SUBMISSION ON:

APPLICATIONS FOR REVISION LODGED BY GASNET AUSTRALIA (OPERATIONS) PTY LIMITED AND VICTORIAN ENERGY NETWORKS CORPORATION ISSUES PAPER

16 May 2002

Introduction

Pulse welcomes the opportunity to comment on the issues paper on the applications for revision lodged by GasNet Australia (Operations) Pty Limited ("GasNet") and Victorian Energy Networks Corporation ("VENCorp").

In considering any changes to costs that are passed through to retailers, it is important that the Australian Competitions and Consumer Commission ("the Commission") consider, amongst other things, whether retailers are able to pass through those charges to their customers. If retailers are not allowed to pass through any change to GasNet's charges, value would merely be transferred from the retail businesses to GasNet, adversely impacting retailers. In addition, where changes in tariffs are meant to provide market signals to customers to influence their consumption patterns, this benefit cannot be achieved unless the charges are passed through to end customers. Pulse strongly encourages the Commission to consider whether downstream adjustments as a consequence of its decisions are reflected through to the end user.

Pulse does not propose to address every question posed by the Commission in its issues paper but to limit its comments to a few key issues raised by GasNet's proposals.

Proposal to claim easement costs as part of the Capital Base

Pulse opposes GasNet's proposal to claim easement costs as part of their Capital Base. The easements are not assets owned by GasNet and should not be counted as part of their Capital Base. Easements are not routinely considered as part of an owner's asset base which is borne out by the fact that the distribution businesses do not include easement costs as part of their asset base.

Section 8.4 of the National Third Party Access Code for Natural Gas Pipeline Systems ("the Code") refers to "a return on the value of the capital assets that form the Covered Pipeline (*Capital Base*)". That is, for assets to be included in the capital base, they must form part of the "covered pipeline". The definition of "pipeline" in section 2 of Schedule 1 of the Gas Pipelines Access (SA) Act 1997 does not include any land or easements.

Section 8.14 of the Code unambiguously states that "Where an Access Arrangement has expired, the initial Capital Base at the time a new Access Arrangement is approved is the Capital Base applying at the expiry of the previous Access Arrangement adjusted to account for the New Facilities Investment or the Recoverable Portion, Depreciation and Redundant Capital as if the previous Access Arrangement had remained in force". This clearly indicates that a reopening of the Capital Base is not anticipated.

Allowing GasNet to revisit the Capital Base after its initial determination of 6 October 1998 would be inconsistent with the spirit of the Code, which is for the Access Arrangement to provide users with certainty and consistency. Furthermore, given GasNet's own admission that there was no error in arriving at the initial estimation, it is difficult to see how the Commission can justify reopening its previous decision.

The gas businesses were acquired with the 1998 regulatory asset bases and tariffs derived from them. GasNet purchased its business with these parameters in place and should not be permitted to obtain a windfall now by claiming easement costs in the Capital Base. Any such gain will be at the expense of retailers and consumers.

The proposal ignores the relationship between transmission tariffs, distribution tariffs, VENCorp charges and retail tariffs. If GasNet's capital base were to be inflated through this claim, this would result in price shock to customers who are on market contracts and would also impose a cost burden on retailers for those customers on deemed / standing tariff arrangements.

Definition of Services

There is an internal inconsistency in GasNet's submission. GasNet asserts that it has no reference services, yet it is seeking reference tariffs. The argument raised by GasNet against reference services is that it has only one User, that is, GasNet, and that for this reason the inclusion of reference services is not relevant. However, this argument overlooks the fact that GasNet's services are provided to Users through the Service Envelope Agreement with VENCorp. If GasNet's services are deemed not to be reference services, this leaves VENCorp in the invidious position of having to pass through costs negotiated on a commercial basis. It also leaves Users without direct recourse to GasNet in the event of non-performance. Additionally, denying that there are other Users of GasNet's reference services overlooks the number of customers who come directly off the Principal Transmission System.

As a regulated monopoly, services generated by the infrastructure owned by GasNet should be characterised by reference services and reference tariffs.

Pass-through Events

GasNet appears to have significantly broadened the class of pass-through events to include Insurance Events and Regulatory Events. To date, most access arrangements have confined themselves to Tax Events only. The Commission should seek to establish whether this sort of risk-shifting behaviour by GasNet is consistent with the WACC being claimed by the applicant. This is more so the case where GasNet is seemingly not contemplating negative pass-through events. It needs to be noted furthermore that the widening of the definition of events that qualify for pass-through treatment (and hence by-pass Section 2 of the Code) has the effect of bringing in more elements of rate-of-return regulation and is antithetical to the incentive regulation that underpins the Code.

TUoS Zones to be defined by Custody Transfer Meter (CTM)

The TUoS zones are currently defined by postcode. GasNet has made a unilateral proposal to redefine the TUoS zones by CTM. This change would impose a cost on VENCorp to redefine its settlement systems. VENCorp, after early discussions with GasNet, had put through a Retail Gas Market Rules change that obliges distributors to pass postcodes for all 2nd tier basic meter supply points. GasNet has an obligation to the industry to provide a mechanism by which VENCorp can readily assign 2nd tier meters in its Meter Register to the custody transfer meters set out in the Schedule of the draft GasNet Access Arrangement.

In addition, the change to CTM impacts retail systems, including transfer systems. Customer management and billing systems will need to store CTM by customer to allow billing. These changes can be expensive and take time to implement.

GasNet's proposed change from postcode to CTM has not been anticipated and therefore not incorporated into industry planning for FRC. It is therefore out of place for GasNet to be making this proposed change at this late stage in the process. In any case, given industry's commitment to systems activity to prepare for FRC, it may not be possible for industry to implement the change by 1 January 2003.

LNG Reserve

The Market System Operation Rules govern the obligations of VENCorp, GasNet and retailers in relation to GasNet's Liquified Natural Gas (LNG) storage facility. This obligation requires 3,000 tonnes to be held as a strategic reserve for system security. It could be contended that this is a required ancillary service and therefore not subject to normal commercial negotiations.

GasNet is currently undergoing a process to set commercial prices for the balance of its LNG capacity, now that this component is no longer subject to regulated prices under the Tariff Order. Pulse is of the view that it would be improper for GasNet to price this capacity to make up any revenue shortfall from the commercial negotiations mentioned above. Any increase in price to VENCorp would be passed through and would result in increased prices to all consumers.

38% increase in 2003 followed by a real decrease of 4.5% per annum

Pulse is of the view that the proposed increase is unacceptable. The 38% increase in the first year of the arrangement is a consequence of:

- Upward revisions to the Capital Base inherited from the first Access Arrangement
- Lump-sum claim in 2003 for efficiency gains from the first Access Arrangement
- Lump-sum claim for the K factor carry-over.

Notwithstanding the merits of the above claims, a tariff scenario such as this results in unacceptable price shock to retailers and customers. Pulse submits that the lump sums associated with efficiency gains and K factor carryovers should be treated as annuities over the life of the second Access Arrangement. This would avoid the disrupting effects of a step increase in tariffs.