

# HUNTER GAS USERS GROUP

4 May 2004

Mr Jim Cox  
Acting Chairman  
Independent Pricing and Regulatory Tribunal  
Level 2, 44 Market Street  
Sydney NSW 2000

Dear Sir,

## **Review of Gas Access Arrangement submitted by AGL Gas Networks**

We refer to IPART's Invitation for Submissions on the proposed revisions to the AGL Gas Networks (AGLGN) Access Arrangement for NSW Network.

### **Hunter Gas Users Group**

The Hunter Gas Users Group (HUG) welcomes the opportunity to present its views to IPART on the AGLGN Access Arrangement.

The HUG represents large and medium-scale industrial gas users from the Newcastle and Hunter region and comprises the following entities: Weston Aluminium, OneSteel, Hydro Aluminium, Tomago Aluminium, Industrial Galvanisers, Orica, The Treloar Group, Lovell Springs and Milltech. The HUG is chaired by Mr Garbis Simonian, Managing Director, Weston Aluminium.

The HUG is supported by a number of regionally-based government and business entities such as the Hunter Economic Development Corporation, Hunternet, the Hunter Business Chamber and the Australian Industry Group.

An effective and competitive market for energy and energy infrastructure services is imperative for the HUG, both for its own competitiveness reasons, but also for its customers, who include the major industrial companies located in the Hunter Valley.

These HUG member companies in aggregate consume over 15 PJ per annum and represent most of the major industrial users of gas in the region.

### **The Price of Gas into the Hunter**

The price of gas into the Hunter region is a major concern for the HUG. Under the Access Arrangement cost and pricing structures, Newcastle – as a major industrial centre located at the end of the AGLGN Trunk main – is at a clear locational disadvantage against other gas consumers located further upstream. HUG member

companies are the most remote gas users and in effect are exposed to the longest supply chain of all users in the State.

This has created a situation where delivered gas prices into Newcastle are the most expensive in the State.

Accordingly, we are primarily concerned with the cost of transporting gas to the Hunter Region on the AGLGN distribution network.

The Hunter Gas Users Group acknowledges the potential for pricing disadvantage which may emerge as a result of locational issues. However, the Group seeks to ensure that any such disadvantage is not exacerbated by unbalanced or unreasonable terms and conditions under the AGLGN Access Arrangement. Accordingly we offer the following comments to IPART as part of its review of the recently submitted Review of Access Arrangement submitted by AGLGN.

### **Headline Tariff Changes**

AGLGN indicated in its public presentation on 19 February 2004 that Newcastle Contract reference charges would fall by an average of 19%. The following table summarises the proposed changes in reference charges:

Reference Charges for Newcastle/Central Coast  
\$/GJ of MDQ per annum

	Current AA 2003/04	Proposed AA 2004/05	% change
<b>Trunk Zone</b>			
Horsley Park	110.431	116.348	5%
Wilton	119.653	116.348	- 3%
<b>Local Network</b>			
<b>Zone 1</b>			
First 200 GJ	150.423	73.044	- 51%
Next 400 GJ	90.254	43.827	- 51%
Next 1000 GJ	60.170	29.218	- 51%
Next 2000 GJ	45.127	21.913	- 51%
Rest	30.084	14.609	- 51%
<b>Zone 2</b>			
First 200 GJ	442.314	312.745	- 29%
Next 400 GJ	265.389	187.647	- 29%
Next 1000 GJ	176.925	125.098	- 29%
Next 2000 GJ	132.694	93.823	- 29%
Rest	88.463	62.549	- 29%
<b>Zone 3</b>			
First 200 GJ	934.943	698.701	- 25%
Next 400 GJ	560.966	419.220	- 25%

Next 1000 GJ	373.977	279.480	- 25%
Next 2000 GJ	280.483	209.610	- 25%
Rest	186.988	139.740	- 25%

The stated 19% average decrease is by no means consistently applied across all zones and therefore customers.

Clearly there is little change in Trunk Charges – in fact they increase for users sourcing gas from a Horsley Park receipt point.

The Local Network Charges vary from a 51% decrease for Zone 1 users to only 29% and 25% respectively for Zones 2 and 3 users.

- **Why is there such a large variation in reductions between the various Local Network zones?**
- **How are these figures derived and are they derived on an equitable basis?**
- **How do the continued high charges for Zones 2 and 3 encourage new industry into the Hunter region?**

### **Valuation of Pipelines**

There is no supporting evidence in the Access Arrangement Information which enables third party assessment of the value of particular assets in the network system. In particular, we refer to the lack of information regarding either historical or replacement cost of pipelines in the Newcastle region.

During the last AGLGN Access Arrangement review, PPK/Kinhill were engaged by AGLGN and prepared a report titled “NSW Gas Networks Depreciated Optimised Replacement Cost”.

Given the lower costs which would be associated with pipeline construction in the Newcastle region (ie predominantly due to easier pipe laying environment), the HUG is keen to ensure that appropriate pipeline valuations support the higher local network charges being imposed on users in the Hunter region.

- **We seek to understand whether a further report has been prepared to review these costs – in particular the unit costs assessed for the construction of pipelines in the Newcastle region versus the Sydney region.**

### **Local Network Capacity Reservation Service**

The Contract Local Network Tariffs are established as outlined in Section 9.2.3 of the Access Arrangement, but are then adjusted for capping of the Reference Tariff (Section 9.2.5) and the rolling in of Decrement customers (Section 9.2.6).

Section 9.2.5 provides that “customers whose price would otherwise exceed the capped rates in Table 9.5” are capped customers and “the shortfall between the expected revenue from these customers and the revenue that would be achieved if they were to pay the Reference Tariff that would have resulted without rolling in is borne by the remaining customers”.

Under Section 9.2.6, “decrement customers are customers whose transportation charge (not including metering components) is discounted as provided under Section 8.43 of the Code and approved by the Tribunal”.

AGLGN states that “decrement and capped customers first cover their Meter and related charges, then their Trunk Charge and part of their Local Network Charge”. AGLGN further states that “shortfalls are calculated on a regional basis so that, for example, a shortfall in the Sydney Local Network will not affect Newcastle’s Local Network price”.

We have concerns regarding the level of costs from capped and decrement customers being recovered under the Local Network Capacity Reservation charge and the implied cross subsidy that results.

It is not clear to us from the Access Arrangement:

- **What is the ongoing level of decrement and capped customer revenue recovered from Local Network Capacity Reservation service customers in the Hunter Region?**
- **What would the resulting decrease in Local Network Capacity Reservation charge be if those costs were removed?**
- **Are capped and decrement customer’s costs relating to Local Network Tariff Service customers included in the Local Network Capacity Reservation charge?**
- **Is IPART satisfied pursuant to section 8.43 of the Code that some or all of any discount given to a capped or decrement customer may be recovered from other system customers?**
- **Why has AGLGN determined that “shortfalls are calculated on a regional basis” and how can that be seen as reasonable?**
- **Is it fair that only system customers in the Hunter Region should bear the cost of capped and decrement customers in that region where a lesser impact could be achieved by smoothing that cost over all customers in all regions?**
- **To what extent does to decision to arbitrarily allocate these shortfalls on a regional basis rather a system-wide basis merely exacerbate the comparatively high network tariffs being borne by Newcastle users?**

We are of the view that it is incumbent on AGLGN and IPART to provide answers to the above questions.

The matter as to whether revenue foregone from capped or decrement customers and recovered in higher tariffs from other customers constitutes a prudent discount under section 8.43 of the Code is debatable. The basis of providing a capped charge appears to be rather arbitrary and not related to the service “not being used by that User” as contemplated by the Code.

### **Trunk Capacity Reservation Service**

We note that Trunk Service Tariffs from Horsley Park/Wilton to the Hunter Region have little changed compared with Local Network tariffs.

At the time the previous Access Arrangement was considered (1999), there were 36 contact customers in the Newcastle/Hunter Region, using 20.362 PJ/year. In 2003 the number of contact customers had increased to 56, using 18.295 PJ/year.

Given the increase in contact customers, we would expect that maximum day demand on that section of the trunk main to have increased providing greater revenue under the Trunk Capacity Reservation Service Tariff to AGLGN. As the trunk tariff applicable to TZ6 is proposed to decrease by 1.5%, while the total transmission cost from Wilton has reduced by 2.8% and the total transmission cost from Horsley Park has increased by 5.4%, we are left to speculate that there must be other factors inhibiting a significant reduction in Trunk Capacity Reservation Service Tariff.

- **Are there any costs related to stranded assets or capped or decrement customers being borne by Trunk Service customers applicable to any of transmission zones?**
- **How does AGLGN explain the proposed trunk charges into the Newcastle zone given the varying influences of decrease in forecast demand, increased contract users and the reduction in Local Network charges?**

### **Postcode Local Network Allocations**

It remains a mystery as to the logic of Assessment Ratings for Postcodes to derive Contract Price Zones. This is particularly concerning to the HUG in relation to the apparent arbitrariness of the allocations but more importantly the pricing implications which result from the such an allocation.

AGLGN and IPART must recognise that the implications for an allocation between Zone 1 and Zone 2 or between Zone 2 and Zone 3 are massive.

The Local Network Unit Charges between Newcastle Zones 1 and 2 differ by a factor of four – ie it is four times more expensive in zone 2 than zone 1. Similarly, it is over two times more expensive between zones 3 and 2.

The following table is drawn from information provided in Attachment 3 of the Access Arrangement Information, which sets out the assessment ratings for postcodes to derive contract price zones:

Postcode	Locality	Calculated Zone	Assigned Zone
2250	Gosford, Somersby	1	1
2256		1.75	2
2259	Wyong, Tuggerah, Warnervale	1.5	2
2260	Terrigal	2.25	2
2261	Berkeley Vale, Long Jetty	2	2
2262	Blue Haven, Budgewoi, Buff Point, Doyalson, San Remo	2.25	2
2285	Cardiff, Edgeworth	1.5	1
2290	Gateshead, Bennetts Green	2.5	3
2294		1.5	2
2298	Waratah	2.25	2
2300	Newcastle	2.5	3
2304	Mayfield, Kooragang	1.25	1
2305	New Lambton Heights	2.25	2
2308	Callaghan, Newcastle University	1.5	1
2314	Williamstown RAAF	2.5	3
2320	Maitland, Rutherford	2.25	2
2322	Tomago, Hexham, Beresfield	1	1
2323	East Maitland, Metford	1.75	2
2324	Raymond Terrace	2.5	3
2325		2.5	3
2326	Weston	2.25	2
2330		2.25	3

This allocation methodology is very arbitrary – and very expensive if a particular user is deemed or assigned to a higher prices Zone.

- **How can in some cases a Calculated Zone of 1.5 be Assigned Zone 1 and in other cases Zone 2?**
- **How can in some cases a Calculated Zone of 2.25 be Assigned Zone 2 and in other cases Zone 3?**
- **Is it fair and reasonable that an arbitrary assessment of a postcode to derive a calculation of either 2.25 or 2.5 should then have a 400% impact on the applicable Local Network Charges?**
- **Where is the financial and analytical rigour which supports the continued use of a completely arbitrary allocation methodology – which then results in a huge financial penalty associated with being “assessed” into zone 2 instead of zone 1 or into zone 3 instead of zone 2? Would not something less punitive and more transparent be more appropriate?**

Furthermore, AGLGN indicated in its public presentation on 19 February 2004 that it was retaining the 2000 AA Postcode boundaries for the purpose of allocating customers to zones. It should be a matter of public record how these allocated postcodes are being applied by AGLGN.

- **AGLGN should provide a copy of those boundaries to interested parties (via IPART) to enable interested parties to verify their decisions – as postcode boundaries have changed since that date.**

### **Regard for Future Developments**

The HUG notes AGLGN's request for an Access Arrangement period to apply through to June 2010. We point out our concern that IPART acceded to AGLGN's request last year to delay the current review process by six months from June 2004 to December 2004 on the grounds of uncertainty regarding the regulatory regime. For AGLGN to follow that approach with a request for a longer Access Arrangement period seems somewhat inconsistent.

The NSW gas market continues to evolve – with various potential development opportunities including potential for gas delivered into the AGLGN network from either CSM developments in the Hunter or northern regions of the State, or potentially even a new major pipeline connection linking gas from SE Queensland into the Newcastle region.

In determining not only the appropriate period for the proposed Access Arrangement but also in relation to the relevance of such future developments on the terms and conditions that will apply during such period, IPART need to have clear regard for such developments, the potential need for backhaul arrangements, connection rules and obligations for AGLGN where third parties may seek to connect to the AGLGN network.

- **The HUG seeks that IPART approve a shorter term than that proposed by AGLGN, and furthermore ensures that there is an ability for IPART to monitor and re-open issues which impact the regulated outcome in the event of major new developments which may impact gas supplies into the region during the term of an approved Access Arrangement.**

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We look forward to participating further in the Public forums and in providing additional submissions during the course of this Review process.

Yours sincerely

Garbis Simonian  
Chairman  
Hunter Gas Users Group