

# **TUBRIDGI PIPELINE SYSTEM ACCESS ARRANGEMENT**

## **SUBMISSION BY CMS Gas Transmission Australia 10 December 1999**

CMS wishes to make the following comments in regard to the Access Arrangement and accompanying documentation for the Tubridgi Pipeline System as submitted to OffGAR on the 21 October 1999.

### **1.0 Access Arrangement**

#### **1.1 Virtual Pipeline**

The Tubridgi Access Arrangement treats the 10" Griffin pipeline (PL19) and the 6" Tubridgi pipeline as one "virtual" pipeline. CMS does not accept the principle of the notional resizing of physical assets for regulatory purposes nor does CMS accept that this was ever the intent behind the optimisation methodology referred to in the Code.

#### **1.2 Incentive Mechanisms**

CMS supports in principle the Incentive Mechanisms outlined in Section 3.2.3 as being compliant with the requirements of the Code and appropriate to provide longer term certainty for both Users and Service Providers, as well as providing ongoing incentives for the latter to further improve already comparatively lean costs of operation.

#### **1.3 Negotiated Services Rebate**

The Tubridgi Access Arrangement states that as revenue from Negotiated Services has not been included in the revenue base, a Negotiated Services Rebate to Forward Haul Reference Service Users will occur to the extent that the predicted revenue is exceeded (reference AA Section 3.2.5). Clarification may be required that the revenue base thus defined and from which the Reference Tariff is determined, comprehensively captures all revenue receipts generated by the subject pipelines.

#### **1.4 Queuing Policy**

Under the Tubridgi Queuing Policy, failure to accept an offer of spare capacity within 10 days removes Users from the queue (AA Section 7.3). It is not clear whether the Users lose their place in the queue if the capacity offered does not fully satisfy the User's requirement. This requires clarification.

## 2.0 Access Arrangement Information

### 2.1 WACC

In calculating WACC, the Tubridgi Access Arrangement uses the approximate midpoint between two transformation methods (the “reverse transform” which yields 8.01% and the “market practice” transform giving 9.38% pretax real). CMS notes that it believes the latter practice to be the appropriate methodology, complying with the intent of the Code that regulatory intervention not distort investment decisions and that it should embrace market-based incentives. This approach has been accepted in the Regulator’s Draft Decision for the Parmelia Pipeline.

CMS would also note that the resulting relativity between the WACC values for Parmelia and the Tubridgi pipeline system are an appropriate recognition of the relative levels of commercial risk. However, it is the view of CMS as a proactive investor in the Australian and international energy industry, that the absolute values of regulated returns and the application of the methodology by which these are derived, continues to fall short of a realistic recognition of the commercial factors underlying infrastructure investment decisions. A clear distinction needs to be recognised between what constitutes an acceptable rate of return for pre-existing assets which face future commercial risks but which have already largely realised the benefits for which they were originally intended, and an acceptable risk-adjusted rate of return for an asset which is at the beginning of its intended use. The messages being sent to Industry by the Australian Regulatory community to date have not been reassuring, although the Office of Gas Access Regulation in Western Australia appears to be ahead of other regulatory bodies in this regard.

### 2.2 Beta

The Tubridgi Access Arrangement quotes an asset beta of 0.6 and equity beta of 1.3. CMS merely wishes to comment that the continued trend towards acceptance of industry average values for such surrogate measures of risk amounts to acceptance of the principle of cross-subsidy. Users of pipelines which face higher risks benefit from lower tariffs at the expense of not only capital investors, but also at the expense of Users of pipelines (and even distribution networks) which face lower market risks.

### 2.3 Metering Equipment

Section 3.1.1 of the AAI provides a description of the components of the Reference Service which includes “readings of Metering Equipment at Transmission Receipt Points once each Pipeline Day, with readings provided to Pipeline Users on a monthly basis”, although there is only a requirement of the Service Provider for “the provision and maintenance of Metering Equipment at Transmission Delivery Point”. This seems inconsistent. Further, it is not clear to CMS what is meant by “Transmission Receipt Point” and “Transmission Delivery Point”, nor how these precisely relate to the “User Receipt Point” and “User Delivery Point” meter requirements specified in GTC Sections 5 & 6. While the

latter are required to “continuously and instantaneously measure the Quantity of Gas delivered” through each Point, as a point of principle, CMS suggest that the provision of daily meter readings to Users should be daily rather than monthly as specified in AAI Section 3.1.1 in order for Users to have full access to information which would enable them to manage gas imbalances.

## 2.4 Depreciation

The Tubridgi Access Arrangement states asset lives as being 80 years for pipeline with 50 years for meter stations and 15 years for SCADA/comms. Depreciation for pipeline and meter stations however is based on a 20 year life. The argument presented is to accelerate depreciation in order to reduce the risk of assets being made redundant if future demand fails to materialise (AAI Section 4.1.3). CMS supports the principle espoused by the Tubridgi Parties as being an appropriate and pragmatic response to the recognition of a commercial risk of this nature.

## 2.5 Key Performance Indicator's

Key Performance Indicator's are compared in AAI Table 6 (AAI Section 4.1.4.4). The Tubridgi Access Arrangement concludes that comparisons are “difficult to draw meaningful conclusions from”. CMS concurs with the view that such a simplistic comparison of unit costs is unhelpful, and would further add that such an approach can be potentially misleading as it fails to account for the widely disparate circumstances specific to individual pipelines across Australia, to say nothing of overseas.

## 3.0 General Terms & Conditions

### 3.1 Overruns and MDQ Ratchet Clause

The Tubridgi Access Arrangement provides that if Peak Daily Quantity (PDQ) exceeds the contracted Maximum Daily Quantity (MDQ) not only is the Overrun Rate incurred as a penalty for that day (as one would expect) but the MDQ is also subsequently set at the higher PDQ commencing from the following day (GTC Section 4.4). Effectively MDQ is ratcheted up to be equal to the maximum PDQ on any day, with no apparent downward mechanism nor defined duration. The implication is that a User would potentially continue to be paying a higher than necessary reservation charge long after any short term overrun had occurred. CMS strongly opposes such a mechanism and would urge that it be removed.

### 3.2 Delivery Quantities and Service Provider Indemnity

Section 2.2 of the GTC which deals with Delivery Quantities appears to give the Service Provider indemnity from causing any User imbalance as well as permitting the User to be charged for imbalance even if it was somehow caused by the Service Provider. This seems unreasonable and appears to require clarification.

### 3.3 Gas Specifications

No gas specifications are provided in the documentation. GTC Section 8.1 refers only to “specifications reasonably specified from time to time by the Tubridgi Parties by notice given to the User”. Receipt Pressure is similarly treated in GTC Section 9.1. CMS would query whether or not such specifications should not form a part of the documentation otherwise specified in detail in order to comply with regulatory requirements.

### 3.4 Supply Curtailment

Section 13 of the GTC deals with Supply Curtailment by the Service Provider and gives rise to a number of queries. Section 13.1(d) mysteriously provides for curtailment if there is insufficient gas being delivered into the pipeline system to meet demand. What is the intention? Section 13.1(e) provides for curtailment in response to gas imbalance but does not specify how this should be determined nor provide any tolerance. Should it not? Furthermore Section 13.2 specifies **advance notice** to Users of as little as 14 days for interruptions to service. This seems to be too short. In addition, CMS suggests that advance notice according to a pre-specified annual maintenance plan should be provided to Users.

### 3.5 Invoices

According to GTC Section 14.5 invoices are due for payment within 7 days (with no indication that these should be taken as “business days”). This is too short, especially when GTC Section 18.4 stipulates that if the due date falls on other than a business day, payment is due on the last preceding business day.

### 3.6 Billing Quantity Estimates and Gas Allocation

In the absence of meter readings, billing quantity estimates are specified to be “on whatever basis the Tubridgi Parties consider reasonable” (GTC Section 15.2). CMS would argue that the basis for such estimates should be by agreement with Users. The determination process for Gas Allocation similarly excludes input from the User (GTC Section 15.3 & 15.4) and CMS is of the opinion that it should therefore be amended. Further, it is not clear how this process relates to the mandatory requirement for an Apportionment Agreement between all parties as specified in AA Section 4.3.

### 3.7 Interest penalties

Under GTC Section 19.1 interest penalties unpaid at the end of a month are capitalised and the interest compounds. CMS suggests that this provision should be removed or amended in favour of some more equitable arrangement.

### 3.8 Right to Offset Unpaid Amounts and Suspend Services

GTC Section 19.2 provides individual Tubridgi Parties the right to offset unpaid amounts against “any and all other amounts owing or due” by the User. This appears to effectively link unrelated business transactions and CMS questions the propriety of such a clause. Further, Section 19.3 of the GTC does not allow

for any grace period before the right to suspend services in response to any unpaid amounts due is exercised. This does not seem reasonable.

### 3.9 Bank Guarantee

Under GTC Section 20.3 the User's Bank Guarantee (which is based on MDQ) must be maintained at equivalent to at least 2 months charges under all circumstances. This seems onerous particularly as according to GTC Section 4.4 MDQ is ratcheted up from the day following any excursion of PDQ and that additionally under GTC Section 20.6, failure to meet this condition relieves the Tubridgi Parties of "any obligation to comply with the terms of the [transport] Agreement".

Furthermore, GTC Section 20.4 does not clearly define what restricts the Service Provider from calling on the User's Bank Guarantee in response to even minor transgressions of the User's obligations. It also provides that the Service Provider may call upon the Bank Guarantee without notice to the User. Some modifications appear to be required to this section in order to safeguard the legitimate interests of Users.

### 3.10 Termination of Agreement

Termination of an Agreement can be as a result of failure to pay, breach of obligation, insolvency, reduced credit rating or if "there is any material adverse change, *in the opinion of the Tubridgi Parties*, in the ability of the pipeline User to comply with its obligations..." (GTC Section 21.2). This latter discretion contained in GTC Section 21.2(e) appears to excessively rely upon opinion rather than evidence.

Where a breach of obligation can be remedied, the User has 14 days (specified under GTC Section 21.2(b)) from notification to effect remedial action. CMS would argue that this time limit may prove somewhat short in certain circumstances, for instance where unforeseen replacement parts might have to be procured, transported to a remote location and fitted. A limit of 28 days might be more appropriate.

### 3.11 Decommissioning

Decommissioning of either receipt or delivery points or the entire pipeline system can be effected at the sole discretion of the Tubridgi Parties only requiring that Users be given at least 3 months notice (GTC Section 21.4, 22.1 & 22.2). The form of notice is not specified and CMS suggests that it might avoid potential for conflicts of understanding if it were. It might also be considered reasonable that some form of justification for decommissioning of facilities be provided as part of such notice.

### 3.12 Limit on Claims Against the Service Provider

Claims against the Service Provider are limited to 1 month from time first known or should have become known to User (GTC Section 23.2). CMS contends that this limitation should be removed.

### 3.13 Limited Liability of the Tubridgi Parties

GTC Section 23.3 limits liability of the Tubridgi Parties to separate individual proportions. CMS considers that it may be necessary to obtain legal advice as to whether liability should be “joint and several” given the wording of the rest of the Tubridgi Access Arrangement in regard to the precise nature of any shared liability between the Tubridgi Joint Venture Parties and the Operator acting on their behalf.