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Dear Ms Kaur

SOUTH AUSTRALIAN GOVERNMENT SUBMISSION ON ACCC DRAFT DECISION "ACCESS ARRANGEMENT PROPOSED BY EPIC ENERGY PTY LTD FOR THE MOOMBA TO ADELAIDE PIPELINE SYSTEM"

The ACCC's draft decision was handed down on 16 August 2000. The Deputy Premier and the Minister for Minerals and Energy were briefed by the ACCC on this draft decision on Friday 18 August 2000. Enclosed is the South Australian Government's submission on this ACCC draft decision. It follows on from the submissions made previously by the Deputy Premier and the Regulator under the *Natural Gas Pipelines Access Act 1995* pertaining to the Issues paper.

The submission contains a number of main points, which are noted below:

- Contractual rights and exclusivity rights after 30/3/95, and relationship to laterals. There is a strong possibility that the draft ACCC decision might overturn existing contractual and exclusivity rights, by redefining certain contractual terms. The SA government has always honoured the principle of sanctity of contracts, for existing contracts covered by the Gas Access Code, as well as to give certainty to future investors in infrastructure in SA.
- Reallocation of contracted capacity in the Moomba to Adelaide pipeline. The current gas purchase contracts between Origin Energy and Terra Gas trader have certain rights to nominate for capacity. The ACCC appear to be proposing such contracted rights might be amended, which would be detrimental to these companies.

- Return on investment. The ACCC draft decision, through (a) a lower than expected WACC, (b) a low initial capital base, (c) an unusual treatment of deferred tax liability which lowers the initial capital base, and (d) a proposed mandatory early review trigger of the access arrangement. The latter point means that if the government's recent request for submissions for a new pipeline actually led to the construction of a new pipeline in SA, then the Access Arrangement would need to be reviewed earlier than expected. This would increase regulatory uncertainty and so has the potential to deter future investment in new pipelines to SA. By striking a better balance between investment opportunities and haulage prices, the ACCC has

the opportunity to create the environment for improved supply security, together with enhanced supply options.

- Regulatory weighted average cost of capital (WACC) allowed is 13.0 % nominal cost of equity or real pretax WACC of 6.7%. This is significantly lower than the real pretax values for WACC allowed by the South Australian Independent Pricing and Access Regulator (SAIPAR) for Envestra in the draft decision of 8.1%, and the 8.25% real for electricity distribution in SA. The Minister for Minerals and Energy commented that "the SA Government does not have any major issues with the WACC proposed by SAIPAR" in his letter to SAIPAR of 14 June 2000. The SA government would be concerned with how such a low WACC might adversely impact new investment in pipelines in SA in the future, as well as future augmentations of the existing MAPS.

- Application of some ACCC's suggested changes to the access arrangement which relate to contractual terms and definitions, in particular with respect to contracted capacity, have the potential to make the normal operation of the existing contracts impracticable and confusing, increasing costs to all involved parties.

- The ACCC is foreshadowing a mandatory section 3.17 early review trigger in the access arrangement, if for example, the Government's recent Request For Submissions for a new pipeline actually led to the construction of such a pipeline in the time of the access arrangement. Such a trigger would (a) significantly increase regulatory risk to Epic Energy, in that there would be no certainty for future income during the remainder of the access arrangement period, (b) deter future investors in new pipelines in SA through creating uncertainty about projected incomes from new investments, and (c) possibly deter future augmentation to the existing MAPS.

- The ACCC has made certain reasons for their decisions confidential, which make independent evaluation of their reasons not subject to scrutiny. It is possible that in doing this the ACCC may be breaching the requirements of the Gas Access Code, and that the draft decision might therefore be defective.

- Technical requirements proposed by the ACCC to be in the access arrangement. Certain proposed requirements may have the impact of affecting safety, and efficient and effective operation of the MAPS.

- A number of pro-competitive suggestions are made with respect to; releasing unused capacity, backhaul, and interruptible services.

Yours sincerely

Hon. Wayne Matthew MP
MINISTER FOR MINERALS AND ENERGY
MINISTER ASSISTING THE DEPUTY PREMIER

8 September 2000

SUBMISSION TO THE ACCC RE. C2000/269
ACCC DRAFT DECISION – "ACCESS ARRANGEMENT PROPOSED BY EPIC ENERGY SOUTH AUSTRALIA PTY LTD FOR THE MOOMBA TO ADELAIDE PIPELINE SYSTEM" –

This submission addresses a number of aspects of the Draft Decision – "Access Arrangement proposed by Epic Energy South Australia Pty Ltd for the Moomba to Adelaide Pipeline System", as specified below.

SANCTITY OF CONTRACTS

BACKGROUND
The policy intent of the Code as derived from the CoAG Communique of February 1994 pertaining to "Free and Fair Trade in Natural Gas" was "that contracts entered into prior to the enactment of any complementary gas industry legislation would, for the duration of those contracts, not be subject to that legislation". Again, in August 1994, CoAG noted its general "commitment to protect existing property rights and contractual arrangements in the development of the new access regime". The complementary gas legislation referred to above is that agreed by CoAG in November 1997 under the Natural Gas Pipelines Access Agreement; and contained in the *Gas Pipelines Access (SA) Act 1997*. Such legislation was enacted more than two years after the commencement of the relevant gas transport contracts between the pipeliner and shippers. It is the SA Government's contention that it was the intention of CoAG and the Parliament of SA to ensure that all aspects of these contracts, including those within the regulatory framework current at that time (ie the Natural Gas Pipelines Access Act 1995) be honoured for their entire period. To do otherwise is indicative of nations unable to ensure the sanctity of business agreements, and establishes an insecure investment climate.

Prior to the sale of the Pipelines Authority of South Australia assets, the South Australian Government sought to put in place the new regulatory approach embodied by National Competition Policy. This new regime was established by third party access Bill, the *Natural Gas Pipelines Access Act 1995* enacted in May 1995. Owing to the closeness of its enactment, and the introduction of the Competition Policy Reform Bill 1995 into the Commonwealth Parliament, its consistency with the Commonwealth provisions was confirmed considerably later, by the then Trade Practices Commission in October 1995.

The South Australian Government agrees with the ACCC view that the sale process should have been informed by CoAG principles, and it is this governments view that such regulatory proposals were complied with in full. Obviously it was not able to foresee the development of a more specific access regime as incorporated into the *Gas Pipelines Access (SA) Act 1997*.

The ACCC makes the assertion in 3.1.5 that the shipper contracts contain "exclusivity provisions" that were agreed post 30 March 1995. It goes onto assert that these clauses permit shippers to hoard unused capacity, and proposes changes on page 124 that may impinge on shippers contractual

rights. Without the reasoning in the ACCC's Annexure 4 being made public it is not possible to be certain on this matter. The Commission was previously informed that the *Natural Gas Pipelines Access Act 1995* provided a clear remedy to the practice of hoarding capacity consistent with that available under Part IIIA of the *Trade Practices Act 1974*.

> The South Australian *Natural Gas Pipelines Access Act 1995* permitted an arbitrator to diminish contractual rights in the situation where such rights were not being utilised (section 36). This section is similar to the effect of S44W (1) of the *Trade Practices Act 1974* regarding a "pre-notification right". The *Natural Gas Pipelines Access Act 1995* remains in operation (except Part 2) in respect of this pipeline until the ACCC approves the access arrangement for the Moomba to Adelaide pipeline. Any dispute brought to the Regulator of the *Natural Gas Pipelines Access Act 1995* prior to such ACCC approval may be dealt with under that Act, and any award made will continue as if it was a determination of an arbitrator under the *Gas Pipelines Access (SA) Act 1997*.

DISCUSSION

It is considered that existing haulage agreements must be honoured fully.

The exceptions to this general policy from within the Code are Exclusivity Rights which arose on or after 30 March 1995. Section 10.8 of the Code defines "Exclusivity Right" as follows:

> **"Exclusivity Right"** means a contractual right that by its terms either:
> (a) expressly prevents a Service Provider supplying Services to persons who are not parties to the contract; or
> (b) expressly places a limitation on the Service Provider's ability to supply Services to persons who are not parties to the contract,
>
> but does not include a User's contractual right to obtain a certain volume of Services.

It would appear from the definition of "Exclusivity Right" that an Agreement, which provides for a certain volume of Services, does not satisfy this definition, and therefore does not constitute an Exclusivity Right. This would appear to be the case even if the quantity of Services contracted for were to have the *effect* of preventing the Service Provider (e.g. by utilising the whole of the available capacity of the pipeline) from supplying Services to other persons.

It is not possible, on the basis of the draft decision in its present form, to accept that any of the current haulage agreements constitute or contain Exclusivity Rights. It is quite possible that even if certain terms in the existing haulage agreements could be construed as Exclusivity Rights and therefore rendered unenforceable, this would still not in itself create additional Spare Capacity in the Pipeline System.

Section 10.8 of the Code defines Spare Capacity in the case of a Pipeline described as a Contract Carriage Pipeline, as the difference between Capacity and Contracted Capacity plus the difference between the Contracted Capacity and the Contracted Capacity which is being used. This in effect means that Spare Capacity is comprised of two separate components.

There would appear to be little doubt that the first component (the difference between Capacity and Contracted Capacity) could, if it exists, be required to be reallocated without breaching any existing haulage agreement. However, it is doubtful whether capacity which is contracted but unused may be reallocated by the powers within the Code without the agreement of existing shippers without overriding the existing agreements. There is no clear power in the Gas Pipelines Access Law (including the Code) for a Relevant Regulator to permanently transfer contracted capacity from one User to another, or to require an existing shipper to "relinquish" any capacity.

The issue of uncontracted capacity in a pipeline should be considered in three fundamental ways, as based on historical precedence of how pipelines are generally operated in Australian and world-wide: (a) on a daily basis, (b) on a medium term basis of say many weeks, and on an annual basis. Purchasers usually have contracted rights to nominate for gas on a daily basis, and are usually subjected to some annual contracted quantity. On a daily basis purchasers can nominate up to a maximum daily quantity (MDQ) subject to their market orders. In the case of the Moomba to Adelaide Pipeline System (MAPS), purchasers have the contracted right to nominate MDQ's which effectively take up the full capacity of the pipeline. This arrangement is efficient in that no excess unused capacity exists for which customers and end users have to pay. In effect all of the costs have been spread across the entire pipeline capacity, rather than being allocated across a reduced amount. On a medium term basis, if a purchaser has no need to nominate for MDQ for say many weeks, and then such unused capacity should be made available to new shippers. This position is supported by the Government, if such transfer of uncontracted capacity does not infringe contractual rights. The existing SA Natural Gas Pipelines Access Act 1995 has provision for removing any hoarded capacity by binding arbitration.

However as noted in the background the Natural Gas Pipelines Access Act provides such a power, as does Part IIIA of the *Trade Practices Act 1974*. Essentially the relevant part of the Competition Policy Reform Bill was recognised in the drafting of the *Natural Gas Pipelines Access Act 1995,* which permitted contracted but unused capacity to be passed through to another party. This component of the 1995 access regime was part of the sale process, and was viewed by the South Australian Government as consistent with National Competition Policy. The diminution of contractual rights proposed (page 124) by the ACCC is viewed as inconsistent with the contractual arrangements at the time of the asset sale. Also, a resolution of the hoarding capacity issue in the manner envisaged by the *Natural Gas Pipelines Access Act 1995* is consistent with maintaining the contractual framework agreed at the point of sale.

A mechanism that is worth considering is to retain the provisions of s 36 (2) of the *Natural Gas Pipelines Access Act 1995* for the length of the current access arrangement period. This would only apply to the Moomba to Adelaide Pipeline System, and could be achieved by amending the *Gas Pipelines Access (SA) Act 1997*. This combined with the current proposal by Epic to provide an incentive to utilise unused capacity is likely to provide the means for a secondary market in such capacity. Unlike the Commission's proposed changes, this approach recognises the sanctity of existing contracts.

FURTHER CONSIDERATIONS

It is arguable that the ACCC's proposals are contrary to the doctrine of privity of contract. This doctrine, in essence, is to the effect that a contract creates rights and obligations only between the parties to it. A contract does not confer rights or impose obligations on a stranger to the contract.

A further matter is whether, if the ACCC (being a Federal body) were to deprive a person of a contractual right, this would constitute an acquisition of property, which, under section 51(xxxi) of the Constitution, must be on "just terms." Currently, this point has not been addressed by the draft decision.

RETURN ON INVESTMENT

BACKGROUND

The South Australian Government strongly believes that the best way to introduce real competition and place downward pressure on prices to gas consumers in the long term is to facilitate basin-on-basin competition. This requires new pipelines to connect new basins to existing markets – much as is envisaged in the Request for Submissions process for New Gas Supply Options for South Australia. Box 1 explains the latest developments on this front within South Australia. If new pipelines are deterred, this competition will not be possible.

Further, given that the only way to attract a new pipeline into South Australia is to allow it to earn the long run marginal cost of entry, a new pipeline may find itself more expensive than MAPS, and as such may have difficulty competing with MAPS for customers. When this is combined with a likely desire on the part of upstream parties to exclude any new pipeline from other basins (and hence a tendency to offer lower cost gas for the period such a threat of competition exists) it is likely to mean that such entry is deterred – again to the long-run detriment of all gas consumers.

DISCUSSION

The future return on Epic's investment in the MAP is essentially determined by the proposed WACC, asset base and depreciation schedule.

The draft decision proposes to reduce this return on new contracts to around 13% pa nominal post tax of the regulated asset base. This represents a reduction of nearly a third from the current nominal post tax return estimated to be 18%. This represents a significant fall in income.

A key issue in this context is whether this return on investment is sufficient to attract new entry into the gas transmission business – that is, to attract new pipelines into the State that could potentially compete with existing supply sources.

A new entrant is likely to enter any market where the returns are expected to be sufficient to cover the long run marginal costs of entry. In the case of a regulated market like gas haulage, entry will be considered if a commercial opportunity exists (ie gas is required to be transported from A to B and customers are prepared to pay for such transportation) **AND** the expected regulated returns will cover the long run marginal entry costs.

The draft decision could impact on expectations among potential new pipeline investors as to the returns they can expect if they enter the gas haulage market. As such, the draft decision contains a low WACC and an approach to determining regulated asset base values which may result in revenues that are lower than the long run marginal costs of providing the service, thereby deterring new pipeline interests.

Box 1: South Australian Gas Pipeline Developments.

Gas demand has been steadily growing in South Australia for a number of years. Recently there have been a number of developments in the South Australian energy market, which provide a window of opportunity for new gas supplies into South Australia. These include:

- The announcement by SAMAG Limited (SAMAG) of its intention to develop a new magnesium smelter at Port Pirie in South Australia;
- The construction by National Power of a 500MW power station at Pelican Point (currently nearing completion), with announcements that National Power is looking into the feasibility of extending this power station to 800MW;
- The opening of the existing gas market in South Australia to supply from new sources due to the fact that a number of contractual commitments with existing gas producers expire over the next 6 years;
- Fast growing demand for electricity (and hence gas) in South Australia.

In 1999, the State commissioned Allens (The Allen Consulting Group) and RISC (Resource Investment Strategy Consultants) to undertake a review of the gas market in South Australia. Around the same time, the South Australian Government undertook a review of energy issues facing the State. As a result, and given the gas market opportunities highlighted above, the State decided that it should take an active role in encouraging the market to develop new gas supplies into South Australia through the development of a new pipeline.

This resulted in the issue of a Request for Submissions for New Gas Supply Options for South Australia on 16 June 2000, intended to facilitate the development of additional sources of gas supply into the State. Seventeen responses were received on 31 July 2000 and six proposals have been short-listed for further development. All six involve proposals for new pipeline infrastructure of various forms.

REALLOCATION OF RELEASED OR SURRENDERED CAPACITY

BACKGROUND

The ACCC's proposed amendment regarding reallocation of released or surrendered capacity is apparently contrary to the intention of section 2.24-2.25 of the Code to preserve pre-existing contractual rights. It is noted though that the Commission does state that any such a capacity release provision should be subject to the provisions of the relevant existing haulage agreements (page 129).

One problem that could well arise in practice with any attempt to require a reallocation of Unused Capacity is the continual reallocation that could follow.

If, for example, a shipper lost a customer and the Service Provider were to transfer capacity to the new shipper in accordance with the ACCC's proposals, the Service Provider would be required to reallocate capacity to the original shipper if the original shipper gained a new customer with a capacity equal to that of the lost customer. It is not clear that the ACCC's proposals could deal with regular customer "churn."

It is also unclear on what legal basis a new carrier would be entitled to any allocation of capacity from an original shipper. It is quite probable that if it were not physically possible to satisfy both contracts, such a contract would be read down or would become unenforceable if the original shipper were to insist on exercising its contractual rights.

The ACCC has acknowledged that "the scope of services that Epic can offer is constrained even without the asserted "exclusivity rights" (page 121).

DISCUSSION

It is considered that there are serious doubts as to whether proposals for reallocation of released or surrendered capacity (pages 125-132 of Draft Decision) are in accordance with the Code, or are practicable. That is, the ACCC has apparently not considered (at least not expressly) that a shipper that loses a dedicated customer is quite likely to be able to utilise the capacity previously used to service that customer, either through servicing an additional customer, or though providing incremental capacity to its other existing customers.

CONFIDENTIALITY OF REASONS

BACKGROUND

It is not possible to make a fully informed submission, as envisaged by section 2.15 of the Code, on issues raised by the ACCC with respect to existing haulage agreements, at least in part because the ACCC has not made all the required information available.

The ACCC considers that the two clauses of the existing haulage agreements between Epic and Terra Gas Trader (TGt) and Origin Energy contain Exclusivity Rights (page 119 of Draft Decision). However, it has not provided further details, beyond stating that they have been identified to the parties only in Confidential Annexure 4. The ACCC states:

> Confidential Annexure 4 identifies the relevant clauses to the parties only, states reasons for the Commission's view that the clauses incorporate exclusivity rights and states the Commission's assessment of their effect on third party access (page 119 of Draft Decision).

There is also stated to be further assessment in Confidential Annexure 4 of the effect of particular clauses and the reason why it is proposed to require particular amendments to the Access Arrangement (pages 120, 121, 124 and 129 of Draft Decision).

DISCUSSION

The effect of this is that some of the reasons that constitute part of the draft decision are outlined in Confidential Annexure 4. It is doubtful whether a Relevant Regulator has the power to issue reasons for a draft decision in a confidential document.

Section 7.7 of the Code requires Relevant Regulators to give reasons for their decisions. It states:

7.7 If the NCC, Relevant Minister, Relevant Regulator or Arbitrator is required under this Code to make a draft decision or a final decision, the NCC, Relevant Minister, Relevant Regulator or Arbitrator concerned must include its reasons in its draft decision or final decision.

The confidentiality provisions in sections 7.11 and 7.12 of the Code refer only to confidential documents furnished by a person to the NCC, Relevant Minister or Relevant Regulator. They do not enable a Relevant Regulator to put reasons in a draft or final decision into a confidential document. Similarly, there is no provision in the Gas Pipelines Access Law (GPAL) which enables a Relevant Regulator to put reasons for a draft or final decision into a confidential document where a document has been provided under section 41 of the GPAL.

The South Australian Government views the proposed changes to the Access Arrangement which flow from the contents of Confidential Annexure 4 (including those listed on page 124) should not be required (see above section), and that if they are to be considered this can only occur after the reasoning for the proposed changes has been fully disclosed.

It is also suggested that because reasons for the draft decision have not, on their face, been presented (i.e. the Draft Decision itself acknowledges that reasons have not been presented for aspects of the Draft Decision) the Draft Decision is defective. Consideration would need to be given by the ACCC as to the means by which this might be remedied. It might be possible to release Confidential Annexure 4 (followed by a further reasonable period to make submissions) or alternatively to issue a fresh Draft Decision which fully outlines reasons for the Draft Decision.

ABILITY TO REVIEW THE ACCESS ARRANGEMENT SUBJECT TO AN EXTERNAL TRIGGER

BACKGROUND

The ACCC is foreshadowing a mandatory section 3.17 trigger in the AA, if for example, the Government's recent Request For Submissions (RFS) for a new pipeline actually led to the construction of such a pipeline in the time of the Access Arrangement Period.

The trigger for early review is normally when there is a material change in circumstance and is at the Service Provider's request (as allowed for by the Code). This Draft Decision raises the possibility that Epic would be obliged to

call for a review if another pipeline is built. A new transmission pipeline could have two effects:

- There could be reduced loads due gas suppliers switching to such a pipeline but the existing contracts should prevent the loss of base income during this access period.
- There could be substantially increased income from back haul if the Government's proposal of Minerva to Port Pirie via Wasleys is adopted.

DISCUSSION

Such a trigger would (a) significantly increase regulatory risk to Epic Energy, in that there would be no certainty for future income during the access arrangement period, especially if contractual terms are overturned, (b) deter future investors in new pipelines in SA through creating uncertainty about projected incomes from new investments, and (c) possibly deter future augmentation to the existing MAPS.

It may be preferable for EPIC to be in a position to respond to new entry in a competitive manner, without the need for a trigger to re-open the Access Decision. Returns set at the long run marginal cost of entry would achieve this objective, with EPIC then having some ability to discount these rates if competition demanded such an action.

It is particularly important that a backhaul service is available, given there appears to be no specific back haul tariff for Wasleys to Port Pirie in the current Access Arrangement proposal. This is of concern as it may be required for the proposed Port Pirie magnesium refining plant.

The Government is of the view that in immature markets, especially where, as in SA insufficient pipeline capacity currently exists to serve the projected requirements of both direct gas users and power generators, that arbitrary ill defined triggers such as those proposed by the ACCC are detrimental to investor confidence, and potentially detrimental to end users in SA in that the security of energy supply is threatened.

COST OF CAPITAL

BACKGROUND

Currently, Epic receives a nominal post-tax return on equity of around 18%; the ACCC decision, were it to have any real force in the initial Access Arrangement Period would reduce this to a nominal post-tax return of around 13%. However it is noted that existing contracts between Epic and Origin and Terra Gas Trader means the 18% return will persist until the existing contracts expire at the end of 2005.

The Draft Decision provides for Reference Tariffs up to 11% lower than those proposed by Epic owing to a reduced return on capital through a lower Initial Capital Base and WACC). This would reduce Epic's revenue in the first year of the AA from $51.2 to $45.7m. As indicated above, due to existing contractual arrangements this reduction is almost 'hypothetical' in nature.

The ACCC has identified further changes to Epic's proposed Access Arrangement in several key areas which include;

- A reduction in the proposed initial capital base ($354m) of $44 million to $310m.
- A proposed pre-tax real WACC of 6.7% which is significantly different to the benchmark of 7.75.

DISCUSSION

The regulatory weighted average cost of capital (WACC) allowed in the draft decision is 13.0 % nominal cost of equity or real pretax WACC of 6.7%. This is significantly lower than the real pretax values for WACC allowed by SAIPAR for Envestra in the draft decision of 8.1%, and the 8.25% real for electricity distribution in SA, notwithstanding the riskier nature of gas transmission assets. The Minister for Minerals & Energy commented that "the SA Government does not have any major issues with the WACC proposed by SAIPAR" in his letter to SAIPAR of 14/6/2000. The relationship and the basis of the post tax nominal WACC and the pre tax real WACC on a benchmarking basis is also of concern.

It is noted that the Commission's goals of enhancing competition in the natural gas industry will have the effect of moving Australian gas pipelines to a more risky position, more akin to their US counterparts. On this basis, it might be argued that a greater risk premium is warranted to reflect the increasing competitive risks faced by the industry.

While it is difficult to extract directly comparable information from the US, evidence suggests that natural gas pipeline allowed returns are greater than those for a pure electricity distribution company. It is understood this reflects the riskier nature of gas pipeline assets.

In view of these factors, the SA government would be concerned that such a low WACC might adversely impact on new investment in pipelines in SA in the future, as well as future augmentations of the existing MAPS.

INITIAL CAPITAL VALUATION:

BACKGROUND

It is noted also that the asset base proposed in the draft decision appears to be at the low end of the range of potential values outlined by the Commission's consultants, who indicate an accuracy of +/- 25% in their estimates. EPIC argued for a capital base of $383m ($June 2000), while the draft decision proposes to reduce this to $310m – a reduction in the order of 19%. On these calculations, Epic's proposed asset base was within the error range indicated by the ACCC's consultants.

Also, the ACCC is proposing to adjust the initial capital valuation for MAPS by an amount equivalent to a deferred tax liability

DISCUSSION

The deferred tax liability concept is unusual in that it appears to be counter to generally accepted accounting practice. It is not clear that the Gas Access Code provides for such an unusual concept. It is understood that some US precedents exist for this proposal. It would be helpful if such precedents could be made public, and the reasons for the proposal are made clear.

The net result of these decisions appears to mean that the returns EPIC can expect to earn under the draft decision (assuming revenues are determined in accordance with the decision, which will not occur in effect until 2006 at the earliest) may be less than that which a new entrant would require to enter the market and build new gas haulage facilities.

BACKHAUL SERVICES

BACKGROUND

The Draft Access Decision makes little reference to the issue of backhaul services, on the basis that there has been no demand for such services to date.

While this is true while no additional pipelines supply gas into Adelaide, one of the issues for a new entrant preparing to enter the market may be the issue of backhaul to supply customers who are located north of Adelaide – for example regional load centres such as Port Pirie.

DISCUSSION

Evidence from the US indicates that rates for backhaul and other exchange services have been a contentious issue. Pipelines in the US are required to offer unbundled rates, including those for backhaul and exchange. Typically, backhaul and exchange services are charged at rates that are lower than forward-haul rates, reflecting the impact of such services on the pipeline system.

It should be noted that the proposed Access Arrangement may allow the application of the FT Services for backhaul situations. This would be unacceptable, as it is not cost or distance reflective. It is therefore argued that a special backhaul service be made available in the final decision. The South Australian Government believes it is undesirable to wait for a new pipeline before consideration is given to backhaul services.

VARIOUS TECHNICAL ASPECTS

A number of specific aspects of the Services Policy, Terms and Conditions, and Review of the Access Arrangement are discussed in Appendix 1. Some of these address the overlap between the license requirements under the *Gas Act 1997* and conditions under the Code.

APPENDIX 1

TECHNICAL COMMENTS OF THE DRAFT DECISION OF THE EPIC ACCESS ARRANGEMENT

1. Principal receipt and delivery obligations of user. Clause 12 Terms and Conditions (page 138).

   The requirement to change the inlet temperature of gas from 71C to 60C is a technical issue and safety should not be compromised. The current acceptance of 71C and the existing cooling equipment was installed after the thorough review following the stress corrosion split on the Moomba to Sydney pipeline. Currently Epic cool the gas through its plant after the receipt point and the cost of operating this plant has been included in the access arrangement. Epic maintains that a lower gas temperature is consistent with cheaper and safer operation. Whilst it is agreed that 60C is a safer operating temperature than 71C and is a pipeline operational requirement, however who cools this gas needs to be carefully assessed. If Epic were to relinquish its current practice through new requirements contained in the access arrangement then it appears that the obligation to cool the gas will be transferred to the production plant operators. This may result in a new cooling plant being constructed thus increasing the cost of gas. The costs for cooling the gas have already been incorporated into the access arrangement and the closure/reduced operation of this plant would provide a windfall to Epic. As the current users are allowed 71C it would be uncompetitive to require a different temperature for new user (provided that the gas enters prior to Epic's cooling plant).

   The government would be concerned if this proposal increased the risk of stress corrosion cracking of the MAPS, and thus threatened security of gas supply to SA consumers. The rationale for the decision should be made explicit in clear technical and economic terms.

2. Gas Quality. Clause 15 Terms and Conditions (page 138).

   The South Australian Government is about to legislate a gas quality specification. This specification has been agreed to nationally. Public consultation with regard to this legislation have been held, including with Epic. Epic's proposed specification should reflect this.

   With regard to out of specification gas, the proposal that Epic is required to describe the steps that it will take to ensure that Users are not adversely affected by the proposed change in specification is a sound one.

3. Imbalance and Zonal Variation Clause 19 Terms and Conditions (page 140).

   The requirement for a maximum imbalance of 8% appears to affect payments and not to affect security of supply. It has been raised that it

may cause disputes. If these disputes were to affect supply then this charge may need to be reviewed. It is also questioned whether any revenues from this have been included in operational income.

4. Allocation of delivery point quantities. Clause 22 Terms and Conditions (page 155).

   The ACCC has concern that there is not provision for the allocation by the service provider in the absence of an agreement between parties as there will be (real time) unmetered facilities in distribution systems. It has invited submissions on this matter. This issue is being addressed by the Technical Regulator's distribution licence conditions in the requirement for a Network Consumer Code. It will be requirement of this Code to have in place an agreed apportionment and balancing system for all gas entering a distribution system (from a transmission system such as Epic's).

5. Interruptible services:

   It is noted by the ACCC that the provision of interruptible services may not be effective. Subject to the discussion on page 5 concerning *medium term unused capacity*, stronger powers to prevent capacity hoarding might improve accessibility to interruptible services.

6. Impacts on Operation of Existing Haulage Contracts amongst Producers, Origin Energy, Terra Gas trader, and Natural Gas Authority of SA:

   In view of the limited time to analyse the impact of the draft decision on the day to day operations of the existing haulage and purchase contracts pertinent to the MAPS, it is strongly suggested that detailed discussions with the operators be held to flesh out any impacts on the operations of the contracts.