9 June 2000

Mr Luke Berry
National Competition Council
GPO Box 250B
Melbourne VIC 3001

Dear Sir

Draft Recommendation:
Application For Coverage Of The Eastern Gas Pipeline

This submission is made by Woodside Energy Limited (Woodside) in response to the NCC's Draft Recommendation on an application from AGL Energy Sales and Marketing Limited (AGL) for coverage of the Eastern Gas Pipeline (EGP) which is being constructed, and will be operated, by Duke Energy International (DEI). The NCC is simultaneously considering an application from East Australian Pipeline Limited (EAPL) for revocation of coverage of parts of the Moomba-Sydney Pipeline (MSP).

Woodside's interest in coverage of the EGP arises principally from our participation in the Kipper gas field in Bass Strait, offshore Victoria as we, or potential customers for gas from future development of the field, may seek to ship gas via the EGP.

We consider it is in the national interest to facilitate the cost-effective delivery of increasing quantities of gas to the nation's major market regions. To achieve this goal the framework of regulation and the commercial environment must encourage:

- lowest reasonable transmission pipeline tariffs;
- expansion of transmission pipeline capacity; and
- construction of new pipelines linking new or alternative gas fields to these major markets.

Such development will guarantee the supply of gas to an expanding gas market whilst encouraging gas-on-gas competition. It will also ensure that, as the next decade unfolds, reserves remote from the major market areas in SE Australia can supplement the declining reserves close to those markets.

Gas markets need competitive delivered gas prices in order to develop. The delivered gas price comprises two major components; the gas sales price and the transmission tariff. Basin to basin competition will provide much of the potential needed to maintain competitive gas prices. The National Gas Access Code was set up primarily to satisfy the requirement of keeping the transmission tariffs at reasonable levels, in the absence of pipe on pipe competition. The requirement that the transmission tariff be kept at justifiable levels, based on the repayment of the capital spent, has been effective in maintaining tariffs at the lowest reasonable level. This approach has been shown to develop the gas market at a faster pace than any of the previously available regulatory systems eg. in the Western Australian environment.

Woodside is primarily interested in the minimum set of regulation that ensures that the gas consumer is going to have the lowest reasonable delivered gas price available. Accordingly, given the relatively underdeveloped state of Australia's gas pipeline infrastructure, and the desire for competition at all levels of the gas market, Woodside submits that the EGP should be subject to coverage under the code for its entire length. Coverage should be subject to regular review in accordance with provisions of the Code, with the review taking into consideration changes in commercial circumstances that deliver outcomes consistent with a genuinely competitive pipeline environment.

Our comments below relate to the four criteria to be considered by the NCC.

Criterion (a)
That access (or increased access) to services provided by means of the pipeline would promote competition in at least one market (whether or not in Australia), other than the market for the services provided by means of the pipeline.

For the purpose of this discussion the relevant markets comprise the markets for natural gas in the Sydney and ACT region, and regions along the length of the EGP. The crucial elements of increased competition comprise upstream gas supply and gas transportation. It is insufficient to assert that the existence of alternative gas pipeline routes to Sydney, for example, will of itself provide an adequate degree of competition. The EGP and EAPL do not compete in point to point transmission services, they merely have a common termination point, and run in parallel for a minor percentage of their respective lengths.

Access to the pipelines under the Code is the means by which competition will best occur between upstream gas suppliers to the relevant markets. Competition will be promoted to the extent that suppliers in different basins compete with each other (inter-basin) and when suppliers within a single basin compete with each other (intra-basin). Over time this will occur when Kipper is developed, when fields are discovered and developed in recently re-released acreage in the Cooper Basin, and major gas fields in the Timor Sea and North-West Australia are developed and connected. In the medium term, new entrants to gas markets will face high barriers to entry such as the economies of scale of field development. Their ability to compete may be further limited unless they secure access to pipelines on terms at least equivalent to those provided under an Access Arrangement under the Code.

Finally, access will be facilitated if there is a consistent and clear access and tariff arrangement for the entire length of the line. There is little to be gained by a situation where a shipper needs to deal with an Access Arrangement for part of the distance to Sydney, and then to negotiate with either EAPL or DEI for an acceptable tariff for the remaining distance

Criterion (b)
That it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the pipeline.

It is certainly uneconomic to duplicate the EGP at this time. DEI states on page 21 of its submission, "The EGP represents a significant foundation investment with very low levels of capacity utilisation in the early years. Clearly, the pipeline will not generate sufficient revenue to recover the cost of operation, a commercial return and the decline in value of the asset, in the early years."

Given the limited potential, in the short term, for gas market growth in the Sydney area there would be little or no opportunity to gather sufficient market to underwrite a competing pipeline running from Longford to Sydney. Further, once the EGP is operational the incremental investment required to enhance its pipeline capacity by adding compression will be much cheaper than constructing a parallel pipeline. This is alluded to in the DEI submission where Duke "will undertake to expand the EGP to its nominal maximum capacity of 110 PJ/a and maintain the stated tariff path, with the only proviso that each expansion is commercially viable." Typically pipelines can add compression and gain additional capacity at less than the initial unit capital cost. Thus for all practical purposes it would be impossible for another pipeline promoter to build a pipeline in direct competition (that is from Longford to Sydney) with the EGP. Hence the EGP is a natural monopoly for gas sourced from Bass Strait

Criterion (c)
That access (or increased access) to the services provided by means of the pipeline can be provided without undue risk to human health or safety.

There is no evidence to suggest that access will affect human health or safety

Criterion (d)
That access (or increased access) to the services provided by the pipeline would not be contrary to the public interest

Consistency in tariff pricing methodologies between the two pipelines which transport gas to the ACT/Sydney will provide simplicity and efficiency for shippers. The Gas Reform Task Force stated one of its five major objectives as being "to reduce uncertainty for market participants, which is consistent with, but which will reduce much of the uncertainty associated with the largely untested provisions of Part IIIA of the Trade Practices Act that currently may be applied to market participants".

DEI's comments suggest it believes application of the Code leads to tariffs which are too low. This in turn means that, if there is access under Part IIIA of the Trades Practices Act, they will argue vigorously for tariffs which are higher than they expect to be permitted under the Code. Thus access as regulated under the Code would best promote the public interest by yielding tariffs which are lower to the gas consumer and which will result in lower costs for delivered gas.

Contrary to suggestions made by EAPL coverage of both the EGP and the MSP under the code will provide open and transparent information that will allow shippers to achieve access with reasonable transmission tariffs in a timely and efficient manner. It is counter-intuitive to suggest that transparency may lead to collusion.

In contrast to the requirements for regular review of Access Arrangements under the code – at intervals not exceeding five years - DEI's proposed undertaking will run without change for 20 years. Such inflexibility appears to be contrary to the public interest.

Finally, DEI has submitted rules for resolving differences between the ACCC (the Regulator) and itself, and for resolving differences between Shippers and itself. Presumably the same rule would apply if the section downstream of the ACT offtake was covered by a Part IIIA access undertaking. In other words DEI proposes to create a system which does all the things that the Code does other than set tariffs against an established set of criteria, but creates an additional concern. The section in DEI's submission to the ACCC which deals with the ACCC's relationship with DEI (Section 15), attempts to write a set of regulated steps which the ACCC should be compelled to adopt. As the ACCC is the regulator in this matter, any prescribed steps in dealing with concerns or disputes should be the province of regulation. The alternative is clearly contrary to the public interest.

The fact that DEI sees the need to set up these procedures confirms the Gas Reform Task Force's original view of the Part IIIA legislation.

We agree with the NCC's conclusion that access (or increased access) to services provided by the EGP, by means of coverage under the code is not contrary to the public interest.

Conclusion
Woodside believes that the EGP should be covered under the code for its entire length. We endorse the NCC's view that the EGP provides a point to point service: it displays natural monopoly characteristics.

Our comments about coverage of the EGP are made with full consideration of future evolution in Australia's gas transmission system. We wish to see the development of new pipelines encouraged where justified by new markets, new supply sources and economics. To that end we do not wish to discount the opportunity to negotiate gas transportation arrangements on the basis of commercial negotiation in preference to an access undertaking under Part IIIA of the Trade Practices Act, or an Access Arrangement under the Code. We envisage situations where such negotiation may encourage pipeline development that otherwise would not have occurred.

Yours faithfully

J W Schneider
Director Eastern and Northern Australian Gas
Woodside Energy Limited