶ VENCorp Access Arrangement Information 28 March 2002, p.10

⁷ The amount charged by GasNet to VENCorp is regulated under a Victorian Governments Tariff Order at \$1.4 million per annum until 31 December 2002.

Table 3.2: Initial settings of VENCORP reference tariffs

Description of Tariff	Initial Tariff (GST exclusive)	Initial Period
Registration Tariff	\$30/day/registered market participant	5 years
Tariff D Commodity Tariff	\$0.03248/GJ	5 years
Tariff V Commodity Tariff	\$0.08055/GJ	5 years
Transmission Meter Data Management Tariff	\$7.00/day/meter	6 months to 30 June 2003
Distribution Meter Data Management Tariff	\$2.62965/day/meter	6 months to 30 June 2003
LNG System Security Tariff	\$0.00751/GJ	6 months to 30 June 2003

Source: VENCORP Access Arrangement Information 28 March 2002, p 5

Referring to the detail in Table 3.2, VENCORP states that the registration of market participants carries with it administrative costs associated with the provision of a range of information services desired by those participants and provided by VENCORP irrespective of their level of market activity. Further, VENCORP states that the registration tariff has been set at a level that it believes is consistent with other similar services such as NEMMCO registration fees.⁸

VENCORP proposes that commodity tariff's D and V remain fixed through the access arrangement period. VENCORP's commodity tariffs recover costs not allocated to its registration, meter data management and system security services. These costs are related to the integrated operation of the PTS and a market, and are detailed in Table 2 of VENCORP's proposed revised access arrangement.

The proposed commodity tariffs are not uniform, in that 70 per cent of common costs are allocated to Tariff V and 30 per cent to Tariff D. VENCORP aims to allocate its common costs as efficiently as possible. That is, it aims to achieve fairness and equity in its tariff structure across a range of different customer types. It does this by using the actual cost of delivered gas as a proxy for willingness to pay.⁹ Therefore, the commodity tariffs are structured so that where charges are required to be greater in a market segment, then this occurs in a segment with low price elasticity so as to minimise distortion in usage and investment. It is on this basis that Tariff V customers pay more than Tariff D. VENCORP states that;¹⁰

...this approach is consistent with Ramsey pricing principles. However, the approach was not derived nor based on any objective to apply Ramsey pricing principles. As such, a generic critique of Ramsey pricing principles is unlikely to be relevant in the context of VENCORP's proposed Tariff V and Tariff D commodity tariffs

Transmission meter tariffs reflect an estimation of the cost of VENCORP's in-house meter data function. VENCORP states that this function includes collection, processing and storage of meter data from transmission supply point meters. VENCORP argues that it is highly problematic to attempt any true cost reflective pricing for this service. Therefore VENCORP

⁸ VENCORP Access Arrangement Information 28 March 2002, p.10

⁹ VENCORP Access Arrangement Information 28 March 2002, p.9

¹⁰ VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.9

charges are based on an estimation of the costs associated with providing this service. The distribution metering tariff reflects the external costs associated with providing the reference service. This service is contracted through a competitive tender process, where as the transmission meter service is an estimation of its own in-house meter data agent function.

VENCorp outlines that the LNG system security tariff reflects the charge by GasNet to VENCorp for the provision of this service. Under the tariff order the charge is capped at \$1.4 million until 31 December 2002 when the cap expires.¹¹

3.1.3 Submissions

Submissions received were in relation to VENCorp's cost allocation methodology, LNG storage for system security, prudent discounts and a new customer class in the Victorian market know as Tariff M. Submissions relating to each issue are noted in turn below.

Cost allocation methodology

VENCorp states that its principles for cost allocation balances cost reflectivity against complexity and the cost effectiveness of being able to identify, set and levy cost reflective tariffs to users. Further, VENCorp argues that the separation of its costs from those of GasNet's ensures a considerable element of cost transparency by an evident separation of the costs and charges for these two primary services.

VENCorp released a paper entitled *Review of Access Arrangements for the Principal Transmission System - Issues Paper* on 23 October 2001 This paper sought input from interested parties on a range of matters in regard to its revised access arrangement prior to finalising revisions to be submitted to the Commission. The paper also set out the process that VENCorp proposed to follow in preparing and finalising revisions to its access arrangement.

According to VENCorp, most respondents agreed that the current reference services description adequately represented VENCorp's role in gas. Many were supportive of the current range and definition of the services provided by VENCorp.¹² In a submission received by the Commission, Origin Energy stated its support for VENCorp's proposed cost allocation methodology and made the general point that the application of the Ramsey pricing principles is acceptable in regard to VENCorp's cost allocation under the requirements of the Code.¹³

LNG storage for system security purposes

As discussed in chapter two, a number of interested parties submitted that GasNet is in a position to exercise market power in the supply of LNG services in relation to the PTS, in particular, with regard to the system security reserve. Section 2.3.2 of the Commission's Draft Decision for GasNet's revised access arrangement outlines the Commission's consideration of this matter. The Commission does not propose to regulate the LNG system security reserve once the relevant provisions of the Tariff Order cease to have effect.

¹¹ VENCorp Access Arrangement Information 28 March 2002, p.42-43

¹² VENCorp Review of Access Arrangements for the PTS – Issues Paper 23 October 2001, p.1-8

¹³ Origin Energy submission 17 May 2002, p.10

Prudent discounts

While VENCORP proposed clause 5.2.2 (a) (i) in its access arrangement that allows it to introduce a prudent discount, it believes that in the first instance, GasNet alone should offer prudent discounts. However, VENCORP has stated that it will consider prudent discounting and has provided for this in its proposed access arrangement.¹⁴ VENCORP believes that the following matters should be considered in deciding the extent of any prudent discount to be offered by VENCORP:¹⁵

1. VENCORP's tariff policy in its proposed access arrangement enables VENCORP to consider prudent discounting on a case-by-case basis, but it should be noted that in doing so, VENCORP may be required to seek a revision of its access arrangement under section 2 of the Access Code;
2. The best way of achieving prudent discounting is for GasNet to seek the full prudent discount. To the extent that GasNet is able to offer, and takes responsibility for deriving, prudent discounts that (in conjunction with non-discounted published VENCORP and other charges) will encourage continued or new consumption, then it should do so to the full extent. Advantages of this approach include:
 - a. This approach is consistent with GasNet having the commercial relationship with users, particularly in relation to extensions and expansions of the PTS;
 - b. Implementation by one Service Provider is likely to be more efficient and easier for users to understand;
 - c. From GasNet's perspective, it should be indifferent in this matter. GasNet will be kept whole as it will recover any shortfall in revenue from other users;
 - c. The outcome for other users is likely to be materially the same regardless of whether GasNet offers the full prudent discount or whether GasNet offers a prudent discount in conjunction with VENCORP;
3. VENCORP concurs with the Commission's observation that "in practice, as the VENCORP reference tariff makes up a comparatively small part of the combined charge, VENCORP may not in itself have the capacity to offer a sufficient discount"; and
4. VENCORP believes that there is little justification for providing different charging structures for its reference services given the nature of the benefits provided by such to users.

ENERGEX Retail believes that the cost of prudent discounts should be the responsibility of the decision maker (such as GasNet or VENCORP). ENERGEX Retail is not convinced that customers generally should finance these discounts and proposes that GasNet be fully accountable for these costs.¹⁶

Origin Energy requested that the Commission recognise the benefits of avoided bypass to all users of the system by addressing the \$/GJ rate put forward by VENCORP. The operating tariffs should be adequately discounted to reflect the system wide benefits to users.¹⁷

¹⁴ VENCORP Access Arrangement 28 March 2002, p.10

¹⁵ VENCORP Submission to ACCC on Access Arrangement Issues paper, 13 May 2002, p.7

¹⁶ ENERGEX Retail submission 9 May 2002, p.2

¹⁷ Origin Energy submission 17 May 2002, p.10

Tariff M

ENERGEX Retail notes that the Essential Services Commission (ESC) had recently released the access arrangement proposals for the three incumbent Distributors in Victoria. The access arrangement proposals contain a new tariff called Tariff M, proposed by TXU, that replaces their existing Tariff D for some customers. ENERGEX Retail believes that, if accepted by the ESC, this will conflict with VENCORP's proposed commodity charges.¹⁸

VENCORP believes that it does not need to change to its revised access arrangement to accommodate the new distribution Tariff M proposed by TXU for its distribution tariffs. VENCORP stated that its proposed tariff mechanism enables a distributor to stipulate to VENCORP whether a customer is to be classified as transmission Tariff V or D, for the purpose of applying GasNet and VENCORP transmission charges, and failing such stipulation, creates a default mechanism to allocate the correct category based upon volume.¹⁹

3.1.4 Commission's considerations

The Commission's Final Decision for VENCORP's access arrangement in October 1998 concluded that, given the then structure of VENCORP and that no historical data were available for its operations, tariffs that would more accurately reflect users' costs were not technically feasible at that time.²⁰

VENCORP's proposed revised access arrangement essentially maintains the same reference tariff policy and cost structure in determining its charges for the second access arrangement period.

Cost allocation methodology

VENCORP's revenue comprises approximately 15 per cent of total PTS revenue. VENCORP's costs are allocated to four different tariff categories (six individual tariffs) as discussed below.

Registration tariff

In setting the registration tariff, VENCORP has identified administrative and other costs associated with the provision of a range of information services. These costs are largely fixed in that they are related to VENCORP's communication infrastructure, for example its market information bulletin board and web site. Much of this infrastructure is used to communicate operational and market information and VENCORP does not disaggregate between different customer types for the provision of this service. As such, the Commission considers it appropriate that customers are allocated a proportion of these fixed costs, and that on balance, VENCORP's approach derives a registration tariff that reflects the need to balance cost recovery against minimising barriers to entry for certain market segments.

Data meter management tariffs (distribution and transmission)

Costs incurred by VENCORP in retrieving, processing and storing transmission meter data are greater than would be the case if VENCORP performed the same function for distribution. This is because there are only 200 (approximately) transmission data meters thereby reducing

¹⁸ ENERGEX Retail submission 9 May 2002, p.7

¹⁹ VENCORP email to Commission staff 11 July 2002, p.4

²⁰ Commission's Final Decision 6 October 1998, p.114

the economies of scale, there are larger quantities and a broader range of data required of transmission meters, and finally, transmission meters are read twice every hour as opposed to daily for distribution.

In addition, due to the overlap between transmission meter data management and VENCORP's role in system security scheduling and wholesale market settlement, the transmission meter data management tariff is not purely cost reflective. A portion of the cost associated with transmission meter data management is allocated to the common cost pool and therefore recovered through the commodity tariffs. The Commission accepts VENCORP's statement that any truly cost reflective tariff for this service would be highly problematic, and agrees that it is nevertheless appropriate to have a price signal to reflect the costs incurred in providing the service. The Commission notes that this tariff has not changed in nominal terms since it was introduced at market commencement, and considers it appropriate to continue to charge a flat rate of \$7/meter/day.

In relation to the distribution meter data management tariff, the Commission considers that the competitive tender process undertaken by VENCORP to have data collected, processed and stored for its 900 distribution supply point meters, is likely to result in an efficient, cost reflective tariff. The Commission notes that this tariff has increased in nominal terms since VENCORP's estimate in 1998, but has increased at a lesser rate than inflation over the period.

System security tariff

The system security service is the means by which VENCORP ensures the ultimate security of the transmission system and public safety in the event of a major interruption of supply or transportation capability. The initial setting of the system security tariff was based on VENCORP's contracted position with GasNet for use of its LNG facility over the period 1 January 2003 to 31 May 2004.²¹ VENCORP recovers these costs through a single tariff per GJ on all users, on the basis that all users receive benefit from the facility in proportion to their use of the pipeline system.

The Commission considers it appropriate that VENCORP continue to pass through to users the external cost incurred in providing this service. The Commission also considers it appropriate that the tariff be levied in the manner proposed by VENCORP which is consistent with that used during the initial access arrangement period.

Commodity tariffs

Costs not allocated to VENCORP's information, meter data management, and system security services, are allocated to its market and system operational service. These costs relate to VENCORP's statutory functions that include:

- coordinating the interaction of gas production, gas storage, transmission pipelines and supply facilities;
- development and management of emergency preparedness; and
- operating and administering a market for the purpose of directing the operation of the PTS and facilitating trading arrangements.

²¹ VENCORP Access Arrangement Information 28 March 2002, p.13

VENCorp proposes to continue to recover costs for these services through commodity tariffs allocated between Tariff D and Tariff V withdrawals. VENCORP's rationale for this structure is that where charges are required to significantly exceed its guideline of 1 to 1.5 per cent of total delivered gas for a particular customer, then this occurs in market segments that exhibit price inelasticity. That is, in general, high use customers are levied a lower average dollar per GJ rate than low use customers.²²

The Commission understands that the commodity tariffs are not always cost reflective in that users of the transmission system also use other components of the market such as gas production, storage or supply in different proportions. However, the Commission received submissions in support of VENCORP's cost allocation methodology, and did not receive any submissions that suggested an alternative cost allocation method.²³ The Commission considers that it is appropriate for VENCORP to continue to use its cost allocation methodology with respect to the commodity tariffs for the second access arrangement period.

In conclusion, the Commission considers that in allocating its costs and setting reference tariffs, VENCORP's proposal strikes an appropriate balance between cost reflectivity, simplicity and not distorting investment, in accordance with the requirements of the Code. Therefore the Commission proposes to accept VENCORP's proposed cost allocation methodology.

Prudent discounts

VENCORP's cost of service pricing policy reflects that it is a non-profit organisation. Therefore, VENCORP does not have the ability to absorb the cost of prudent discounts through its profit. By default, the cost of any prudent discounts would be passed on to other users, irrespective of regulatory approval.

In VENCORP's proposed revised access arrangement, it acknowledges that it may be required to seek a revision of its access arrangement under section 2 of the Code before it can legally recover the cost of such discounts from other users. The Commission concurs with VENCORP's analysis and considers that, as it stands, such a prudent discount would require a full review under section 2 of the Code. The Commission considers that it would be inappropriate for VENCORP to offer such a prudent discount prior to regulatory approval under section 2 of the Code. Accordingly the Commission proposes the following amendment to VENCORP's proposed revised access arrangement. Also, section 8.1.5 of the Commission's Draft Decision for GasNet proposes an amendment to GasNet's revised access arrangement in relation to prudent discounts.

Proposed amendment 1

VENCORP must remove the fifth dot point of clause 5.2.2 (a) (i) that provides for VENCORP to introduce a new commodity tariff in the form of a prudent discount.

²² VENCORP Access Arrangement Information 28 March 2002, p.6

²³ The Commission notes that as part of VENCORP's own consultation, industry requested that VENCORP revisit the split between Tariff D and Tariff V. VENCORP has done this and presented its analysis in section 2.7 of the access arrangement information. The conclusion however, is that the status quo is most appropriate.

3.1.5 VENCORP'S COMPLIANCE WITH SECTIONS 8.1 AND 8.2 OF THE CODE

An appraisal of VENCORP'S compliance with sections 8.1 and 8.2 of the Code needs to be considered in conjunction with GasNet'S revised access arrangement, given the allocation of responsibility between them for complying with the Code, and that this is usually done by one service provider.

As noted in section 1.2 of this Draft Decision, pursuant to section 2.46 of the Code, the regulator must also take the factors set out in section 2.24 and the provisions of the access arrangement into account when assessing proposed revisions to an access arrangement. The Commission has given due consideration to each of these factors in assessing VENCORP'S proposed reference tariff and reference tariff policy (and the other elements set out in sections 3.1 to 3.20 of the Code).

Section 8.1 (a) providing the Service Provider with the opportunity to earn a stream of revenue that recovers the efficient costs of delivering its Reference Services over the expected life of the assets used in delivering that Service.

VENCORP operates on a cost recovery basis, making no allowance for profit. The Commission considers that the high degree of transparency required with respect to VENCORP'S operations mitigates inefficient costs. Following analysis of VENCORP'S tariff modelling, the Commission considers that VENCORP'S proposal provides it with the opportunity to recover efficient costs associated with providing its services. As such, the Commission considers that VENCORP'S proposal complies with section 8.1 (a) of the Code. The Commission will continue to review VENCORP'S annual budgets and reference tariffs and encourage greater efficiency wherever possible.

Section 8.1 (b) replicating the outcome of a competitive market

VENCORP aims to replicate the outcome of a competitive market by earning revenue that is sufficient to recover efficient costs and by allocating its charges such that they reflect the benefit provided to users. The Commission considers that VENCORP'S proposal complies with section 8.1 (b) of the Code.

Section 8.1 (c) ensuring safe and reliable operation of the Pipeline

The safety and reliable operation of the Pipeline is a statutory obligation placed upon VENCORP under chapter 6 of the MSOR and the Gas Industry Act in addition to the Code. As VENCORP'S proposed revenue includes funding for the safe and reliable operation of the transmission pipeline, the Commission considers that VENCORP'S proposal complies with section 8.1 (c) of the Code.

Section 8.1 (d) not distorting investment decisions in Pipeline transportation systems of in upstream and downstream industries

VENCORP'S charges reflect the costs incurred in the efficient operation of the gas market. VENCORP has designed its tariffs such that they are not likely to distort investment decisions in upstream or downstream industries. This has been done through three key aspects of its proposal. First, through the Tariff D and Tariff V split in which higher charges are levied on customer groups that exhibit price inelasticity. Second, VENCORP'S five year tariff proposal provides greater certainty with respect to the level of tariffs. Finally, the registration tariff has been set so as to minimise barriers to entry.

Section 8.1 (e) efficiency in the level and structure of the Reference Tariff

VENCorp's tariff structure is by necessity a compromise between cost reflectivity, facilitating new entry, promoting competition and simplicity. Consequently, charges to users do not always purely reflect the specific costs incurred. VENCorp's functions do not in general have a one to one relationship with users. As such, VENCorp allocates its costs primarily on a per GJ basis, thus providing an appropriate price signal for the cost of providing its services. With respect to the level of VENCorp's tariffs, following analysis of VENCorp's forecast costs the Commission considers that the proposed tariffs are efficient.

Section 8.1 (f) providing an incentive to the Service Provider to reduce costs and to develop the market for Reference and other Services

The Commission is of the opinion that VENCorp's governance structure places some incentive upon it to reduce costs and remain open to respond to the needs of industry. This is supported by VENCorp's proposed real reduction in tariffs of an estimated 10.9 per cent and a revised tariff approval process in response to industry. While ideally the Commission would prefer greater performance incentives placed upon VENCorp, it has not yet determined any feasible options.

Section 8.2 (a) the revenue to be generated from the sales (or forecast sales) of all Services over the Access Arrangement Period (the Total Revenue) should be established consistently with the principles and according to one of the methodologies contained in this section 8

VENCorp applies a cost of service methodology to calculate its total revenue requirements, making no allowance for profit. As VENCorp does not recover an amount for profit, its resulting tariffs are lower than they would be otherwise. VENCorp does however recover all other costs in a manner consistent with section 8 of the Code. As such the Commission considers that VENCorp's proposed revised access arrangement complies with section 8.2 (a) of the Code.

Section 8.2 (b) to the extent that the Covered Pipeline is used to provide a number of Services, that portion of Total Revenue that a Reference Tariff is designed to recover (which may be based upon forecasts) is calculated consistently with the principles contained in this section 8

VENCorp's reference tariff structure is a compromise between cost reflectivity, facilitation of new entry, and simplicity. The Commission considers that VENCorp's reference tariffs achieve a reasonable balance and are consistent with section 8.2 (b) of the Code.

Section 8.2 (c) a Reference Tariff (which may be based upon forecasts) is designed so that the portion of Total Revenue to be recovered from a Reference Service (referred to in paragraph (b)) is recovered from the Users of that Reference Service consistently with the principles contained in this section 8

VENCorp's reference tariffs are designed to recover costs associated with the provision of its reference services. Although not always cost reflective, the Commission notes that VENCorp has designed its reference tariffs to the maximum extent commercially and technically feasible to recover costs associated with the provision of its reference services. The Commission notes that given VENCorp's reference tariffs represent only a small proportion of the total charge to end users, any additional attempt to introduce further intricacy in its tariff structure may incur additional administrative costs without commensurate benefits to users. As such, the Commission considers that this meets the requirements of section 8.2 (c) of the Code.

Section 8.2 (d) Incentive Mechanisms are incorporated into the Reference Tariff Policy wherever the Relevant Regulator considers appropriate and such Incentive Mechanisms are consistent with the principles contained in this section 8

VENCorp does not seek to retain any revenue above the actual cost of providing its reference service. The Commission considers that VENCorp's governance, reporting structure and budgeting process, which involve an open and transparent consultation process, ensures that users are able to comment on planned expenditures and opportunities for efficiencies and acts as an effective incentive mechanism. The Commission considers that these structures place reasonable incentive on VENCorp to operate efficiently. In the absence of a further, feasible incentive mechanism, the Commission considers that on balance, VENCorp's proposal meets the requirements of section 8.2 (d) of the Code.

Section 8.2 (e) any forecasts required in setting the Reference Tariff represent best estimates arrived at on a reasonable basis.

VENCorp's expenditure planning involves detailed review and analysis of the tasks that it is required to undertake in order to meet its statutory and stakeholder requirements. These reviews are subject to Board and industry scrutiny and consultation. VENCorp undertakes an Annual Planning Report process that includes econometric modelling, forecasting and scenario analysis by independent experts, that form the base for converting its costs to tariff rates. VENCorp has acknowledged that the differences between its own demand forecasts and those of GasNet are likely to be immaterial. Accordingly, the Commission considers that in setting its reference tariffs, VENCorp's expenditure forecasts represent the best estimate, arrived at on a reasonable basis, and that GasNet's demand forecasts are reasonable.

3.2 Demand forecasts

3.2.1 VENCorp's proposal

VENCorp's demand forecasts are derived from the VENCorp Annual Planning Review (APR).²⁴ VENCorp engaged the National Institute of Economic and Industry Research (NIEIR) to develop an integrated econometric forecast system capable of developing short and long-term energy forecasts at the national, state and regional levels.

To complement the econometric forecasts, VENCorp surveyed very large industrial customers and, where appropriate, gas demand forecasts generated from the econometric forecast models were adjusted to include planned load expansion or reduction obtained from the survey. This survey included a focus on gas cogeneration, an expanding technology that VENCorp views as a key growth driver in industrial loads.²⁵

VENCorp estimated three system demand scenarios. The medium scenario was submitted in its revised access arrangement information and is presented in Table 3.3.

²⁴ VENCorp Annual Gas Planning Review 2002 to 2006, November 2001

²⁵ VENCorp Annual Gas Planning Review 2002 to 2006, November 2001, p.87

Table 3.3: VENCORP total annual demand forecasts

Financial Year	Medium Scenario (PJ)
6 months to 30 June 2003	98.5
2004	223.4
2005	233.0
2006	240.2
2007	245.5
6 months to 31 December 2007	137.0

Source: VENCORP Access Arrangement Information 28 March 2002 p 27 Table 23.

Note: Total annual demand forecasts include gas power generation and exclude exports to NSW and underground storage withdrawals.

3.2.2 Submissions

There is a difference between the annual demand forecasts underlying those proposed by VENCORP and GasNet. Both GasNet and VENCORP based their demand forecasts on those published in the VENCORP APR. However, GasNet proposed to adjust these estimates to account for a warming trend in Melbourne, which it says arises from a combination of an enhanced greenhouse effect and an ‘urban heat island’ effect. Submissions from interested parties suggest that the assumptions used in deriving gas demand projections should be the same for both entities.

Origin Energy comments that the difference between GasNet’s forecast gas load and VENCORP’s is due to VENCORP not applying a warming trend. Origin suggests that forecast gas loads should be similar and that the VENCORP forecast should be used.²⁶ Further, Origin encourages the Commission to establish a requirement that both GasNet and VENCORP arrive at consistent demand forecasts, noting that GasNet has modified the original VENCORP data.²⁷

AGL submitted that GasNet has adjusted VENCORP’s forecasts down because of predicted urban warming. However, AGL argues that to some extent VENCORP recognised this through the downward adjustment of their Effective Degree Days (EDD) calculations. AGL states that whilst load forecasts are in themselves speculative, the effect of a reduced load forecast coupled with a proposed increased capital base would tend to infer higher overall tariff rates than would otherwise be the case for GasNet.²⁸

ENERGEX Retail suggested that the GasNet model provides little value and that the energy flows over the period of the access regime should be referenced to VENCORP’s annual forecast. ENERGEX believes that the underlying assumptions for the treatment of the assets should be the same for both of the businesses.²⁹ As such, ENERGEX states that an essential component of the Commission’s approval is for the same volume calculations to be used in both GasNet’s and VENCORP’s applications.³⁰

²⁶ Origin Energy submission 17 May 2002, p.2

²⁷ Origin Energy submission 17 May 2002, p.10

²⁸ AGL Energy submission 9 May 2002, section 5

²⁹ ENERGEX Retail submission 9 May 2002, p.2

³⁰ ENERGEX Retail submission 9 May 2002, p.8

Finally, Duke Energy believes that there is little rationale in basing the pricing structure for the two access arrangements on different demand forecasts and that consistency between access arrangements should be required.³¹

VENCorp's forecasts are shown with GasNet's for comparison on a calendar year basis in Table 3.4:

Table 3.4: Comparison of VENCORP and GasNet demand forecasts

Calendar Year	VENCORP (PJ)	GasNet (PJ)	Difference (PJ)
2002	211.4		
2003	216.6	216.2	0.4
2004	225.9	225.3	0.6
2005	233.5	232.7	0.8
2006	238.3	237.2	1.1
2007	242.6	241.3	1.3

Source: VENCORP submission to ACCC on Access Arrangement Issues Paper 13 May 2002, p.20

VENCORP submitted that there is a comparatively small difference in annual demand forecasts with the difference increasing to 1.3 PJ by 2007. However VENCORP believes that the differences are not significant when compared to normal load variations due to weather cycles and load forecast uncertainty over five years.³²

VENCORP states that the differences in demand forecasts are due to the different underlying assumptions used by VENCORP and GasNet in respect to urban and global warming effects.³³

VENCORP adjusted the urban temperature standard to represent the average weather as recorded at the Melbourne Bureau of Meteorology (BOM) site in 2001. GasNet commissioned CSIRO to assess the trend in temperature observations. CSIRO concluded that the trend was mainly due to urban warming and partly to global warming. GasNet extrapolated this trend in temperature observations to the VENCORP forecasts assuming that the warming effect would impact the whole PTS.³⁴

3.2.3 Commission's considerations

GasNet and VENCORP have based their demand forecasts on those published in the VENCORP Annual Planning Review (APR). However, GasNet proposes to adjust these estimates to account for a warming trend in Melbourne which it says arises from a combination of enhanced greenhouse effect and an urban heat island effect.

³¹ Duke Energy submission 13 May 2002, p.2

³² VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.21

³³ VENCORP submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.20. VENCORP reports a statistically significant upward trend in average winter temperatures observations at the Melbourne Bureau of Meteorology (BOM) over the last 50 years.

³⁴ VENCORP submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.19-20

The Commission concurs with the views expressed by interested parties that forecast volumes should be consistent across the two access arrangements. It notes that there is a preference by interested parties for VENCORP's forecasts to be adopted.

VENCORP's demand forecast volumes were based on an independent econometric analysis by NIEIR. However, the Commission notes that the Essential Services Commission (ESC) proposes to accept demand projections from three Victorian gas distribution businesses for their revised access arrangements, which are consistent with GasNet's approach. As stated the Commission's preference is for multiple service providers to adopt a consistent approach.

The Commission considers that the VENCORP APR forecasts have been determined through a transparent process, involving public consultation and form a sound basis for the demand forecast that will be used to derive the tariffs to apply for the second access arrangement period. However, the Commission notes that the CSIRO report commissioned by GasNet supports a comparatively small adjustment to these estimates and that VENCORP considers the differences immaterial. Further, GasNet submits that no credible critique has been provided of the CSIRO report.

On balance, the Commission proposed to accept GasNet's demand forecasts. Accordingly it has proposed an amendment to VENCORP's access arrangement. However it will consider further submissions before making its Final Decision.

Proposed amendment 2

VENCORP must amend its total annual demand forecasts in Table 23 and Table 24 of its revised access arrangement information so that they are consistent with those proposed in section 7 of GasNet's revised access arrangement information.

3.3 Forecast revenues

3.3.1 Code requirements

The Code permits a choice of three methodologies for determining the total revenue. Section 8.4 outlines these as:

Cost of Service: The Total Revenue is equal to the cost of providing all Services (some of which may be the forecast of such costs), and with this cost to be calculated on the basis of:

- (a) a return (Rate of Return) on the value of the capital assets that form the Covered Pipeline (Capital Base);
- (b) depreciation of the Capital Base (Depreciation); and
- (c) the operating, maintenance and other non-capital costs incurred in providing all Services provided by the Covered Pipeline (Non-Capital Costs).

IRR: The Total Revenue will provide a forecast Internal Rate of Return (IRR) for the Covered Pipeline that is consistent with the principles in sections 8.30 and 8.31. The IRR should be calculated on the basis of a forecast of all costs to be incurred in providing such Services (including capital costs) during the Access Arrangement Period.

The initial value of the Covered Pipeline in the IRR calculation is to be given by the Capital Base at the commencement of the Access Arrangement Period and the assumed residual value of the Covered Pipeline at the end of the Access Arrangement Period (Residual Value) should be calculated consistently with the principles in this section 8.

NPV: The Total Revenue will provide a forecast Net Present Value (NPV) for the Covered Pipeline equal to zero. The NPV should be calculated on the basis of a forecast of all costs to be incurred in providing such Services (including capital costs) during the Access Arrangement Period, and using a discount rate that would provide the Service Provider with a return consistent with the principles in sections 8.30 and 8.31.

While these methodologies provide different ways of assessing the total revenue requirement, their outcomes should be consistent. For example, it is possible to express any NPV calculation in terms of a cost of service calculation by the choice of an appropriate depreciation schedule. In addition, other methodologies are acceptable under section 8.5 of the Code provided they can be translated into one of these forms.

3.3.2 VENCORP'S PROPOSAL

VENCORP'S forecast total revenue is calculated by using a combination of the cost of service methodology (without a return on capital) and the price path approach.

VENCORP'S proposed tariffs result in a financial performance over the second access arrangement period as outlined in Table 3.5.

Table 3.5: Statement of VENCORP'S financial performance (\$'000) ^a

	Plan		Estimate			
	Jan-Jun 2003	2003/04	2004/05	2005/06	2006/07	Jul-Dec 2007
Total Revenues ^b	7 177	16 389	16 911	17 359	17 738	9 970
Total Costs ^c	8 387	16 634	17 208	17 956	18 091	8 857
Operating Surplus / (Deficit)	(1 210)	(245)	(297)	(597)	(353)	1 113
Previous period surplus / (deficit)	1 837	689	601	508	153	23
Financial Income	62	157	204	242	223	95
Surplus / (Deficit) Carried forward	689	601	508	153	23	1 231

Source: VENCORP.

a: VENCORP'S Access Arrangement Information p.45 Statement of Financial Performance values are all in 2002 dollars. Values in this table have CPI escalation applied. Financial Income is shown to enable summation of Surplus / (Deficit) Carried Forward.

b: Revenues include Commodity, System Security, Metering and Registration tariffs. Also included are revenues from competitive services and consultancies.

c: Costs include Labour, Expenses and Non-Operating Items

VENCORP states that its budget has been developed according to its statutory obligations and functions under the Gas Industry Act and MSOR. Appendix 1 to VENCORP'S access arrangement information sets out key assumptions underpinning its financial forecast.

VENCORP proposed that registration and commodity tariffs be fixed for five years. To calculate these commodity and registration tariffs, VENCORP undertook an exercise that is summarised as follows:

- VENCORP started by forecasting costs over the period;

- then set its target surplus for the end of the period; and then,
- using forecast demand, solved for the required (constant) tariffs that when multiplied by demand in each period provided sufficient revenue to cover costs, at least to the extent that the carry forward surplus or deficit did not breach the set tolerance limits.

In addition, VENCORP proposed a re-balancing mechanism that will enable it to average out movements in net revenues associated with changes in demand and not result in short-term movements in tariffs. VENCORP stated that;

- tariffs will be subject to a price path with rebalancing constraints during the Access Arrangement Period as follows;
- an annual re-balancing mechanism at VENCORP's discretion to increase its tariffs by up to the greater of CPI or 2% for annual accumulated aggregate under-recovery of at least \$1.5m but less than \$3m.
- For annual accumulated aggregate under-recovery in excess of \$3m VENCORP can seek a variation to this Access Arrangement under section 2 of the Access Code for an increase in tariffs to recover that part of an under-recovery in excess of \$3m.
- For an annual accumulated aggregate over-recovery above \$1.5m, VENCORP is to reduce its tariffs by at least 2%.³⁵

It is important to note from Table 3.5 that VENCORP plans to bring forward from the current access arrangement period a surplus of \$1.8 million, and to run an operating deficit until the end of the second access arrangement period in July - December 2007. This financial profile results in an estimated surplus of \$1.2 million being carried forward at the end of the second access arrangement period in 2007.

3.3.3 Submissions

ENERGEX Retail supports the overall structure and magnitude of VENCORP's proposed charges. ENERGEX states that whilst there has been much debate over the costs of Victoria's market carriage regime, VENCORP's charges make up only 1 per cent (approximately) of its customers' final bill.³⁶

Five year tariff proposal

Industry has expressed to VENCORP a desire for greater certainty in tariffs. According to VENCORP:³⁷

Industry has strongly expressed, during the annual consultation process on VENCORP's budget, the view that it was highly desirable for greater certainty with respect to tariffs for gas transmission. In response to this industry feedback, VENCORP proposed revisions to its access arrangements for a process to stabilise tariffs where possible over the full regulatory period, thereby mitigating the potential for annual fluctuations that are likely under the current annual approval processes for commodity tariffs.

³⁵ VENCORP Access Arrangement 28 March 2002, p.9

³⁶ ENERGEX Retail submission 9 May 2002, p.7

³⁷ VENCORP Review of Access Arrangements for the PTS – Report on VENCORP Public Consultation, January 2002, p.13

An example of this response to VENCORP was the comments of BHP Billiton that it has a preference for certainty of all regulated prices. It considers that users of the PTS need to know in advance the cost of gas supply. BHP Billiton considers that, regardless of whether such costs are related to system management or to other factors, certainty of pricing is of high importance.³⁸

Also, ENERGEX Retail's submission to the Commission supports VENCORP's proposal for greater price certainty through a five year price path.³⁹

3.3.4 Commission's considerations

VENCORP has submitted a revised access arrangement that largely maintains the status quo with respect to its reference services, the corresponding terms and conditions of service, and the allocation of costs across its services.

The Commission has already approved VENCORP's tariffs for the financial year ending 30 June 2003, however VENCORP (and the Commission) have yet to determine meter data management tariffs and the system security tariff beyond the first six months of the second access arrangement period. These tariffs will continue to be set (and approved by the Commission) on an annual basis. Interested parties note that there is a risk of an increase in the system security tariff. This was discussed in section 3.1.3 of this Draft Decision and is addressed in the Commission's Draft Decision for GasNet, section 2.3.2

As it currently stands, the Commission's approval and reporting process for all VENCORP's tariffs occurs annually. Industry has expressed a desire for greater certainty in VENCORP's tariff structure, and in response, VENCORP has submitted a proposal to extend the approval period for registration and commodity tariffs to five years, which it says will achieve a level of price stability over the second access arrangement period.

The Commission has assessed VENCORP's tariff calculations in some detail and considers that the approach adopted is sound. The methodology involves VENCORP forecasting its costs over the period, setting its target surplus for the end of the period and then using forecast demand to solve for the required tariffs that will derive sufficient revenue to cover costs.

The approach by VENCORP mitigates the potential for annual fluctuations that are likely under the current annual approval process (particularly for commodity tariffs), while including safeguards that would prevent VENCORP from having to carry substantial over or under recoveries. The Commission considers that VENCORP's proposal to absorb an accumulated net under or over recovery during the second access arrangement period is reasonable, and that reducing its current surplus from \$1.8 million to \$1.2 million at the end of 2007 is appropriate.

As noted, the Commission understands that VENCORP's proposal to fix commodity and registration tariffs over the period 2003-07 has been made in response to industry's desire for greater price stability. The Commission did not receive any submissions that expressed opposition to VENCORP's proposal. Given the general support for VENCORP's approach, the

³⁸ BHP Billiton 2003 Victorian Gas Access Arrangements VENCORP's Issues Paper, A Review December 2001, p.13

³⁹ ENERGEX Retail submission 9 May 2002, p.7

benefit provided in the form of greater price stability without any significant compromise in the transparency and efficiency requirements placed on VENCORP, the Commission considers that VENCORP's proposal is reasonable and meets the requirements of the Code.

4. Non-tariff elements

Section 3 of the Code establishes the minimum content of an access arrangement, which includes the following non-tariff mandatory elements:

Services Policy - An Access Arrangement must include a policy on the Services to be offered.

The Services Policy must:

- include a description of one or more Services which are to be offered;
- where reasonable and practical, allow Prospective Users to obtain a Service that includes only those elements that the User wishes to be included in the Service; and
- where reasonable and practical, allow Prospective Users to obtain a separate tariff in regard to a separate element of a Service.

Terms and Conditions - An Access Arrangement must include the terms and conditions on which the Service Provider will supply each Reference Service.

Capacity Management Policy - An Access Arrangement must state whether the Covered Pipeline is a Contract Carriage Pipeline or a Market Carriage Pipeline.

Trading Policy - An Access Arrangement for a Contract Carriage Pipeline must include a policy on the trading of capacity. The Trading Policy must, amongst other things, allow a User to transfer capacity:

- without the Service Provider's consent, if the contract between the User and the Service Provider is unaltered by the Transfer; and
- with the Service Provider's consent, in any other case. Consent may be withheld only on reasonable commercial or technical grounds.

Queuing Policy - An Access Arrangement must include a policy for defining the priority that Prospective Users have to negotiate for specific Capacity (a Queuing Policy).

Extensions/Expansions Policy - An Access Arrangement must include a policy setting out a method for determining whether an extension or expansion to the Covered Pipeline is or is not to be treated as part of the Covered Pipeline for the purposes of the Code.

Review Date - An Access Arrangement must include a date on or by which revisions to the Access Arrangement must be submitted and a date on which the revised Access Arrangement is intended to commence.

Each of the non-tariff elements listed above is discussed in this chapter. However, VENCORP's is not required to include a trading policy, as the PTS is a market carriage system of pipelines. Also, pursuant to section 10.2 (c) of the Code, the requirement for an access arrangement to have an extensions and expansions policy has been allocated to GasNet.

4.1 Services policy

4.1.1 Code requirements

The Code requires an access arrangement to include a policy on the service or services to be offered. The services must comply with the principles in sections 3.1 and 3.2 that state:

- 3.1 An Access Arrangement must include a services policy on the Service or Services to be offered (a *Services Policy*).
- 3.2 The Services policy must comply with the following principles:
 - (a) The Access Arrangement must include a description of one or more Services that the Service Provider will make available to Users or Prospective Users, including:
 - (i) one or more Services that are likely to be sought by a significant part of the market; and
 - (ii) any Service or Services which in the Relevant Regulator's opinion should be included in the Services Policy.
 - (b) To the extent practicable and reasonable, a User or Prospective User must be able to obtain a Service which includes only those elements that the User or Prospective User wishes to be included in the Service.
 - (c) To the extent practicable and reasonable, a Service Provider must provide a separate Tariff for an element of a Service if this is requested by a User or Prospective User.

4.1.2 VENCORP'S PROPOSAL

VENCORP will make its reference services available to users and prospective users of the PTS in accordance with the reference tariff policy described in section 5.2 of its proposed revised access arrangement.

VENCORP states:⁴⁰

Reference Services are those required to perform its statutory functions under the Gas Industry Act and MSO Rules in respect to the Principal Transmission System, but exclude VENCORP'S functions under section 160(1)(j) of the Gas Industry Act relating to full retail competition.

However, VENCORP notes that its ability to provide the VENCORP Reference Services is dependent upon GasNet making the PTS available to VENCORP to operate in accordance with the MSO Rules.⁴¹

VENCORP'S reference services are described in Table 2 of its proposed revised access arrangement.

4.1.3 Submissions

Despite sections 3.1 and 3.2 of the Code, which require an access arrangement to include a services policy and reference service, GasNet has proposed not to include a reference service in its revised access arrangement. VENCORP believes that both VENCORP and GasNet should describe the reference services they provide, and the terms and conditions on which those services are offered, in their respective access arrangements. VENCORP states that together,

⁴⁰ VENCORP Access Arrangement 28 March 2002, p.5

⁴¹ VENCORP Access Arrangement 28 March 2002, p.5

the two access arrangements should describe the total services provided to users, and each entity should describe the particular reference services for which it seeks approval of a reference tariff. As such, VENCORP requests:⁴²

that the Commission require a change to GasNet's access arrangement to include a description of the transportation and capacity services that GasNet provides and details of the terms and conditions of access. The rationale for this request follows:

- VENCORP is a significant user of the GasNet system;
- VENCORP requires GasNet transportation and capacity services in line with clause 5.3.1(a) of the MSO Rules;
- VENCORP and other users need to understand the reference services, terms and conditions GasNet will apply to extensions and expansions of the PTS;
- GasNet proposes to charge reference tariffs (which account for around 85% of the total fee for using the PTS) without describing corresponding reference services. VENCORP's legal advice is that this is incorrect at law, and contrary to the intention of the Access Code.

VENCORP states that this can be achieved by:⁴³

GasNet including in its access arrangement either the entire Service Envelope Agreement, or describing the key obligations from that agreement.

BHP Billiton submits that there is some confusion over who is the service provider of the Victorian transmission pipeline. BHP Billiton states that it appears, at a practical level that VENCORP is the service provider and that GasNet has no responsibility to users of the system. BHP Billiton requests that this issue be clarified as the determination of risk and liability will fundamentally affect the decision on allowable WACC.⁴⁴

The Energy Users Association of Australia (EUAA) questioned which organisation is responsible for the Victorian gas transmission pipelines system. The EUAA submits that it is logical that VENCORP is the responsible agency, however as VENCORP is a legislated 'no liability' organisation, the EUAA has doubts as to where users may seek redress in any compensation claims.⁴⁵

ENERGEX Retail suggests that VENCORP's functions in facilitating FRC should be recognised and included as part of VENCORP's reference services for access to the PTS. ENERGEX argues that the operation of the FRC market is fundamental to the way participants obtain access to the PTS and that the paradigms for metering of the domestic market are inextricably linked to the mechanism for determining imbalance costs in the wholesale market.⁴⁶

⁴² VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.3

⁴³ VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.3

⁴⁴ BHP Billiton submission 21 June 2002, p.36

⁴⁵ EUAA Submission on the GasNet and VENCORP Victorian Gas Transmission Access Review, 11 July 2002, p.11

⁴⁶ ENERGEX Retail submission 9 May 2002 p.8

In relation to FRC, the Gas Industry Act stipulates the process for regulation of VENCORP's FRC costs with the Essential Services Commission (ESC) as regulator. VENCORP states that it has a:⁴⁷

...transitional role for facilitating full retail competition (FRC), to be reviewed in 2004. This is not part of the Reference Services provided by VENCORP at the wholesale gas market level for access to the principal transmission system. Correspondingly, it is not appropriate that the costs associated with this transitional FRC role be included in VENCORP's reference tariffs relating to services at the wholesale gas market level for access to the principal transmission system.

Whereas wholesale level services are regulated under VENCORP's Access Arrangement by the Commission under the Access Code, section 69 of the Gas Industry Act 2001 provides for VENCORP's costs associated with its transitional role in FRC to be recovered through a separate regulated process, subject to approval by the Essential Services Commission.

DNRE states that when operating the PTS, VENCORP does so within the capacity and operational constraints set out in the SEA. As such, DNRE believes that the MSOR provides that:⁴⁸

...the Service Envelope Agreement may cover "gas transportation service", as drafted the agreement does not provide gas haulage per se. Instead what it does, as its primary task, is make available to VENCORP capacity on the PTS for it to operate in accordance with the operating constraints. And it is as part of that operation that VENCORP transports gas over the pipeline.

Further, DNRE states that schedule 3 of the SEA specifies services that are capable of being categorised as ancillary services in terms of the capacity and operating constraints of the PTS are as defined in the SEA, and these are services that are provided by GasNet to VENCORP.⁴⁹

4.1.4 Commission's considerations

Services policy

The Commission considers that where multiple service providers are responsible for complying with the Code, their access arrangements must allocate responsibility between the service providers for complying with the obligations imposed by the Code.

VENCORP has proposed to maintain the status quo for the second access arrangement with respect to its services policy. However, VENCORP's ability to provide the VENCORP reference services is dependent upon GasNet making available the PTS to VENCORP to operate in accordance with the MSOR.

The Commission has considered the strong views of interested parties for GasNet to include a reference service for the services it provides to VENCORP in its revised access arrangement. Section 5.3.1(a) of the MSOR states that VENCORP and a transmission pipeline owner must:

...enter into a service envelope agreement, and thereafter must at all times ensure that there is a valid service envelope agreement in force between them, under which the Transmission Pipeline Owner agrees, amongst other things, to provide to VENCORP gas transportation

⁴⁷ VENCORP Access Arrangement covering letter 28 March 2002, p.6

⁴⁸ DNRE submission 9 May 2002, p.5

⁴⁹ DNRE submission 9 May 2002, p.6

services and pipeline capacity by means of the pipelines of that Transmission Pipeline Owner which form part of the transmission system on terms which are not inconsistent with:

- 1 the access arrangement, if any, of the Transmission Pipeline Owner; and
- 2 the Tariff Order, if applicable.

The Commission proposes that GasNet amend its revised access arrangement to include a reference service for the services it provides to VENCORP. This amendment is in section 11.1.5 of the Commission's Draft Decision for GasNet's proposed revisions. Also, it is proposed that VENCORP amend its revised access arrangement to address the concern that VENCORP's proposed revised access arrangement does not reflect the allocation of responsibility between GasNet and VENCORP. Clause 5.1.1 of VENCORP's revised access arrangement refers only to VENCORP's reference services. It does not acknowledge that VENCORP is the entity that supplies the whole service to retailers.

Accordingly, the Commission proposes that VENCORP amend its proposed services policy to clarify that it is VENCORP who provides to users, not only VENCORP Reference Services, but also the transportation of gas through the PTS via the market carriage system under the MSOR.

Proposed amendment 3

VENCORP must clarify Clause 5.1.1 of its revised access arrangement that VENCORP provides to users, not only VENCORP Reference Services, but also the transportation of gas through the PTS via the Market Carriage system under the MSOR.

FRC exclusion

The Commission has considered ENERGEX's suggestion that VENCORP's functions in facilitating FRC should be recognised and included as part of VENCORP's reference services for access to the PTS. However, the Commission notes that VENCORP's FRC functions are stated in section 69 of the *Gas Industry Act 2001* and that this is a separate regulatory process overseen by the ESC. As such, the Commission considers that this issue is not within the scope of this review. Accordingly, VENCORP's FRC costs are not included in the calculation of its tariffs and revenues for the purposes of its access arrangement.

4.2 Terms and conditions

4.2.1 Code requirements

The Code requires an access arrangement to include the terms and conditions on which a service provider will supply each reference service. Section 3.6 states:

An Access Arrangement must include the terms and conditions on which the Service Provider will supply each Reference Service, and that the terms and conditions included must, in the Relevant Regulator's opinion, be reasonable.

4.2.2 VENCORP's proposal

VENCORP states that its ability to deliver its service is dependent on GasNet making the PTS available to VENCORP. GasNet's access arrangement currently acknowledges that VENCORP is a 'user' of GasNet's services, however GasNet's revised access arrangement fails to make a

commitment to continue to make the PTS available for VENCORP in accordance with the MSOR and SEA.⁵⁰

As such, VENCORP proposes to operate the PTS made available to it by GasNet pursuant to GasNet's access arrangement and the SEA for users in accordance with the MSOR. In order to access the PTS, users must register as Market Participants under the MSOR. Details of the terms and conditions on which VENCORP will supply each reference service are contained in the MSOR.⁵¹

4.2.3 Submissions

No submissions were received on this issue.

4.2.4 Commission's considerations

The Commission notes that VENCORP is proposing to maintain the status quo, and that no concerns were raised by users or prospective users of the PTS regarding the terms and conditions in VENCORP's proposed revised access arrangement. The Commission considers that VENCORP's proposed terms and conditions meet the requirements of the Code.

4.3 Capacity management policy

4.3.1 Code requirements

The Code requires that an access arrangement include a statement that the covered pipeline is either a contract carriage pipeline or a market carriage pipeline. Section 3.7 states:

An Access Arrangement must include a statement (a Capacity Management Policy) that the Covered Pipeline is either;

- (a) a Contract Carriage Pipeline; or
- (b) a Market Carriage Pipeline.

4.3.2 VENCORP's proposal

VENCORP and GasNet have elected the market carriage option under the Code, consistent with the obligations of VENCORP (under the Gas Industry Act as independent system operator for the PTS) to operate that system with an integrated spot market under the provisions of the MSOR. Pursuant to section 3.8 of the Code, the Victorian and NSW ministers have given notice to the Commission permitting the use of the market carriage model for the second access arrangement period relevant to their jurisdictions. As such VENCORP states that:

the MSO Rules provide for a Market Carriage system of managing third party access to the PTS whereby;

- a) users are not required to enter into contracts for the specified services, and are able to use certain services whether or not they hold Authorised MDQ or AMDQ Credit Certificates. Instead, Users are able to obtain access to the Principal Transmission System by meeting the basic requirements for safety, prudential management and (in the case of retailers) licensing;

⁵⁰ VENCORP submission to the ACCC on Access Arrangement Issues Paper, 13 May 2002 , p.5

⁵¹ VENCORP's Access Arrangement 28 March 2002, p.13

- b) pipeline operation and the spot market for gas are fully integrated. The use of the Principal Transmission System is limited only by what is physically achievable and economically optimal, not by services individually contracted with the operator, VENCORP, as a Service Provider;
- c) users' charges are based on actual usage of the Principal Transmission System and the services provided to them by VENCORP; and
- d) users have the ability to transfer their rights to Authorised MDQ and AMDQ Credit Certificates rights to other parties, and can acquire additional rights by entering into commercial arrangements with other Users and pipeline owners.⁵²

4.3.3 Submissions

BHP Billiton requests that VENCORP be required to demonstrate the cost-benefits of the MSOR. BHP Billiton states that the market carriage model has:

...some positive features but the MSOR as developed minimises the benefits coming out of this model, and interpolates a number of negative features out of the contract carriage model.

The provision of the gas spot price comprises the need for many of the costly features of the MSOR as they are written. A review of the variation of the spot price since introduction of the MSOR indicates that a cost/benefit review of the MSOR has never attempted to identify the cost to the users of the MSOR.⁵³

4.3.4 Commission's considerations

The Commission concluded in 1998 that the Victorian market carriage approach was consistent with the Victorian Code's principles and criteria. As required by section 3.8 of the Code, the Victorian and NSW ministers have given notice to the Commission permitting use of the market carriage model for the second access arrangement period for those parts of the PTS in their relevant jurisdictions.

On 20 May 2002, the Commission received applications for the renewal of authorisation of the MSOR from VENCORP. The applications seek renewal of authorisation for VENCORP's MSOR for a ten year period commencing 1 January 2003. The Commission released an Issues Paper in June 2002 to assist interested parties in their submissions to the Commission on this issue. The Commission intends to release its Draft Determination on VENCORP's application in September 2002.

Further, section 205 of the Gas Industry Act requires that a review of Part 8 of that Act, which covers VENCORP's operations and functions, must be undertaken in 2007 and completed by 31 December 2007. The review will address whether or not there is a continuing need for VENCORP, or a similar statutory authority. It must have particular regard to the competitiveness of markets for and in relation to gas.

The Commission expects that the review will examine the overall market structure and operations in Victoria, including the market carriage capacity management system and the role of VENCORP as independent system operator. Accordingly, the Commission does not propose to assess the current market structure or the relative merits of the two capacity management systems as part of the current review.

⁵² VENCORP's Access Arrangement 28 March 2002, p.14

⁵³ BHP Billiton submission 21 June 2002, p.37

The Commission concludes that GasNet and VENCORP's proposal to continue under a market carriage capacity management system meets the requirements of the Code.

4.4 Trading policy

4.4.1 Code requirements

Principles of a trading policy are set out in section 3.9 of the Code.

The Access Arrangement for a Covered Pipeline which is described in the Access Arrangement as a Contract Carriage Pipeline must include a policy that explains the rights of a User to trade its right to obtain a Service to another person (a Trading Policy).

4.4.2 VENCORP's proposal

VENCORP states that sections 3.9, 3.10 and 3.11 of the Code are not applicable, as the PTS is a market carriage system of pipelines.⁵⁴

4.4.3 Submissions

There were no submissions received on this issue.

4.4.4 Commission's considerations

VENCORP has not proposed a trading policy in its revised access arrangement for the PTS. The Commission considers that VENCORP does not require a trading policy to meet the minimum requirement of the Code, as the PTS is a market carriage pipeline.

4.5 Queuing policy

4.5.1 Code requirements

Requirements for a queuing policy are set out in sections 3.12 to 3.15. Section 3.12 states:

An Access Arrangement must include a policy for determining the priority that a Prospective User has, as against any other Prospective User, to obtain access to Spare Capacity and Developable Capacity (and to seek dispute resolution under section 6) where the provision of the Service sought by that Prospective User may impede the ability of the Service Provider to provide a Service that is sought or which may be sought by another Prospective User (a Queuing Policy).

Section 3.13 outlines what a Queuing Policy must contain.

The Queuing Policy must:

- (a) set out sufficient detail to enable Users and Prospective Users to understand in advance how the Queuing Policy will operate;
- (b) accommodate, to the extent reasonably possible, the legitimate business interests of the Service Provider and of Users and Prospective Users; and
- (c) generate, to the extent reasonably possible, economically efficient outcomes.

⁵⁴ VENCORP's Access Arrangement 28 March 2002 p.14

4.5.2 VENCORP'S PROPOSAL

VENCORP did not propose any change from the current Queuing Policy. The Queuing Policy for the PTS is described in clause 5.3 of the MSOR, which provides a means of allocating spare capacity when it becomes available.

These provisions permit VENCORP to allocate spare capacity as Authorised MDQ to those who request it where there is sufficient Authorised MDQ to allocate, to auction it where the requests exceed the available quantity, and to provide for bilateral contracting and trading of capacity as Authorised MDQ and AMDQ Credits which are fully tradeable and transferable.

4.5.3 SUBMISSIONS

No submissions were received in relation to this matter.

4.5.4 COMMISSION'S CONSIDERATIONS

VENCORP has not proposed any changes to the queuing policy in its revised access arrangement. Consequently, the Commission considers that VENCORP'S queuing policy for the PTS continues to meet the requirements set out in sections 3.12 to 3.15 of the Code.

4.6 EXTENSIONS AND EXPANSIONS POLICY

4.6.1 CODE REQUIREMENTS

Section 3.16 of the Code requires an access arrangement to have an extensions/expansions policy. However, if there is more than one service provider in connection with a covered pipeline section 10.2 (c) of the Code applies:

Responsibility for complying with the obligations imposed by this Code on the Service Provider is allocated among them by their Access Arrangements or their Access Arrangement.

4.6.2 VENCORP'S PROPOSAL

Pursuant to section 10.2 (c) of the Code, responsibility for complying with the obligation imposed by section 3.16 of the Code to include an extensions/expansions policy in an access arrangement has been allocated to GasNet.

4.6.3 SUBMISSIONS

As the responsibility for complying with the Code has been allocated to GasNet, no submissions were received in relation to VENCORP'S proposal.

4.6.4 COMMISSION'S CONSIDERATIONS

The Commission considers that the allocation of responsibilities between GasNet and VENCORP with regard to extensions and expansions complies with section 10 (c) of the Code.

4.7 Review and expiry of the access arrangement

4.7.1 Code requirements

The Code outlines the review and expiry of an Access Arrangement in section 3.17, which states:

An Access Arrangement must include:

- (a) a date upon which the Service Provider must submit revisions to the Access Arrangement (a Revisions Submission Date); and
- (b) a date upon which the next revisions to the Access Arrangement are intended to commence (a Revisions Commencement Date).

4.7.2 VENC Corp's proposal

VENC Corp proposed a revision submission date of the access arrangement of 31 March 2007. The proposed revision commencement date is 1 January 2008.

4.7.3 Submissions

There were no submissions received on this issue.

4.7.4 Commission's considerations

The Commission considers that VENC Corp's proposed revision submission date and revision commencement date meet the requirements of the Code.

5. Information provisions and key performance indicators

5.1 Information Provision

5.1.1 Code requirements

Certain categories of information must be included in the access arrangement information that must accompany an access arrangement. The specific items of required information are contained in Attachment A of the Code and appendix B to this Draft Decision.

The provision of information for the review of an access arrangement is detailed under sections 2.6 and 2.7 of the Code, which state:

- 2.6 Access Arrangement Information must contain such information as in the opinion of the Relevant 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.
- 2.7 The Access Arrangement Information may include any relevant information but must include at least the categories of information described in Attachment A.

5.1.2 VENCORP'S PROPOSAL

VENCORP submitted access arrangement information in conjunction with its proposed revised access arrangement on 28 March 2002. Appendix 2 of VENCORP'S access arrangement information details VENCORP'S compliance with the information required by Attachment A to the Code.

5.1.3 Submissions

BHP Billiton formally requested:⁵⁵

That the Commission, under Section 2.9(b) of the Third Party Access Code to consider whether the Access Arrangement Information filed by GasNet and VENCORP for the Victorian transmission network complies in full with Sections 2.6 and 2.7 of the Code.

Further, BHP Billiton stated that users are required to take a 'bundled' service from GasNet and VENCORP for the provision of the service. BHP Billiton considers that there needs to be an aggregation of the costs to be incurred for the aggregated service. BHP Billiton submits that these costs need to be broken down so that proper comparison of KPIs can be made and appropriate benchmark comparisons made with other transmission pipeline businesses.⁵⁶

ENERGEX Retail submitted that GasNet and VENCORP should be compelled by the Commission to make a joint application and that the Commission'S approval be conditional on each business providing its individual part of the combined service. Further, ENERGEX Retail maintained that the Service Envelope Agreement (SEA) should be made public.⁵⁷ It believes that it is not possible to understand the relationship between GasNet and VENCORP

⁵⁵ BHP Billiton submission 17 May 2002, p.14

⁵⁶ BHP Billiton submission 17 May 2002 p.9

⁵⁷ ENERGEX Retail submission 9 May 2002 p.1 & 6

without access to the SEA and sees no reason why it should not be made public as part of the applications made by both VENCORP and GasNet.

TXU states that it is encouraged by the form of the VENCORP submission, and its compliance with the spirit and requirements of the Code.⁵⁸

5.1.4 Commission's considerations

Under section 2.30(b) of the Code, the Commission reviewed VENCORP's access arrangement information in conjunction with its proposed revised access arrangement. The Commission was satisfied that VENCORP's access arrangement information satisfied the requirements of section 2.6 and 2.7 of the Code. It met each of the relevant categories of information required as set out in Attachment A.

While ENERGEX Retail argued that both GasNet and VENCORP should be compelled by the Commission to make a joint application, section 10.2 of the Code states that where:

- (a) there is more than one Service Provider in connection with a Covered Pipeline;
- (b) one is the owner and another is the operator; and
- (c) responsibility for complying with the obligations imposed by this Code on the Service Provider is allocated among them by their Access Arrangements or their Access Arrangement,

each Service Provider is responsible for complying with the obligations allocated to it.

Accordingly, the Commission cannot compel the two service providers to submit a joint application. As such, both GasNet and VENCORP have allocated responsibility for complying with the Code among them. The Commission considers that this complies with the requirements of section 10.2.

In regards to the SEA, it is a public document and was released with the Commission's Final Decision in 1998 This can be accessed from the Commission's web site at <http://www.accc.gov.au/gas/fs-gas.htm>

As discussed in section 11.1.5 of the Commission's Draft Decision for GasNet, the Commission proposes that GasNet amend its revised access arrangement to include in its services policy the services that it supplies to VENCORP and state that the terms and conditions on which GasNet supplies the services to VENCORP are set out in the SEA and MSOR.

5.2 Key performance indicators

5.2.1 Code requirements

The Code identifies the need for key performance indicators (KPI) to be disclosed by service providers to interested parties. Category 6 of Attachment A of the Code lists the information required to be provided regarding KPIs:

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

⁵⁸ TXU covering letter 31 May 2002, p.1

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

The Commission may have regard to other operational and financial indicators in relation to the manner in which values have been attributed to total revenue. Section 8.6 states:

In view of the manner in which the Rate of Return, Capital Base, Depreciation Schedule and Non Capital Costs may be determined (in each case involving various discretions), it is possible that a range of values may be attributed to the Total Revenue described in section 8.4. In order to determine an appropriate value within this range the Relevant Regulator may have regard to any financial and operational performance indicators it considers relevant in order to determine the level of costs within the range of feasible outcomes under section 8.4 that is most consistent with the objectives contained in section 8.1.

5.2.2 VENCORP'S PROPOSAL

VENCORP has acknowledged the need for mechanisms to demonstrate and test performance and to promote efficiency. VENCORP has stated that it is supportive of providing relevant external performance benchmarks that will assist in assessing its performance with similar organisations. However, work completed to date by VENCORP on the potential for benchmarking performance against other similar organisations has led it to conclude that meaningful direct comparison with the statutory gas functions of VENCORP is highly problematic and likely to be ineffective in producing cost efficiencies.

VENCORP states that NEMMCO reached this conclusion in a recent attempt to benchmark its fee structures to other electricity power pool operators around the world. To the extent that meaningful external benchmark data becomes available, VENCORP has proposed to consider it and where appropriate amend its performance monitoring regime.⁵⁹

In the absence of benchmarking, VENCORP has developed a series of internal corporate KPIs against which it reports to its board and industry participants on a monthly basis and publishes outcomes annually through its annual report and corporate plan.⁶⁰

In order to comply with Code requirements VENCORP has derived a set of internal KPIs as follows:⁶¹

- a) Cost efficiency KPIs – those KPIs that provide an insight to the efficient level of operating costs incurred by VENCORP in completing its statutory functions and roles; and
- b) Operational KPIs – those KPIs that monitor VENCORP's performance to ensure that it meets a minimum quality of service provision implicit in its cost structure.

VENCORP stated that it has not included cost efficiency KPIs for the half-year period 1 July to 31 December 2007 due to seasonality of the load profile and fixed costs.⁶²

During September 2001, VENCORP commissioned consultants to undertake a survey of its key stakeholders to help measure current levels of satisfaction and to determine the value of the

⁵⁹ VENCORP Access Arrangement Information p.31

⁶⁰ VENCORP Access Arrangement Information p.31

⁶¹ VENCORP Access Arrangement Information p.31

⁶² VENCORP Access Arrangement Information p.31

services VENCORP provides. Responses were sought in relation to 32 services provided by VENCORP across its gas and electricity functions.

The range of ratings of VENCORP's performance in delivering the ten services ranked by stakeholders as being of highest importance varied from 'satisfactory' to 'highly satisfied'. All of VENCORP's service offerings rated as being at least satisfactory. The results of the stakeholder survey have been communicated back to those who participated and will be used by VENCORP to develop action plans for improving performance and optimising stakeholder value.

5.2.3 Submissions

The Commission sought comment on the appropriateness of the supplied KPIs included in VENCORP's access arrangement. Submissions were received from interested parties with regards to benchmarking and transparency of VENCORP's decision making process.

Benchmarking and performance indicators

BHP Billiton submitted that VENCORP should benchmark its costs against NEMMCO as it has a similar role to that of VENCORP.

The EUAA submit that an appropriate comparison should be undertaken based upon combined VENCORP and GasNet costs. However the EUAA qualifies this assertion by noting that VENCORP's services are unique, and that some of VENCORP's specific services would be difficult to benchmark.⁶³

VENCORP states that it undertook an analysis as part of its 1999/2000 annual corporate budget process of potential external benchmarks. The conclusion reached by VENCORP was that there were no organisations that offered a meaningful direct comparison with VENCORP's statutory gas functions.⁶⁴

However, VENCORP states that it is willing to consider, and where appropriate amend its performance monitoring regime to take account of meaningful external benchmark data, provided that any such developments can be shown to be:⁶⁵

- cost effective, having regard to the likely value of possible improvements given the small size of VENCORP's total costs and the likely costs for implementation of such measures, and;
- able to provide effect drivers for performance improvements in VENCORP, having regard to its statutory functions.

VENCORP has stated that it remains open to and encourages users to provide sufficiently well developed information on any alternative approaches to that proposed by VENCORP in its access arrangement information.⁶⁶

⁶³ EUAA Submission on the GasNet and VENCORP Victorian Gas Transmission Access Reviews, 11 July 2002, p.11

⁶⁴ VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.17

⁶⁵ VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.18

⁶⁶ VENCORP Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.18

Transparency and effectiveness

ENERGEX Retail states that it is not convinced that the ability of participants to influence actual decisions by VENCORP is effective. It does not share VENCORP's assumptions that industry representation at Board level, as the mechanism for mitigating this risk, is adequate. ENERGEX states that, in a FRC market, the interests of incumbent and independent Retailers will increasingly diverge. As such, ENERGEX anticipates more compelling need for independent retailers to have a separate and direct voice on the VENCORP Board.⁶⁷

DNRE takes the contrary view that VENCORP's current governance arrangements place strong incentives on VENCORP to efficiently deliver services to industry. DNRE states that as VENCORP is a non-profit entity, it passes on the benefits of efficiency gains directly to industry. DNRE argues that to require VENCORP to absorb the financial impact of above-forecast costs would impose asymmetric risk that would be borne by Government. DNRE therefore does not support the imposition of further performance incentives, through penalties for non-performance, on VENCORP.⁶⁸

VENCORP states that the separation of costs for operation of the (PTS) from GasNet's costs provides for significant transparency by a clear separation of costs and charges for these two primary services.

VENCORP acknowledges that energy industry knowledge and interests are an important element in the composition of the VENCORP Board. However, VENCORP states that:⁶⁹

...these are clearly not the only criteria for Board membership. The overall composition of the VENCORP Board must be such that it can execute all of VENCORP's statutory and regulatory obligations and duties (under both the Electricity and Gas Industry Acts and other statutory and regulatory instruments), and meet its responsibilities under Corporations Law.

VENCORP's Directors are nominated by the Victorian Government, such that they constitute a team, with an appropriate mix of individual and complementary skills, to enable effective deliberation and decision making on issues that arise in relation to all of VENCORP's roles and responsibilities.

The VENCORP Board has specifically established the Gas Market Consultative Committee (GMCC) for the purpose of leading industry consultation and making recommendations in relation to wholesale gas market issues. The Board's role is to assess and make decisions based on information and recommendations provided to it by VENCORP management, with industry or public consultation where appropriate.

VENCORP recommended that end-user involvement in the wholesale gas market development could be further addressed through a combination of publication of key documentation on its web site, via its electronic mailing list, standing invitations to end-user representatives, running workshops and public consultation on key market issues.⁷⁰

⁶⁷ ENERGEX Retail submission 9 May 2002, p.7-8

⁶⁸ DNRE submission on the GasNet and VENCORP Victorian Gas Transmission Access Reviews 20 May 2002, p.1-2

⁶⁹ Review of VENCORP's Wholesale Consultative Processes Final Recommendations, February 2002, p.13

⁷⁰ Review of VENCORP's Wholesale Consultative Processes Final Recommendations, February 2002, p.13

VENCorp's recommendations on membership of the VENCorp Board are contained in its report *Review of the Wholesale Gas Market Consultative Processes Final Recommendations – February 2002*. As one of its final recommendations, VENCorp will consider further the issue of re-defining the criteria for retailer representation following the implementation of full retail contestability and in readiness for the Board renewal in March 2003.⁷¹

5.2.4 Commission's considerations

Benchmarking and performance indicators

The Commission considers that benchmarking and performance indicators for VENCorp are important in that it operates on a pure cost recovery basis and does not derive a profit. As such, benchmarking and the use of KPIs are important in compensating for the lack of profit driven performance incentives.

However, the cost of undertaking suitable benchmarking research needs to be considered in the context of the magnitude of VENCorp's costs and the possible benefits that might ensue. The cost of any benchmarking study undertaken should not exceed the benefit it provides in terms of reduced costs for VENCorp. The Commission notes that VENCorp has been unable to identify a suitable comparator on which to base a benchmarking study.

The Commission has taken into consideration submissions by interested parties and the analysis by VENCorp of potential external benchmarking including NEMMCo. The Commission notes that VENCorp has developed internal benchmarks and KPIs that are included in its access arrangement information, and that VENCorp openly encourages users to provide sufficiently well developed information on any alternative approaches to those proposed by VENCorp. The difficulties in developing meaningful and effective benchmarks for VENCorp have not yet been addressed by any party suggesting an alternative approach.

The Commission considers that the approach adopted by VENCorp towards benchmarking and the development of its own internal KPIs reflects a considered approach to the requirements of the Code. The Commission proposes to approve VENCorp's approach in the context that its reference tariffs are reducing in real terms. The Commission will reconsider the issue of benchmarking and KPIs as required.

Transparency and effectiveness

In relation to the concerns raised by ENERGEX, the Commission considers that VENCorp has adopted a measured approach to user involvement in the wholesale gas market through its consultative process during 2001.

The Commission considers that the separation of VENCorp's costs from those of GasNet's provides significant transparency of its reference tariffs, by clearly separating GasNet's return on assets and marketing costs from VENCorp's costs of operating the PTS and providing competitive arrangements for balancing supply, transmission and distribution gas.

In addition, the Commission reviews all of VENCorp's tariffs on an annual basis. Further, meter data management and system security tariffs will continue to be set and approved by the Commission on an annual basis. Accordingly, the Commission considers that the

⁷¹ VENCorp Review of VENCorp's Wholesale Gas Marketing Consultative Process Final Recommendations February 2002, p.13

transparent reporting process is relatively effective in placing reasonable incentives upon VENCORP to reduce costs and remain open to respond to the needs of industry. Evidence of this is in the proposed real reduction in tariffs of an estimated 10.9 per cent over the second access arrangement period.

6. Other matters

6.1 Definition of the PTS

GasNet proposes to merge its PTS and WTS access arrangements, commencing 1 January 2003. It refers to the combined system as the GasNet System (GNS).⁷²

6.1.1 VENCorp's submission

VENCorp states that any possible definitional concerns about the delineation between the WTS and the PTS are not relevant to the revised access arrangement. VENCorp's revised access arrangement continues to use the definition of 'Principal Transmission System' for the following reasons:⁷³

- The Gas Industry Act 2001 is the authoritative instrument and requires VENCorp to operate the Gas Transmission System (which it does pursuant to the MSO Rules), defining the Gas Transmission System as:
 - the primary system, as existed before 1997; and
 - any approved transmission connection or transmission adjunct.

VENCorp believes that continued use of the term 'Principal Transmission System' in its revised access arrangement is a superior approach as this is how the system has been commonly referred to. As such, VENCorp finds no compelling case to alter its revised access arrangement.⁷⁴

6.1.2 Commissions considerations

The Commission prefers that where a pipeline is covered by multiple service providers that the service providers agree to revisions in the first instance. However, as this has not occurred the Commission accepts VENCorp's argument that there is no substantive reason to adopt a new term to describe the PTS that includes the WTS.

6.2 Pricing design

Duke Energy has submitted that the market should internalise as many network externalities as practicable by capturing all costs in the market price for gas.⁷⁵

Duke Energy argues that current pricing design is too simple, resulting in a price that is the same everywhere for the whole day over the PTS. Therefore, within day and zonal scheduling events are not incorporated into the market price and there is a need for compensatory payments outside of the market price to signal future investment in the PTS.

⁷² VENCorp Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.25

⁷³ VENCorp Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.25

⁷⁴ VENCorp Submission to ACCC on Access Arrangement Issues Paper, 13 May 2002, p.25

⁷⁵ Duke Submission to the ACCC Issues paper on proposed revisions to VENCorp and GasNet Access Arrangements, 13 May 02, p.4

VENCorp submits that it has concerns with the particular implementation suggested by Duke Energy. It states that AMDQ and AMDQ credits provide both financial rights, in the form of limited uplift protection and physical rights by prioritising treatment of customers in times of curtailment due to transportation issues.⁷⁶

In support of the current simplified pricing model VENCorp highlights that extensive public consultation by the Victorian government was undertaken prior to the approval of the access arrangement for the initial regulatory period and the authorisation of the MSOR. It was considered at the time that there was not a case for full nodal pricing. VENCorp considers that this has been proven in practice, as only \$1.1 million in total uplift payments have arisen to date, and that this value represents an insignificant proportion of customers total charges for delivered gas.

6.2.1 Commission's considerations

The queuing policy sets out the mechanism for processing requests for service where spare capacity is available but inadequate to satisfy all users and prospective users. The Commission notes the submission made by Duke Energy in relation to within day and zonal scheduling, and notes that this issue will be addressed as part of the Commission's re-authorisation of market and system operations rules. Information about this can be found on the Commission's website www.accc.gov.au under Gas.

⁷⁶ Email by VENCorp on Duke's submission, 10 July 2002, p.3

7. Draft Decision

Pursuant to section 2.35(b) of the Code, the Commission does not approve VENCORP's revised access arrangement for the PTS in its current form. In order for the Commission to grant approval, the amendments (or nature of the amendments) specified in the Draft Decision must be made to the revised access arrangement. The Commission will consider submissions from interested parties and amended revisions from VENCORP (if submitted) before issuing its Final Decision.

Written submissions are requested on the Draft Decision and should be received by the Commission no later than 13 September 2002.

Appendix A: Submissions

The following interested parties provided submissions.

Pre Draft Decision

AGL Energy Sales & Marketing, 9 May 2002

Amcor and Paperlinx, 24 June 2002.

BHP Billiton Petroleum Pty Ltd, 17 May 2002, 21 June 2002, 18 July 2002

Department of Natural Resources and Environment, 22 May 2002

Duke Energy Australia Pty Ltd, 13 May 2002

Energy Advice Pty Ltd, 30 May 2002

Energy Action Group, 31 May 2002

ENERGEX Retail Pty Ltd, 9 May 2002

Energy Users Association of Australia, 4 June 2002 and 11 July 2002

Esso Australia Pty Ltd, 5 June 2002

Origin Energy Limited, 17 May 2002

Pulse United Energy, 16 May 2002

TXU, 3, May 2002 and 31 May 2002

Appendix B: Attachment A

INFORMATION DISCLOSURE BY A SERVICE PROVIDER TO INTERESTED PARTIES

Pursuant to Section 2.7 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, 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