



30 September 2008

Mr Graeme Cook
Chair, GSOO Steering Committee
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Via email to graeme.cook@vencorp.vic.gov.au

Dear Mr Cook

Scope of a National Gas Statement of Opportunities Industry Consultation Paper

The Australian Pipeline Industry Association (APIA) welcomes the opportunity to respond to National Gas Statement of Opportunities (GSOO) Paper (the Paper) released by the Gas Market Leaders Group on 12 August 2008.

As you would be aware, APIA has provided substantial comment to the initial draft Consultation Paper. This response to the latest Consultation Paper, seeks to reinforce key aspects of the GSOO and incorporate other regulatory developments. APIA supports the broad direction of the Paper in respect of accountability, cost-recovery, timeframes and confidentiality issues.

APIA believes that demand and supply forecasts are the critical elements to facilitating gas market development. A focus by the GSOO on supply and demand forecasting will facilitate ongoing pipeline developments.

It is important to note that gas markets and electricity markets are fundamentally different and, as such, the more centralised approach taken to the Electricity Statement of Opportunities is not relevant to the GSOO.

APIA is concerned that the AEMO Statement of Proposed Approach Paper, recently released by the AEMO Implementation Steering Committee, puts forward a substantially different position relating to use of information and confidentiality of information compared to that proposed in the GSOO Paper, and we seek clarification regarding the two approaches in the two papers.

We look forward to your response.

Yours sincerely

CHERYL CARTWRIGHT
Chief Executive



A.P.I.A. Response to the National Gas Statement of Opportunities Industry Consultation Paper (the Paper)

1. Introduction

APIA agrees that the introduction of a national Gas Supply/Demand statement has merit. In developing the Gas Statement of Opportunities (GSOO), APIA considers the following key points should be recognised:

- The gas market is significantly different from the electricity market and the more centralised planning required for the electricity market is not appropriate for the gas market. This is because:
 - Gas and electricity have very different physical properties;
 - Gas supply is location dependent, i.e. gas supply is not “built”;
 - In the electricity market, electricity transmission infrastructure competes with electricity supply infrastructure. Gas transmission structure complements gas supply infrastructure.

Similarly, the Victorian gas transmission environment, consisting of a single owner and a single operator, is substantially different from the gas market on the rest of the Eastern seaboard and so the GSOO will need to be more cognisant of commercial confidentialities.

- Investment is best served if the GSOO focuses on high-level supply/demand analysis.
- Information available from the Short Term Trading Market (STTM) and Bulletin Board should be utilised, where possible, in order to minimise the cost burden on industry.
- Forecasting demand through hypothetical scenario modeling is not desirable, particularly in an environment where there is real uncertainty regarding the impacts of climate change policy.
- The GSOO should not focus on opportunities in relation to jurisdictions for which the AEMO will not have a statutory responsibility.

2. Basis for GSOO and the Need for the GSOO to Reflect Gas Market Realities

The Paper (p3) states:

“The national gas supply demand statement is intended to provide a long term outlook, over 10 years of demand forecast and supply capabilities, highlighting where potential supply shortfalls or transmission constraints may occur in the future. The purpose is to assist industry and potential new participants in commercial decisions on investment and contracting. It will not form a basis for centralised planning of gas infrastructure”

APIA strongly supports the proposal that the GSOO will not form a basis for centralised planning of gas infrastructure, but has concerns that the structure of the GSOO, as proposed, will establish an unnecessary framework that may allow future central planning.

The fundamental differences between gas and electricity markets are substantial. Whilst centralised planning can have a role in electricity infrastructure, the same does not apply to gas infrastructure.

Key physical and market structure differences between gas and electricity transmission include:

- *Physical attributes* – Gas can be stored in pipelines and other storage facilities, allowing demand fluctuations to be met by stored supply. This creates different planning requirements compared to electricity, where production and consumption need to be instantaneously matched. **Electricity's instantaneous matching requires increased levels of planning and co-ordination which is not required for gas.**
- *Market arrangements* – Gas has less-complicated market arrangements, and consequently requires less planning. This network structure of many electricity transmission assets favours an integrated approach to investment, as beneficiaries of the investment may not be physically located on the site of the investment. In contrast, **the point-to-point nature of many current and expected transmission pipeline assets results in the pipeline assets being commercially underpinned by contractual arrangements** because those who benefit from the investment are typically directly linked to the infrastructure.
- *Production and Transmission* – Gas production occurs at sites where gas is found. The location of gas production is, obviously, unplanned and often needs pipelines to be located in remote areas. The location of electricity production can be planned with reference to current infrastructure and loads. **Investment in electricity transmission competes with investment in electricity generation** as, in many instances, growth in demand can be met via either increased generation or increased interconnection. This means that some co-ordination of planning is required in order to assess whether markets are better served by the construction of an electricity transmission asset or an electricity generation asset. This issue does not arise in gas markets as gas production cannot be shifted. There is no locational choice made by investors in gas production and, consequently, there is no locational choice made by investors in gas transmission. Generally, **gas transmission is complementary to gas production; it does not compete with gas production.**

These differences must be acknowledged when designing the GSOO.

Given APIA's position as outlined above, APIA has concerns that the Paper (p5) details the approach to the Electricity SOO and states:

"The approach to the Electricity SOO has a number of useful comparisons for the approach to a GSOO."

While stressing that there are real differences between gas and electricity, APIA recognises that there are some areas where the GSOO and the Electricity SOO should be developed concurrently to ensure consistent assumptions. These include:

- Economic forecasting - GDP growth etc

- Gas price assumptions - assumed costs for gas are sensitive to the supply/demand position
- Interaction of climate change policy and gas energy forecasts

The GSOO should not form the basis for planning of centralised gas infrastructure and should be designed to explicitly recognise the differences between the gas and electricity industry.

The Eastern Gas market has different dynamics from electricity market processes and, as such, the GSOO must be different in order for it to be effective.

3. Purpose of the GSOO

The Paper (p7) states:

“The National Gas Law sets out an objective to promote efficient investment, operation and use of natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.

Investment in natural gas infrastructure and its operations is undertaken by risk-taking companies. Those companies are accountable to their owners for their decisions regarding investment and operations, and resulting profitability. The GSOO should not be considered a plan for investment, or a forecast of investment, operations or price.”

APIA agrees with this statement.

The Paper (p7) continues:

“However, efficient investment will be assisted by the availability of information on the present position of supply, demand and infrastructure capability including interconnection constraints, and possible future trends. The objectives of a GSOO as set out in the GMLG report are therefore to assist existing industry participants and potential new investors in making commercial decisions on investment in infrastructure and contracting in order to mitigate future risks.”

This statement infers that a major rationale for the GSOO is the mitigation of future risk. Implicit in this position is a view that risk mitigation will facilitate efficient future investment. In designing any GSOO it should be recognised that existing industry participants and new investors already mitigate future risks in order to make commercial decisions, mainly through contracts. This fact should be held paramount when considering the rationale for the GSOO, its design and the appropriate costs imposed on industry in complying with GSOO obligations.

MCE and the GMLG should not rule out other mechanisms to facilitate and encourage future investment, such as a change in the capital expenditure regulatory test.

In considering investment, the Paper (p9) states:

“... the role of the GSOO in providing information to enable efficient decisions on investment and operations does not suggest a need for different treatment of covered and uncovered pipelines, as information on both is likely to be required for efficient decisions.”

While there is some truth in this statement, in the case of regulated pipelines efficiency of investment is subject to tests involving regulators. As such, the information requirements of covered and uncovered pipelines are different. Investment in uncovered pipelines requires sufficient information to meet investment tests for privately owned companies subject to capital market disciplines. Investment in regulated pipelines requires this information and also needs to meet additional regulatory tests. The design of the GSOO should recognise this difference.

The GSOO should be designed to explicitly recognise and complement the fact that gas industry participants mitigate future risks through contracts. Furthermore, while the GSOO could facilitate efficient investment, the design of the GSOO should recognise that in the current competitive market infrastructure investors will probably have different investment requirements (i.e. capital hurdles or regulatory hurdles).

4. Scope of the GSOO

4.1 General Scope

The Paper (p10) states

“It is necessary to consider whether greater emphasis should be placed on demand and supply analysis rather than transmission analysis, or vice versa.

The gas market is less meshed than the electricity market and does not have a similar need to maintain instantaneous balance. This may reduce the need for a national and network wide focus on pipeline investment.”

It is imperative that primary emphasis be placed on demand and supply analysis. The drivers of the gas industry are supply and demand. Unless supply and demand are known, assessment of new or expanded pipelines to link supply and demand is completely irrelevant.

Focusing on pipeline infrastructure at the expense of supply and demand analysis will result in either stranded assets or undersized assets.

Gas transmission pipelines are simply interconnections linking supply and demand, as opposed to electricity transmission infrastructure which has the potential to offer an alternative to electricity generation infrastructure.

As such, the scope of the GSOO should focus on supply and demand levels and growth, rather than infrastructure availability. Under the contract carriage pipeline model, sufficient demand at an economic price will result in investment in pipeline infrastructure.

In considering the GSOO the Paper (p17) states:

“Modeling growth in pipeline capacity will be a complex task. The starting point should be to consult expected users of the GSOO on the transmission and other information they consider would be most useful”

This statement is misguided as it implies that the GSOO will be driven by transmission. This view is incorrect. The **gas** market is driven by **gas supply** and **gas demand**, not by the means of transporting gas. The GSOO should focus on gas, not on the means of transporting gas, which is a secondary issue. Given the commercial drivers which exist in the industry, supply and demand will be linked by appropriate infrastructure at an economic price.

4.2 Scope of Supply and Demand

The gas market is driven by demand. The Paper (p 14) identifies one of the main issues in defining demand as the categorisation of demand by end user (e.g. residential, commercial, industrial and power generation).

APIA believes that in considering demand for the GSOO load characteristics are of primary importance. The identity of the end user is only important to the extent that the end user defines the load characteristics.

In relation to supply the Paper (p16) states: *“It will require significant analysis to develop a reliable assessment of reserves.”*

This information does not necessarily need significant analysis by the GSOO as there are appropriate Commonwealth agencies, including Geoscience Australia, which are well placed to provide such information. In addition APIA believes the apparent difficulty in obtaining this information could be overstated when compared with the difficulty in obtaining demand forecasts.

4.3 Scope of Transmission

APIA accepts that covered and uncovered gas transmission needs to be considered as part of the GSOO. However, APIA is concerned that the Paper unduly focuses on gas transmission issues such as defining capacity and modeling capacity (for example see Paper p11, pp 16-17). Pipeline capacity measurement is well understood and is already public via the Bulletin Board process, Access Arrangements, pipeline licenses and numerous other public documents. The focus should be on improving the definitions and projections of production and demand, rather than finessing issues relating to pipeline capacity.

APIA supports the Paper's (pp16-17) general view that capacity should be treated consistently with the Bulletin Board. By the time the GSOO is introduced there will be one to two years of Bulletin Board data which will provide a robust base for analysis.

APIA supports the Paper's (p17) position that:

.....unlike the Victorian system, transmission pipelines face competition in provision of their services and as such scenario based assumptions are all that can reasonably be projected (i.e. the configuration of existing pipelines may be augmented or diminished based on future demand and supply needs).

The paper makes reference to the Victorian gas Annual Planning Report (APR). Transmission pipelines should not be subject to information demands similar to those

of the Victorian gas APR. The APR is specific to the owner, operator and customers of the infrastructure that cannot be commercially by-passed. The APR is inappropriate for all other States as confidential positions of industry players may inappropriately be exposed. The level of investment in gas infrastructure in other states is testament to the fact that the contract carriage system has provided the necessary infrastructure as required.

APIA has no issue with the GSOO being generally consistent with the key principles and parameters of the APR but would oppose a GSOO which was an expanded version of the Victorian APR.

The GSOO should focus on supply and demand rather than infrastructure availability. The drivers of the gas industry are supply and demand. Unless supply and demand is known then discussion about new or expanded pipelines to link supply and demand is irrelevant.

With regard to these factors, there should be more focus on demand, as ultimately demand drives the market.

5. Issues with Gas Markets and Scenario Modeling

The Paper identifies that, like the Electricity SOO, the GSOO should use a scenario based approach because:

“The level of uncertainty is likely to be greater in gas given the rapid growth in gas use; the ‘lumpy’ nature of demand, in particular in systems with a low level of residential load; and the likely but uncertain rapid growth of gas powered generation”.

Predicting the ‘lumpy’ nature of gas demand through hypothetical scenario modeling and analysis will not provide useful information to the market, particularly as it relates to ‘the likely but uncertain rapid growth of gas powered generation’. The ‘lumpy’ nature of gas demand makes scenario modeling more problematic (and more likely to be wrong) than modeling markets where demand growth is ‘smooth’ rather than lumpy. Thus, scenario modeling is unlikely to address uncertainty surrounding future demand.

New gas powered generators, and other large scale projects using gas, are planned and developed over relatively long timeframes, and the gas production and infrastructure market and market participants have demonstrated their ability to ensure the supply of gas will be available for such projects in a timely manner. Whilst demand appears ‘lumpy’ as new large scale users enter the market, these step changes are not instantaneous and do not catch the market by surprise. APIA does not support the use of scenario based modeling in a GSOO.

In undertaking the GSOO it should be recognised that, over extended time horizons, gas competes with other fuels, such as fuel oil and coal, in many markets, including power generation. Changes in these energy markets will have a major impact on gas demand and supply. This needs to be taken into account in any long term analysis.

In undertaking a GSOO, the competitive situation of gas vis-à-vis these competing fuels needs to be considered. In particular, there needs to be an awareness that, unlike electricity, every gas application can be undertaken by a competing fuel. As such, any GSOO must be sensitive to the confidentiality concerns surrounding 'lumpy' projects.

APIA also considers that in preparing long-term scenarios there is a possibility that other regulatory and commercial processes could be inadvertently impacted. For example, care should be taken that information disclosure to the GSOO does not conflict with Access Arrangements or create issues in relation to ASX disclosure requirements.

APIA supports the Paper's (p11) general approach of having more detailed projections for five years followed by general projections for time frames beyond this. Detailed projections beyond five years are likely to lack credibility.

While there may be sufficient information that can be made public for 5 or maybe 10 years, periods after that are problematic for all participants.

The GSOO should be designed to explicitly recognise that gas competes with alternative fuels.

In addition, given the 'lumpiness' of gas demand, it should be acknowledged that scenario based approaches are unlikely to provide certainty regarding future demand and supply outcomes.

In summary, APIA does not support the use of scenario based modeling in a GSOO.

6. Information Issues

6.1 Sources of Information and the need for new information powers

APIA acknowledges the current information systems reporting on gas transmission pipelines are a useful tool in information provision for demand and supply analysis.

As suggested in the Paper (p18) APIA supports the use of Bulletin Board data for the GSOO as it limits the cost of producing information, however APIA considers it should be the responsibility of the GSOO to collect data already provided to the Bulletin Board rather than demanding industry deliver it twice.

APIA considers that AEMO, in preparing the GSOO, should create linkages such that, to the greatest extent possible, the information required for the GSOO is sourced from information already provided for the Bulletin Board and the STTM.

The Paper (p21) raises issues of obtaining confidential information stating:

"Obtaining reliable data will require access to commercially confidential information. In relation to the Bulletin Board, the National Gas Law and Rules have been developed which set out the obligations of parties to provide relevant information."

An alternative would be to obtain expert opinion from consultants and other commentators on this data....

In the longer term legislative backing may be required to support the GSOO.”

In the first instance, APIA supports the use of consultants, commentators and other public sources of information, such as the Bulletin Board, ABARE etc. Following this, APIA would support the use of existing powers such as the powers of the Bulletin Board. New legislation for information is not necessary. The information necessary to facilitating a workable GSOO is demand information. Such information is unlikely to be improved by introducing new legislation.

6.2 Confidentiality of Information

The Paper (p21) states

The introduction of obligations to provide information for the GSOO will also need to be accompanied by measures to protect the confidentiality of that information and to ensure it is only used for defined purposes. ... Chapter 7 of the National Gas Law provides for protection of information provided to the Bulletin Board operator. This may provide a precedent applicable to information provided for the GSOO.

It is imperative that information be confidential, particularly where speculative or incomplete projects are being considered.

In considering the issue of information provision, the GSOO should recognise other confidentiality and disclosure obligations on organisations such as ASX listing rules, existing contracts etc.

6.3 Uses of Information

The Paper (p21) states

“The introduction of obligations to provide information for the GSOO will also need to be accompanied by measures to protect the confidentiality of that information and to ensure it is only used for defined purposes. “

APIA strongly supports these measures restricting information use to defined purposes. APIA would like to indicate that the AEMO Statement of Proposed Approach Industry Consultation Paper, issued by the AEMO Implementation Steering Committee under MCE, states in its recommendations in Chapter 3 – Information Gathering Powers (p22) that:

“...there does not seem to be any basis for limiting the use for which AEMO may put the information.”

APIA would appreciate clarification of these two apparently contradictory statements in the two papers issued by groups reporting to MCE.

It is imperative that information is only used for the purpose for which it is provided.

6.4 Issues with Information Availability in Markets served by more than one pipeline

The Paper (p9) notes

“... the nature of the systems in different locations will affect the benefits of the GSOO. Market participants and new entrants are likely to face greater difficulties in accessing information and planning in markets with multiple users, supplied by more than one basin and by more than one pipeline.”

This statement is wrong and there is no supporting evidence for it. In competitive markets served by two pipelines ample information is available and new entrants can negotiate with multiple producers and pipeliners, and compare multiple prices and thus be more broadly appraised of their options.

Furthermore, the fact that pipelines in these markets are typically uncovered seems to reinforce the issue that information is not as problematic as the Paper assumes.

Publicly available information should be used at the first instance. If confidential information is required current provisions should be used.

Where confidential information is used it should be kept confidential and only used for the purpose for which it is provided.

7. Geographic and Regional issues

Of the four options (p12) identified for a regional framework for the GSOO, APIA does not consider the suggested NEM state-based approach, a regional centre approach or a state boundaries approach as appropriate for the gas industry.

These approaches are inadequate due to there being very significant interstate gas flows (for example NSW obtains 99% of its gas from interstate), and very significant gas loads outside regional centres. Artificially segmenting the market between different regions or states is unlikely to facilitate efficient outcomes for the eastern gas market.

In designing the GSOO, it should be recognised that the East Coast gas market is becoming increasingly integrated. There are numerous legal precedents in the last decade, most notably in relation to statements made by the ACCC and the Federal Court that support this view.

APIA supports the option put forward of having no geographic disaggregation of supply and demand, and to treat the eastern seaboard as one integrated region.

It is inappropriate for the GSOO to focus on opportunities in relation to jurisdictions for which the AEMO will not have a statutory responsibility such as WA or NT.

8. Environmental policy and the GSOO

The Paper (p11) states:

“The introduction of an emissions trading scheme is likely to lead to an increase in gas powered generation, with large impacts on load. Given the materiality of this issue and its impact on production and pipeline systems it may be desirable for the GSOO to include some reasonably long term scenarios, up to 20 years.”

Given the CPRS is not yet finalised and has not been implemented any major decisions relating to the CPRS and the GSOO are premature. An alternative course of action is to wait until the CPRS is in operation and then make meaningful, evidence-based assessments of its long-term impact.

The Garnaut Climate Change Review Draft Report, in Chapter 17.3 Gas Transmission Infrastructure in Australia, states:

“There is no reason to suggest that existing impediments would be any more significant following the introduction of an emissions trading scheme. Lessons should be drawn from the circumstances that have led to this market operating efficiently without government intervention.”

Garnaut has correctly identified that the gas transmission market has functioned efficiently without government intervention and that the gas transmission market is well placed to deal with the impacts on it of climate change policy. The GSOO should be reluctant to impose solutions prior to allowing the market to arrive at its own solution.

9. Mechanics of GSOO

The Paper (p1) states:

“In December 2007 the Ministerial Council on Energy (MCE) agreed that the development and publication of a GSOO would form part of the Australian Energy Market Operator (AEMO) functions.

AEMO will recover the cost of publication through its fees.”

APIA agrees that AEMO and the GSOO will, and should, be run on a cost recovery basis and be required to set fees for its services and functions. APIA believes those organisations which incur an internal cost in providing information to the GSOO should then have access to the GSOO at no further cost. Therefore, the cost of publication of the GSOO should be recovered through an access fee to organisations that are not required to contribute information to the development of the GSOO.

Conclusion

The GSOO should not form the basis for planning of centralised gas infrastructure and should be designed to explicitly recognise the differences between the gas and electricity industry.

The Eastern Gas market has different dynamics from electricity market processes and, as such, the GSOO must be different in order for it to be effective.

The GSOO should be designed to explicitly recognise and complement the fact that gas industry participants mitigate future risks through contracts. Furthermore, while the GSOO could facilitate efficient investment, the design of the GSOO should recognise that in the current competitive market infrastructure investors will probably have different investment requirements (i.e. capital hurdles or regulatory hurdles).

The GSOO should focus on supply and demand rather than infrastructure availability. The drivers of the gas industry are supply and demand. Unless supply and demand is known then discussion about new or expanded pipelines to link supply and demand is irrelevant.

With regard to these factors, there should be more focus on demand, as ultimately demand drives the market.

The GSOO should be designed to explicitly recognise that gas competes with alternative fuels.

In addition, given the 'lumpiness' of gas demand, it should be acknowledged that scenario based approaches are unlikely to provide certainty regarding future demand and supply outcomes.

Publicly available information should be used at the first instance. If confidential information is required current provisions should be used.

Where confidential information is used it should be kept confidential and only used for the purpose for which it is provided.