

GasNet Response to BHP Billiton Submission of 11 October 2002

18 October 2002

GasNet appreciates the opportunity to make a brief response to the most recent submission from BHP Billiton on the GasNet revised Access Arrangement. However GasNet is concerned that BHP Billiton made its submission only two weeks before the scheduled date of the Final Decision, thereby leaving GasNet with little opportunity to prepare a response. Given the short time available, GasNet will only comment on the major issues raised by BHP.

Double Dipping and Opex Forecast

BHP Billiton appears to believe that GasNet stated that certain operating costs, including pigging expenses, had been deferred during the current Access Arrangement period. In fact, GasNet has made no such statement. The fact that no pigging was conducted in 1998 to 2000 does not imply that GasNet deferred these operations. The decision to conduct a pigging operation is based on a range of factors. These include the vintage of each un-pigged pipeline, the diameters of those un-pigged pipelines of a given vintage, and other operational exigencies which vary from time to time. Based on these considerations, GasNet determined it was not necessary to pig in 1998 to 2001, but that it was appropriate and necessary in 2001 and 2002. It should be noted that there was no specific budget for pigging in the original tariff forecast.

In commenting on the operating cost forecast, BHP Billiton has not acknowledged the significant increase in workload since the original cost forecast was produced in 1998, nor the increases in uncontrollable exceptional costs such as insurance premiums.

Benchmarks

BHP Billiton has stated that the GasNet operating costs per km. of main are significantly higher than that of the gas distributors. Whilst we have not analysed this data, GasNet believes that such a comparison is inappropriate. The distribution networks are dominated by low and medium pressure pipelines, whereas all GasNet pipelines are high pressure pipelines. High pressure pipelines must be patrolled regularly and managed with great care, given the severe consequences of a gas leak. On the other hand, the bulk of the gas distribution mains, which carry gas through most streets in the built-up areas, are not patrolled regularly.

BHP Billiton notes the importance of international benchmarking. GasNet has provided the Commission with a study prepared by Cap Gemini which assesses GasNet operations against similar companies in Australia and overseas. The Commission has noted that this study was prepared as a tool to improve operational efficiency, and that the comparator companies were not identified. For these reasons the Commission believes the study is of limited relevance. However, GasNet believes that the study is relevant because it compares the costs of all the major activities between GasNet and other companies. The comparator companies, and the selected peer group, were identified on page 6 of the Benchmarking Report.

BHP Billiton has concerns that the separation of VENCORP and GasNet operations makes benchmarking difficult, and they suggest that for the purpose of assessing KPIs, the operating costs of VENCORP and GasNet should be combined. However GasNet does not believe it is appropriate to simply add the VENCORP and GasNet costs. Firstly, VENCORP operates a unique market carriage regime, which is not comparable in scope or scale to the contract carriage regimes operated on other transmission pipelines. VENCORP also operates a gas market, a function which,

in other markets, is normally undertaken by separate organizations. In addition, there is likely to be some duplication of activities between GasNet and VENCORP, such as overhead functions.

SWP System-Wide Benefits

Competition Benefits

BHP Billiton claims that access to Otway gas has not increased pricing pressures on gas supply. As evidence, they state that Minerva gas has not been accessed within Victoria, despite the existence of the SWP. Furthermore, they claim that the fact that Otway gas is being developed for the SA market, rather than the Victorian market, implies that Otway gas must be more expensive than Gippsland gas (otherwise the Otway gas would be sold competitively into Victoria).

Competition exists when consumers have a choice. Consumers have exercised that choice by buying peaking/intermediate gas requirements from the WUGS facility, and by sourcing base load needs from the Santos fields in the Otway basin. Santos has an active exploration program in the Otway basin, and plans to increase production for sale into Victoria.¹

With respect to the development of offshore Otway gas (Thylacine and Geographe), GasNet understands that this gas will be offered to both SA and Victoria, and will be a competitive alternative to Gippsland gas once it is in production.²

BHP Billiton also argues that if offshore Otway gas is delayed, then Gippsland gas might be supplied to SA, putting upward pricing pressure on Victorian gas, to the detriment of Victorian users. However GasNet believes that the interconnection of the Gippsland, Otway and Moomba fields, and vigorous interstate competition, is more likely to put downward pressure on gas prices.

System Security Benefits

BHP Billiton attempts to reproduce the calculation of the System Security Value (SSV) originally presented by GasNet, but with "corrected" parameters. In particular they have calculated the probability of a failure over the next regulatory period as .05%, and they arrive at a relatively low value for the SSV.

However, GasNet disagrees with the revised parameters proposed by BHP Billiton, in particular the calculation of the probability of failure of the Longford gas processing plant. As GasNet stated in its original Revision Application for the SWP, the calculation of the probability of failure to supply must take account of all possible failure modes (not simply the failure of the gas plant), and must consider the likelihood of failures of varying levels of severity and duration.

BHP Billiton uses the fact that the Longford supply failed for two weeks out of a total operating life to date of 2000 weeks to calculate a probability of failure of 0.1%. They note that other plants have not experienced such catastrophic failures and estimate a revised failure rate of 0.05%. This value is then applied to the total benefit available from the SWP in an emergency to come up with an SSV of \$1.1 m over the next regulatory period.

GasNet disputes many of BHP Billiton's assumptions. For example, it is not correct that Moomba has not suffered severe failures, although none have been as significant as Longford. Nevertheless there is clearly a risk of failure which must be taken into account (the fact that the SA government

¹ Santos Press Release, *Expanded Otway Basin Production*, 30 May 2002

² Woodside Media Announcement, *Woodside and TXU Sign Agreement on Otway Gas*, 14 Aug 2002. R. Myer, TXU, Woodside in Otway Gas Deal, Age Newspaper 16 Aug 2002. GasNet has forecast offshore Otway basin flows into Victoria in 2006 and 2007.

promoted the building of a Victoria-SA pipeline was in response to concerns about supply reliability).

In addition, the volume available from the SWP in an emergency is now estimated to be 250 TJ/day, not 200 TJ/day.

However, the main point of disagreement is the application of the failure probability of 0.05%. This has been applied (in Case 2 in the BHP Billiton submission) as if it represented the total probability of a failure for two weeks at any time during the next five years. In fact, the probability of 0.05% as calculated by BHP Billiton, represents the probability of a failure for one whole week, during *any* one week period. Therefore, the probability of one failure, during any of the next 52 weeks, is approximately $52 * .05\%$ or 2.6%. If we used this probability to determine the probability of one failure of a one week duration over the next five years, we would arrive at a figure in excess of 13%, not the 0.05% as suggested by BHP Billiton. To this estimate would also be added the probabilities of more than one failure over the period, which we have not attempted to calculate. Using this revised probability, and the costs of failure in Case 2 of the BHP Billiton submission (adjusted to a one week failure rather than a two week failure), leads to a very significant SSV for the SWP.

Depletion of Gippsland Reserves

BHP Billiton claims that their depletion life calculations contradict the results of the Saturn Report and the ABARE Report, and that the Longford life to depletion is significantly greater than 2024.

However, the “holistic” methodology employed by BHP Billiton is not different to that used by Saturn and ABARE. For example, ABARE calculates a common depletion date for the Eastern Australian reserves of around 2020, rather than field specific dates. GasNet has also independently verified the ABARE results, and stands by both the results of the Saturn report and the ABARE study.