GasNet's Second Response to ACCC Draft Decision

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1 Introduction

1.1 Background

On 24 August 2004, GasNet lodged with the Commission an application to revise the Access Arrangement under 2.28 of the Code (**Revisions Application**). The revisions contained in the Revisions Application are voluntary and separate from:

(a) the scheduled review of the Access Arrangement, due in 2007; and

(b) the annual tariff adjustment, which for 2005 which commenced on 16 November 2004.

A number of interested parties provided submissions on the Revisions Application. On 14 October 2004 GasNet provided the Commission with a response to these submissions.

The Commission issued a draft decision on 10 November 2004 (**Draft Decision**), which proposed to approve three of the four revisions.

1.2 GasNet's response to the Draft Decision

One of GasNet's revisions proposed removing the current lower tariff for withdrawals into storage facilities to prevent export leakage to the SEA Gas Pipeline. The lower tariff would be replaced with a rebate system.

This aspect of the Revisions Application attracted comment from all submissions received by the Commission.

In the Draft Decision, the Commission proposed not to approve this revision, for three reasons:

(a) the Commission was concerned there may be potential for financial loss for some Users, who claimed to have entered into fixed price contracts based on GasNet's present withdrawal tariff;

(b) in the Commission's view, the revision was not necessary to maintain forecast revenue and the Commission was concerned GasNet could receive a windfall gain; and

(c) in the Commission's view, it would not be consistent with Users' reasonable expectation that the tariff price path would not exceed CPI-X+2% for the access period.

GasNet submitted an initial response to the Commission on 19 November 2004 which addressed the first reason (**First Response**).

This Second Response deals only with the second of those reasons, which was specifically raised by AGL in its submission of 4 October 2004 (**AGL Submission**) and discussed by the Commission in the Draft Decision.

GasNet reserves the right to make further submissions on this, or any other, aspect of the Draft Decision.

1.3 Terminology

For convenience, this Response adopts the terminology used in the Revisions Application.

2 Refill Tariff Revision

2.1 Summary of GasNet's proposal

GasNet currently applies a lower tariff to withdrawals into storage facilities. This tariff is deliberately lower than other tariffs on the GNS to encourage storage.

GasNet has become aware that it is now possible for Users who have access to the WUGS storage facility at Iona to export gas from the GNS to the SEA Gas Pipeline, via the WUGS facility, and receive the benefit of the cheaper withdrawal tariff. This opportunity is not available to Users who export through the nearby SEA Gas delivery point.

This use of the cheaper withdrawal tariff for exports was never intended. This is demonstrated both by the name given to the Refill Tariff and the establishment of a standard withdrawal tariff at the nearby SEA Gas Withdrawal Point. Under the Refill Tariff Revision, GasNet proposes to retain the storage incentives while preventing export "leakage" by:

(a) removing the cheaper withdrawal tariff; and

(b) instead operating a rebate system so that stored gas attracts the lower tariff when it is re-injected into the GNS.

2.2 AGL Submission

AGL contends that the Refill Tariff Revision will cause GasNet to over recover on projected 2002 revenues because Users who export gas will be paying more.

AGL states that it would support the Refill Tariff Revision if any over recovery was repaid to Users as this would maintain "tariffs between GNS and WUGS at their current levels".

2.3 The Draft Decision

In the Draft Decision, the Commission stated that if the Refill Tariff Revision was approved, GasNet would receive a "windfall gain" due to an increase in export volumes.

2.4 This Response

GasNet acknowledges that, if the Refill Tariff Revision is approved, then, by limiting the rebate to gas re-injected into the GNS, GasNet is likely to recover more revenue than was originally expected under the Transmission Refill Tariff. However, it should be noted that, as the Refill Tariff was designed as a cost recovery tariff, there was no forecast of volume or revenue provided or approved in the Access Arrangement merely an expectation that such flows could occur.

Thus, in GasNet's view, it is also incorrect to characterise this extra revenue as a "windfall gain", for a number of reasons:

(a) the increase in export volumes is separate from and should not only be linked with the Refill Tariff Revision;

(b) any revenue relating to actual WUGS refill matches extra costs, and therefore is not a "windfall";

(c) if there is any "windfall gain", this will only occur in relation to export volumes, not reinjected gas;

(d) under the Access Arrangement all other export volumes are also a "windfall" to GasNet, in that the Access Arrangement forecast assumed (based on the best available evidence) that exports from the GNS would be nil; and

(e) as a result, the extra revenue is a legitimate outcome of the incentive mechanism already built in to the Transmission Refill Tariff.

3 No windfall gain

3.1 Outline of issue

AGL expressed concern that Users who export gas through WUGS would be "paying more" and therefore GasNet could over recover.

Similarly, the Commission observed that the Refill Tariff Revision could result in a "windfall gain" to GasNet due to the increase in exports from WUGS. However, the Commission accepted that the "windfall" could be regarded as both a benefit and negative of the volume risk assumed by GasNet in 2002.

The Commission also expressed concern that the incentive properties of the Access Arrangement would be changed if GasNet were able to take advantage of the increased exports by increasing the refill tariff.

3.2 No link

The Refill Tariff Revision seeks to amend the application of the Transmission Refill Tariff to ensure the correct tariff applies to exports through WUGS. For reasons outlined in the Revisions Application, this revision is justified.

However, as exports from WUGS have increased from those forecast in 2002 (ie. nil), the Commission and AGL appear concerned that approval of the Refill Tariff Revision will allow GasNet to recover excess revenue.

In GasNet's view, it is incorrect to link increases in forecast gas flows with the Refill Tariff Revision. A refusal to approve the Refill Tariff Revision due to the possibility of this increased revenue would incorrectly attribute the revenue increase to the change in the application of the refill tariff, not the increased export volumes.

For this reason, any analysis of the Refill Tariff Revision is properly separated from the increased exports.

To assess correctly the financial effect of this revision, the Commission should consider this revision to the Transmission Refill Tariff in the context of the 2002 forecast, not the present forecast. Against the 2002 forecast there would be no change to revenue.

Any increase to GasNet's revenue arising from the increased exports is a legitimate incentive gain, which is discussed further below.

3.3 Re-injected and exported gas

The Refill Tariff Revision will affect both re-injections into GNS and gas exported through WUGS.

Re-injected gas

Re-injected gas does not lead to greater than forecast revenue for GasNet. Any revenue obtained from the imposition of the new Transmission Refill Tariff on stored gas will be returned via a rebate to the shipper once the gas is re-injected.

GasNet concedes it will retain the extra time value of the money it holds by way of the rebate. But the time value of this money will amount to around $25,000, which the Commission considers to be immaterial.

Accordingly, the only possible revenue that will lead to the "windfall gain" contemplated by the Commission and AGL will be that arising due to exports.

Exports always in GasNet's favour

The forecasts used to determine the Reference Tariffs in the Access Arrangement, which were based on the best evidence available at the time and were accepted by the Commission, assumed that GasNet would not earn income from exports.

Accordingly, it was always part of the Access Arrangement that all revenue due to exports be retained by GasNet, subject to the normal price control adjustments.

If GasNet earns revenue from increased exports through WUGS, this is an upside of the overall volume risk package GasNet accepted in 2002. The increased revenue is not due to the change to the tariff (that is, the tariff model is preserved) but due to the extra, unforeseen, volumes through WUGS.

All exports should be treated the same

At present, all withdrawals into WUGS, regardless of whether they are for export attract the lower tariff and are excluded from the price control formula.

However, in GasNet's view all exports, whether through Iona or WUGS, should:

(a) attract the same cost to shippers; and

(b) be subject to the price control formula.

3.4 Incentives maintained

The Access Arrangement is intended to allow GasNet to earn its required average tariff if its withdrawal volumes (with the exception of refill volumes) match the forecast. When these overall volumes exceed the forecast, GasNet will earn more than its target revenue and, likewise, less than its target revenue if volumes are below forecast.

However, as noted above, the increased revenue will not arise because of the change in the application of the tariff but from the change in exported volumes. As such, it is a legitimate incentive gain.

Arguing that increased revenue from an unforeseen change in volumes is contrary to section 8.1(a) of the Code could be used to disallow any incentive based tariff model.

4 Conclusion

GasNet concedes that if this revision is approved, it could recover more revenue than was intended when the Access Arrangement was approved. However, this possibility does not arise due to the operation of the Refill Tariff Revision but due to the increased exports.

This revision is an attempt to recognise that all of the significant volume of gas that is (or may be) exported through the SEA Gas Pipeline should all be treated equally regardless of whether it exits the GNS through the WUGS or Iona Withdrawal Points to the SEA Gas Pipeline.

GasNet seeks the revision to ensure Users pay a fully cost reflective tariff for exports and a marginal cost tariff only for gas being stored for re-injection into the GNS. The increase in exports is coincidental and a reflection of the upside of the volume risk faced by GasNet in its Access Arrangement.