the australian PIPELINE industry association Ltd

13 May 2011

Australian Energy Market Commission
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Via web submission

STRATEGIC PRIORITIES FOR ENERGY MARKET DEVELOPMENT

The Australian Pipeline Industry Association (APIA) welcomes the opportunity to comment on the Australian Energy Market Commission's (AEMC's) Strategic Priorities for Energy Market Development Discussion Paper.

There are several issues that APIA would like to raise for the Commission's consideration, even though the matters are broader than the AEMC has indicated in regard to the Discussion Paper. APIA strongly believes that these issues should be considered by the AEMC.

Ensuring the transmission framework delivers efficient and timely investment

APIA supports the identification of the transmission framework as a strategic priority for the AEMC, and notes that there is currently a Direction Paper open for consultation on this issue.

The Direction Paper makes a brief mention of gas transmission on page 39:
There are a range of factors that influence the locational decisions made by generators, including access to fuel sources, the costs of transmission losses and the risk of constraints. However, generator proponents currently see no explicit price signal of the costs of any associated network augmentation (beyond directly incurred connection costs). This lack of price signal means that trade-offs between the costs of transmission and the costs of generation (potentially including the costs of alternatives to electricity transmission, such as gas pipeline costs) may not be appropriately made. However, the extent to which this will have an impact on efficiency will depend on the materiality of the associated network costs as a proportion of the total costs incurred by the generator.

APIA considers that generators will increasingly focus on the trade-off between gas transmission and electricity transmission in making locational decisions, as gas fired power generation increases the

role it plays in Australia's generation mix. This increase is alreay occurring and is predicted to continue. The differences in the frameworks between the two markets could lead to poorer economically and energy efficient decisions by generators.

In particular, APIA is concerned that when making a locational decision, a generator does not have to consider the congestion created on the electricity transmission network as the costs of this increased congestion are shared xxxxx. This is in contrast to the gas transmission network, where it is likely that the generator will be required to fund all or part of possible pipeline upgrades that might be necessary to meet its gas demand.

APIA supports the case for a transmission charge based on the effects of a generator's locational decision on network congestion and notes the AEMC has identified this as issue for further consideration.

Encouraging increased efficiency of investment in gas transmission

APIA considers there is potential to improve the efficiency of investment in gas transmission infrastructure in Australia. Current investment practice is to build new pipelines or expand existing pipelines with sufficient capacity to meet contracted demand. As pipeline capacity can be readily expanded through compression, incremental expansion is relatively easy to achieve. However, the maximum capacity of the pipeline remains limited by the size of the pipe initially installed.

Investment in larger diameter pipes than would otherwise have been used in the initial construction of a new pipeline or the looping of an existing pipeline should deliver positive outcomes for the Australian economy:

- It should lead to longer term lower transmission costs to gas users. The incremental cost of increasing the diameter of pipe used initially is much lower than that required to loop the pipeline at a later date.
- It should lower the emissions intensity of gas transmission. The biggest contributor to a pipeline's energy usage and emission intensity are its compressors. A larger diameter pipeline requires less compression than a smaller diameter pipeline to deliver the same capacity. With the likely introduction of a carbon price, lessening the emissions intensity of a pipeline will also lead to lower transmission costs.
- It should lead to more efficient use of scarce skills and workforce resources. The gas supply industry in Australia faces increasing skills shortages and workforce issues. With the use of gas in Australia forecast to double by 2030, the workforce will be in high demand. The construction of fewer, larger pipelines would place less strain on this workforce than the construction of more, smaller pipelines.

A concern for gas transmission companies currently limiting the case for the construction of expensive spare capacity is regulatory risk. The Australian Energy Regulator may be asked to make a determination on access to the spare capacity and set a tariff for the spare capacity lower than that paid by the foundation customers of a project. Many gas transportation agreements provide for foundation customers to have their tariffs lowered if any subsequent customers pay a lower price. To mitigate the risk that revenues will be reduced as a result of a regulatory price flowing through to foundation shippers, no spare capacity is built into expansions.

APIA believes that the introduction of mechanisms that address the regulatory risk presented to pipeline investors by spare capacity will result in investors giving greater consideration to its construction.

Treatment of carbon costs in access arrangements

There is an emerging issue in regard to the introduction of a carbon price mechanism and the ability of regulated gas transmission pipelines to pass those costs through to shippers: that of the economic regulators' ability to influence the extent to which carbon costs can be passed through.

There have been indications that economic regulators of infrastructure will decide an efficient level of carbon costs an infrastructure owner will be allowed to pass through to its customers[1]. Economic regulators have determined that pipelines cannot include clauses in access arrangements that enable costs associated with a carbon cost are automatically pass through. Such a declaration is a disturbing development and is not unique to gas transmission pipelines.

It is not appropriate for economic regulators to make judgements about efficient costs associated with a carbon price mechanism. In the worst case, an economic regulator may make judgements in hindsight in relation to the efficiency of carbon reduction options, determining that a pipeline could have reduced or offset emissions differently and thus not allowing recovery of costs that were deemed prudent at the time.

There already exists an opportunity for vigorous debate regarding efficient costs. This occurs during economic regulatory determinations, and it would not be appropriate for companies to engage in further debate regarding efficient carbon costs as this would significantly add to the complexity of regulatory determinations and the costs of determinations.

With the present Government committed to the introduction of a carbon price mechanism, it is appropriate the Commission consider how costs associated with such a mechanism should be treated in regulatory frameworks for both electricity and gas.

If you would like to discuss any of these issues further, please contact APIA on (02) 6273 0577 or sdavies@apia.asn.au.

Yours sincerely

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on behalf of

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[1] The Australian Energy Regulator's draft decision on the Amadeus Gas Basin Pipeline access arrangement proposal, dated 21 April 2011 -
The Western Australian Economic Regulation Authority draft decision on the DBNGP access arrangement proposal, dated 14 March 2011.