SUBMISSION 54: Operating Expenditure

[redacted]

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1. INTRODUCTION

1.1 On 14 March 2011, the Economic Regulation Authority (ERA) made its draft decision (Draft Decision) in relation to the full access arrangement proposal filed by DBNGP (WA) Transmission Pty Ltd (DBP) on 1 April 2010 (Original AA Proposal).

1.2 The Draft Decision indicates that the ERA:

(a) is not prepared to approve the Original AA Proposal; and

(b) requires 109 amendments to the Original AA Proposal in order to make the access arrangement proposal acceptable to the ERA.

1.3 The Draft Decision also fixes a period for amendment of the Original AA Proposal (**revision period)**, which revision period expired on 18 April 2011.

1.4 On 18 April 2011, DBP submitted the following documents pursuant to Rule 60 of the NGR, which make up the amended access arrangement proposal (**Amended AA Proposal**):

(a) Amended Proposed Revised Access Arrangement; and

(b) Amended Proposed Revised Access Arrangement Information.

1.5 Rule 59(5)(c)(iii) of the NGR requires the ERA to allow at least 20 business days from the end of the revision period for submissions to be made (in relation to both the Draft Decision and the Amended AA Proposal). The ERA has advised that interested parties are able to make submissions on the ERA's Draft Decision up until 4:00pm (WST) Friday 20 May 2011.

1.6 While DBP has submitted to the ERA that the Amended AA Proposal contains the information that the NGA (which includes the WA National Gas Access Law text (**NGL**) and the National Gas Rules (**NGR**) requires to be included in order to enable it to be approved by the Economic Regulation Authority (**ERA**), on 18 April 2011, DBP also submitted that DBP will also be filing the following supporting submissions that explain and substantiate the amendments and additions in the Amended AA Proposal that have been made to address various matters raised in the Draft Decision:

(a) Submission (47) Revised Amended Access Arrangement Proposal (this was filed on 18 April 2011)

(b) Submission (48) Overarching

(c) Submission (49) Response to Specific Amendments

(d) Submission (50) Reference Service

(e) Submission (51) Terms & Conditions

(f) Submission (52) Opening Capital Base

(g) Submission (53) Capital Expenditure

(h) Submission (54) Operating Expenditure (being this Submission)

(i) Submission (55) Rate of Return

(j) Submission (56) Other Tariff Matters

(k) Submission (57) Non Tariff Matters

1.7 In this Submission, DBP both substantiates its amendments and additions made in the relation to the operating expenditure in the Amended AA Proposal and responds to the following aspects of the reasoning in the Draft Decision relating to operating expenditure:

(a) The approach to assessing whether the forecast operating expenditure met the requirements of the NGL and NGR as they apply to operating expenditure;

(b) The contractual incentives applying to DBP to incur only prudent and efficient operating expenditure;

(c) DBP's assumptions concerning the forecast operating expenditure associated with the operation of the BEP;

(d) Prudence and efficiency of items of actual operating expenditure in the 2005 to 2010 access arrangement period;

(e) Prudence and efficiency of forecast operating expenditure in the 2011 to 2015 access arrangement period;

(f) Verification of actual operating expenditure in 2005 – 2010; and

(g) Variances in proposed operating expenditure between DBP's Original AA Proposal and its Amended AA Proposal.

1.8 DBP also has issues with the manner in which the ERA has both exercised its discretion in relation to its assessment of this element of the Access Arrangement (ie operating expenditure) and undertaken its task under the NGL and NGR of assessing the relevant provisions of the Original AA Proposal's compliance and consistency with the requirements of the NGL and NGR. This matter is addressed in more detail in submission 48 filed on or about the date of this submission. Throughout this submission, DBP draws the ERA's attention to this point.

1.9 As a final introductory matter, DBP also has issues with the manner in which the ERA has both exercised its discretion in relation to its assessment of the elements of the Access Arrangement relating to the operating expenditure and undertaken its task under the NGL and NGR of assessing the relevant provisions of the Original AA Proposal's compliance and consistency with the requirements of the NGL and NGR that relate to the operating expenditure. This matter is addressed in more detail in submission 48 filed on or about the date of this submission. Throughout this submission, DBP draws the ERA's attention to this point where relevant.

2. ERA'S APPROACH TO THE ASSESSMENT OF OPERATING EXPENDITURE

2.1 Rule 91 of the NGR requires, as the ERA noted in paragraph 787 of the Draft Decision that:

Operating expenditure must be such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services.

2.2 In paragraphs 797 to 800 of the Draft Decision, the ERA set out its approach to the assessment of whether DBP's forecast of operating expenditure for the Original AA Proposal satisfied the criteria of Rule 91. That approach comprised the two steps set out in paragraph 800:

(a) an assessment of whether actual operating expenditure in the period 2005 to 2010 was consistent with the criteria in Rule 91, which the ERA referred to as the "prudence and efficiency criteria" of Rule 91; and

(b) an assessment of whether DBP had provided adequate justification for forecast trends and step changes in levels of expenditure over the access arrangement period (2011 to 2015).[1]

2.3 DBP makes submissions in relation to a number of aspects of this approach.

The relevance of historical operating expenditure in assessing the prudency and efficiency of forecast expenditure in the case of the DBNGP for the AA Proposal

2.4 DBP contended, in submissions made prior to the Draft Decision, that the ERA should not place significant weight on DBP's operating expenditure in the period 2005 to 2010 and moreover, it should not be the sole basis for assessing the prudency of DBP's forecast operating expenditure.

2.5 The ERA concluded, in paragraph 798 of the Draft Decision, that it did not accept DBP's contention that referring to historical expenditure was inappropriate. It should be noted (as demonstrated in the immediately preceding paragraph) that DBP did not, in fact, make this contention in its submissions.

2.6 Notwithstanding this, while the ERA accepted that substantial pipeline expansion had taken place during the period 2005 to 2010 and would affect operating activities and costs, the ERA concluded that operating activities and costs during the period 2005 to 2010 should be taken into account in justifying the forecast costs for the period 2011 to 2015 (Draft Decision, paragraph 799).

2.7 Furthermore, the ERA then went on to say that because it was of the view that the scheme of incentive regulation established by the NGR, which (according to the ERA) allows the service provider to capture the benefits of outperforming the cost forecasts used for reference tariff determination, this justified the ERA placing considerable weight on actual expenditure as an indicator of an efficient level of forecast expenditure (Draft Decision, paragraph 798).

2.8 DBP does not disagree with the view that the regulatory regime of the NGL and the NGR provides incentives which ensure that actual costs are at or near their efficient levels.

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[1] The second bullet point of paragraph 800 of the Draft Decision referred to levels of capital expenditure. DBP presumes the reference to "capital" is an error.

2.9 Nor does DBP disagree with the view, set out in paragraphs 805 to 809 of the Draft Decision, that although its revenues are not determined by the reference tariffs of the regulatory regime, its standard shipper contracts similarly provide strong commercial incentives for prudent and efficient levels of expenditure.

2.10 DBP is, however, concerned – and has previously indicated its concern to the ERA, and to its engineering advisor – that extrapolation of past efficient costs should not be solely or heavily relied on by the ERA in assessing the prudency and efficiency of forecast expenditure, particularly in circumstances of major changes in asset scale, asset configuration and in ownership and organisational arrangements.

2.11 Notwithstanding the above, DBP has made some submissions on the prudency and efficiency of some aspects of its historical operating expenditure for the period 2005-2010 in section 5 of this submission.

Was the operating expenditure for 2005 to 2010 prudent and efficient in accordance with Rule 91 and did DBP attempt to demonstrate this?

2.12 In paragraph 802 of the Draft Decision, the ERA noted that neither the revised Access Arrangement Information, nor DBP's submissions in support of its forecast of operating expenditure, addressed the efficiency of operating expenditure during the period 2005 to 2010.

2.13 There was, however, no reason for DBP to address the issue.

2.14 Rule 72, which governs access arrangement information, requires only that, if the access arrangement period commences at the end of an earlier access arrangement period, the access arrangement information must include operating expenditure (by category) over the earlier access arrangement period (Rule 72(1)(a)(ii)). It does not stipulate that DBP must address the issue of whether that historical operating expenditure is prudent and efficient in the access arrangement proposal. DBP's proposed revised Access Arrangement Information included operating expenditure, by category, for the period 2005 to 2010.

2.15 As to the claim that DBP's initial submissions made at or about the time of the filing of the Original AA Proposal didn't address the issue of whether the historical expenditure was efficient and prudent, although Rule 91 requires that forecast operating expenditure must be prudent and efficient, it does not dictate the way in which the prudency and efficiency of forecast expenditures are to be assessed. As DBP advised in submissions, its forecast of operating expenditure for 2011 to 2015 was built up from its expectations concerning levels of activity required to operate and maintain, during the period 2011 to 2015, a pipeline system which had been almost fully looped since 2005, and which could now provide around twice the capacity which was provided in 2005. DBP sought to demonstrate, in its submissions, that this forecast of operating expenditure was prudent and efficient with reference to the scale of its current operations.

2.16 There is no regulatory requirement for DBP to establish the prudency and efficiency of its forecast operating expenditure by reference to historical levels of expenditure, and DBP did not seek to do so (although note section 5 of this submission which does contain some submissions on the prudency and efficiency of certain items of operating expenditure).

2.17 Moreover, as has been previously outlined by DBP, because of the major changes in asset scale, asset configuration and in ownership and organisational arrangements that have occurred since 2005, little, if any, weight should be attributed to historical expenditure in determining what is efficient and prudent forecast expenditure.

2.18 Accordingly, DBP did not consider that this task was relevant to assessing the prudency and efficiency of forecast operating expenditure.

2.19 In paragraph 810 of the Draft Decision, and in Table 51, the ERA compared actual operating expenditure for the period 2005 to 2010 with the forecast which had been made for the proposed Access Arrangement revisions in respect of which the ERA issued a Further Final Decision in December 2005. The ERA noted that expenditure on fuel gas was substantially (22.2%) less than had been forecast. Other operating expenditure was approximately $7.7 million (2.5%) above the corresponding forecast.

2.20 The ERA advised, in paragraph 811, that:

While requests were made to DBP to provide explain [sic] the differences between forecast and actual operating expenditure, no explanation was forthcoming.

2.21 Furthermore, the ERA noted (in paragraph 811) that its expert engineering advisor had advised that DBP did not use activity based costing, which would have provided greater clarity on the allocation of operating expenditure to different activities and drivers.

2.22 That an explanation of the differences between forecast and actual operating expenditures was not forthcoming is not correct, and the purported advice offered by the ERA's engineering advisor is irrelevant and misleading.

2.23 DBP had advised the ERA, and had advised the regulator's engineering advisor in July 2010, that:

(a) the scale of the pipeline operation had changed significantly since 2005;

(b) the DBNGP ownership and organisational structures which existed prior to 2009 were totally different from those which were in place during 2010, and from those which are expected to be in place during the period 2011 to 2015;

(c) prior to 2009, pipeline service company Alinta Asset Management and its successors, which provided services to a number of pipeline systems across Australia, had provided, at the direction of a small team of DBP senior managers, a wide range of operational and capital project management services to the DBNGP;

(d) Alinta Asset Management and its successors had billed DBP for services provided to the DBNGP, and had provided detailed support for its billings, but not in a form which now allows the billing data and related information to be aligned with the costing and reporting systems which DBP has developed and used to manage a pipeline business which no longer relies on a major external contractor for operational and construction activities, and which now has developed the people, facilities and systems required to undertake these activities internally;

(e) Alinta Asset Management and its successors, which had earlier provided services to DBP, no longer exist, or have been merged into entities which are no longer related to DBP;

(f) the approach to assessing the prudence and efficiency of DBP's operating expenditure forecasts for 2011 to 2015, which was subsequently described in paragraph 800 of the Draft Decision (and which is noted in paragraph 2.2 above), had limited prospect of success; and

(g) Rule 91 did not require the approach which the ERA and its engineering consultant proposed to use in assessing the prudence and efficiency of DBP's operating and expenditure forecasts for 2011 to 2015, and an alternative approach was required which drew on DBP's financial planning and budgeting.

2.24 Having advised the ERA and its engineering advisor of the difficulties, DBP provided, in its Submissions 16, 17 and 44, the limited information which was available, and provided the explanations which could reasonably be made on the basis of that limited information. On the basis of what DBP provided, the ERA was able to make the observations it reported in paragraphs 816 to 822 of the Draft Decision. The ERA's statement that no explanation of the differences between the 2005 forecast (for 2005 to 2010 expenditure) and actual operating expenditures (for the 2005 to 2010 period) was forthcoming is not correct.

2.25 Advice given to the ERA, by its expert engineering advisor, that DBP did not have activity based costing, was irrelevant and misleading. The ERA and its consultant sought to look back to the period 2005 to 2010. What costing systems DBP should have had in place during that period is largely irrelevant. The costing of activity was, for most of that period, undertaken by Alinta Asset Management and, later, by its assigns and successors. Certainly, DBP might have adopted an activity based costing system when activity was "internalised" in 2009, and might have used that system for the purpose of preparing its forecasts for 2011 to 2015. However, the way in which these forecasts were prepared seems to have been of limited interest to the ERA and its engineering advisor because they had already decided on an approach to the assessment of the prudence and efficiency of those forecasts which relied on the use of prior actual expenditures even though such an approach was not required by Rule 91, and, as submitted by DBP, of limited relevance given DBP's and the DBNGP's circumstances.

2.26 Activity based costing is one among many approaches to the planning and monitoring of resource use within a business. Whether activity based costing is superior in environments where multiple organisational processes and systems support resource planning and use is much less clear. The availability of alternatives may be the reason why adoption rates for activity based costing have been relatively low, and appear to be declining. The implementation of activity based costing requires significant organisational and reporting system changes, and is costly. Before it is implemented, the potential net benefits must be clearly identified.

2.27 The ERA's engineering advisor has advocated DBP's adoption of activity based costing without having made any assessment of either the costs or the potential benefits. Moreover, the advisor made no overall assessment of DBP's resource planning, allocation and monitoring processes to assess whether, in the particular circumstances of the business, these may be superior to activity based costing. The implication, of paragraph 811 of the Draft Decision, that DBP's processes are deficient because activity based costing is not used, is misleading.

The ERA and Halcrow appear to have adopted a pre-determined approach, being that the opex for one of the years in 2005-2010 should be a baseline for future opex

2.28 The fact that the ERA has focused so heavily on assessing the actual expenditure for 2005-2010 and has, together with its consultant, used the expenditure from one of those years as a benchmark to assess the prudency and efficiency of forecast expenditure in any of the years from 2011 onwards indicates that the ERA has adopted a pre-determined approach to the establishment of what are prudent and efficient operating costs for 2011 to 2015 – being that the operating expenditure for one of the years in 2005 to 2010 should be a baseline for future expenditure.

2.29 DBP has made previous submissions on this point (see for example, submission 44) and does not intend to repeat them in this submission.

3. CONTRACTUAL INCENTIVES FOR DBP TO BE EFFICIENT AND PRUDENT WITH REGARD TO OPERATING EXPENDITURE

3.1 In paragraphs 801 to 809 of the ERA's Draft Decision in considering DBP's actual operating expenditure for the 2005 to 2010 period, the ERA conclude that expenditure is consistent with governing criteria for operating expenditure in rule 91 of the NGR

3.2 In reaching this conclusion, the ERA relies predominately on accepting that DBP faces commercial incentives for efficiency in operating expenditure. The ERA state that incentives arise from:

(a) The ability of the service provider to retain the benefit of out-performing forecasts of operating expenditure that are taken into account in the determination of reference tariffs (at least to the extent that users of the pipeline are paying tariffs at the level of the reference tariffs);

(b) The inability of the service provider to recover, through regulated tariffs, any operating expenditure in excess of the forecast expenditure (again, at least to the extent that users of the pipeline are paying at the level of the reference tariffs).

3.3 The ERA adds to this line of reasoning by clarifying that while users of the DBNGP do not currently pay the reference tariff, the terms of the SSC or the provision of pipeline services would provide commercial incentives for prudence and efficiency in operating expenditure.

3.4 The ERA states that it considers that these incentives operate similarly to the incentives that exist under the regulatory regime established by the NGL and NGR.

3.5 DBP agrees with the ERA's conclusion that this is a relevant consideration in dealing with actual operating expenditure for the period 2005-2010.

3.6 The ERA however, does not extend this reasoning to DBP proposed forecast of operating expenditure for the period 2011 to 2015.

3.7 DBP submits that it is a relevant consideration that the ERA should take into account in its assessment of the prudence and efficiency of the forecast operating expenditure for the period 2011 to 2015 and, in fact, should be given significant weight in assessing compliance with Rule 91 of the NGR.

3.8 This is so for the following reasons. Under the SSCs, for the period 2011 to 2015, there is an even greater incentive on DBP to be as efficient and prudent in its expenditure as is possible (when compared to the period 2005 to 2010) because:

(a) under the SSC tariffs remain fixed with the exception of:

(i) Escalation for inflation (CPI-X mechanism from 2012)

(ii) Changes for taxation

(iii) Adjustments (increase or decrease) in respect of certain amounts of expansion capital expenditure, calculated as a rate of return on a difference between actual expansion costs and certain benchmarks of expansion costs specified in the SSC.

(b) From 2012, DBP's tariff will decrease on an annual basis in real terms (all other things being equal) because the escalation is only increased by a CPI-X factor, with the x factors are expected to be at or near inflation. In fact, there is a possibility that the "x" factor (2.5%) may be even greater than the inflation rate. This will create even further pressure on prices for DBP further supporting the logic that the SSC provides commercial incentive for costs to be prudent and efficient.

4. OPERATNG EXPENDITURE ASSOCIATED WITH THE BEP LEASE

4.1 In paragraph 168 of the Draft Decision the Authority presumes operating and capital costs for the BEP are included in the forecasts of capital and operating expenditure for the entire DBNGP for the 2011 to 2015 access arrangement period. In paragraph 177 of the Draft Decision, the ERA then queries whether the whole of the operating and capital costs forecast to be incurred by DBP in the operation and maintenance of the BEP from 2011-15 should be included in the forecasts of costs used to calculate total revenue given that DBP leases only part of the capacity of the BEP for the provision of transmission services via the DBNGP.

4.2 DBP refers the ERA to DBP's submissions on these issues made in DBP's submission 52, filed on or about the date of this submission.

5. PRUDENCE AND EFFICIENCY OF CERTAIN ACTUAL OPERATING EXPENDITURE IN THE 2005 TO 2010 ACCESS ARRANGEMENT PERIOD

5.1 In this section of the submission DBP responds to the ERA's deliberations on the prudency and efficiency of a number of categories of DBP's actual operating expenditure for the period 2005 to 2010.

5.2 As an preliminary submission on this issue however, DBP notes that the ERA has sought to identify a benchmark year being 2009 as the year to assess whether the expenditure is prudent and efficient and then to use that benchmark year to assess the forecast expenditure against.

5.3 In this regard, DBP refers to its previous submissions in section 5 of this submission and submits that that the ERA is wrong to be considering that the costs incurred in any particular year in the period 2005 to 2010 should be used as a benchmark of the costs that a prudent and efficient service provider.

5.4 Even if it is appropriate to identify a benchmark year, there is also no reason given as to why the ERA has chosen 2009 as the benchmark year.

5.5 Furthermore, it appears that the only basis the ERA has adopted in assessing whether the expenditure in 2009 is an appropriate benchmark, is to test it against the expenditure in 2008 and seek to understand any step changes in expenditure from 2008 to 2009. This presupposes therefore that only 2008 expenditure is prudent, unless there is an explanation given for the difference and the difference can be explained on prudency and efficiency grounds.

5.6 DBP submits that this approach is flawed. This is particularly so in the case of certain cost categories such as "consulting costs", in which case the costs for 2008 that were categorized under "consulting" did not include all consultants engaged by DBP or its asset manager, whereas the 2009 amount did. This is due to the fact that in 2008, much of the costs were incurred by an asset manager who coded costs differently to DBP and so, it has been difficult to allocate the 2008 costs into the same categories as have been used in 2009 (being when all of the costs were incurred by DBP). So, there is no like for like comparison able to be done. The same issue also applies for IT expenses.

Consulting costs

5.7 At paragraph 817 the Draft Decision, the ERA seeks to justify the costs in the category named as consulting in 2009 as the benchmark costs for consulting that a prudent and efficient service provider would incur. The ERA identifies a step increase of about $3m in costs categorized as consultancy services from 2008 to 2009 in the actual operating expenditure included in the Original AA Proposal, $2m of which it has not been able to understand what it related to. In paragraph 824 of the Draft Decision, the ERA concludes that $1m of the $3m increase from 2008 to 2009 is justified and so, the benchmark costs for consultants that a prudent and efficient service provider would incur in 2009 would be in the order of $4.9m.

5.8 Leaving the issue of benchmarking aside, DBP submits that its costs in 2009 categories as consultants costs are prudent because they were derived from a bottoms up budgeting process controlled by DBP and using a cost categorization approach consistently across all divisions, where each division identified the external consultants required to undertake the activities of the division that were outlined in the annual Business Plan. Accordingly, DBP has greater certainty that, for 2009, all of the consultancy costs have been captured in this category.

5.9 Furthermore, the following tables contain a breakdown of the consulting expenditure in each division of DBP for the 2009/10 budget.

Legal Expenses

Cost	Item
[redacted]	Additional legal support for commercial matters
	Dispute provision
	legal costs associated with bank consents (includes DBP and Financiers' lawyers fees)
	Assistance with business development (initial preparation work only)
	Assistance on agreements with shippers
	Additional legal support for operational matters
	Advise required on regulatory matter inclussive of access arrangmenet process
	legal input into application for variation of ACCC Undertakings
	legal costs associated with responding to ACCC investigations into confidentiality incidents
	legal sign off on policies and procedures review
	Litigation, appeal involvement and an interlocutory injunction
	Costs associated with extension of working capital facility (DBP and financiers legal costs)
	legal issues associated with unitholder issues
	specialist legal advice on access right valuation
	Legal advice on Same Business Test (SBT) tax issues
	Total - Legal

Audit Consulting

Cost	Item
[redacted]	Internal Audit Reviews
	Safety Case Reviews
	Statutory external audits
	ACCC/ERA Ring Fencing compliance report
	General Compliance advice -
	Total - Audit

Reg & Gov Policy Consulting

Cost	Item
[redacted]	Review of opex
	Prudency review
	WACC review
	General economic advice
	Economic assistance for Security & Reliability review by OOE
	Total - Regultory & Government

Risk Management Consulting

Cost	Item
[redacted]	Consulting fees estimate for TCOIR and risk assessments
	Intranet Training and Development
	Obligations register - Training and Dev costs
	Enterprise Document Mgt (EDM) processes consulting and advices
	Ongoing training costs for doc management system
	Crisis and Emergency Mgmt plan tests. Costs to reflect the testing of EMP as well as CMP plus additonal services - training etc
	Enterpirsie Risk Workshops - Facilitated sessions
	Business Continuity Plan review and risk review updates & IT DRP
	Total - Risk

OHSE Consulting

Cost	Item
[redacted]	Mandatory requirements
	Medical assessments
	VSSMS - Vehicle GPS tracking
	Cause testing
	Verification of Venting Calculation for NGERS
	Wellbeing Consultant
	Follow up surveys
	Total -OHSE

Engineering Management

Cost	Item
[redacted]	Rotating Equipment
	CSI Software and Hardware Maintenance agreements
	Specification Update
	Solar Turbines Reps for Borescope Inspections
	Document Control
	Scanning remainder of pre stage 3 documents
	Maintenance of documentation to Launchview
	New contract for Launchview
	Drawing modifications by Worley Parsons.
	Electrical
	Hazardous area repair at compressor stations
	Hazadous area Audit of meter stations
	Update specifications
	Business Systems
	Transcad server, purchasing of hard drives, installation and maintenance
	Pipe Line Intergrity
	Annual CP survey program including Laterals
	DCVG on DBNGP and Laterals
	CP Audit Dig up programs
	Update specifications
	Pigging program
	Earthing system. Distributed anodes to be replaced
	SCADA
	SCADA maintenance contract (Telvent)
	Metering
	Update Specifications
[redacted]	Instrumentation
	Update specifications
	Communications
	Ops and Maintenance Costs associated
	Reliability Engineering
	IRC Reliability Analysis (Phase II and III)
	Mechanical
	Maintenance of emergency equipment
	Total - Engineering Mgmt
5,871,597	**Total Overall**

5.10 As the figures are budget information they do not reconcile with actuals but may assist in providing a guide as to what expenditure is generally broken down to.

IT costs

5.11 The ERA in its Draft Decision has sought to use the costs in the category named as "IT expenses" in 2009 as the benchmark costs for IT expenditure in 2005 to 2010 that a prudent and efficient service provider would incur. The ERA identifies a step increase of about $4.5m in costs categorised as IT expenditure from 2008 to 2009 in the actual operating expenditure included in the Original AA Proposal. It then concludes, in paragraph 820, that some of the increase from 2008 is justified under the prudence and efficiency criteria, but the whole of the increase in charges for IT services provided by WestNet under the revised OSA may not be consistent with the prudence and efficiency criteria. Accordingly, it concludes that the benchmark costs for IT expenditure that a prudent and efficient service provider would incur in 2009 would be in the order of $2.696m.

5.12 The ERA has then amended the forecast of operating expenditure for 2011 to 2015 to reflect a level of IT expenses in each year equal to $2.696m ($2010 31 December), equal to the benchmark cost established by the ERA for 2009.

5.13 DBP does not agree with the ERA's required amendment. The reasons are outlined later on in this submission. Nor does DBP agree that it is appropriate to set the IT expenditure for a particular year as a benchmark that a prudent and efficient service provider would incur for IT expenditure in future years and to reduce the expenditure incurred by DBP in 2009 and recorded as IT expenditure by over $3m and set that reduced amount as the appropriate benchmark.

5.14 Even if DBP is wrong and it is appropriate to set the expenditure in a particular year as a benchmark for future years in order to determine whether the costs for those future years are prudent and efficient, DBP submits that it was wrong to reduce the 2009 IT expenditure by over $3m and set the prudent and efficient benchmark costs at $2.696m. These reasons have been outlined previously in DBP's submission 44 (which neither the ERA nor Halcrow appear to have considered in the Draft Decision.

5.15 In summary, a number of significant events have led to increased IT expenditure to explain the change in expenditure between 2008 and 2009 and to justify the 2009 actual IT expenditure as prudent and efficient.

Transition of OSA from Alinta to WestNet

5.16 When DBP's IT services under the OSA were transitioned from Alinta (in Melbourne) to WestNet in Perth in 2007 and 2008, there was a significant reduction in the size of the service provider which resulted in a reduction in economies of scale that caused an increase in:

(a) licensing costs

(b) data centre operating costs

(c) Disaster recovery site costs (we now have a fully functioning DR site, this was never established under Alinta)

5.17 WNES are entitled to cost pass through only under the OSA. When WNES built their cost pass through model, it became clear that the previous cost pass through model developed by Alinta under the OSA was poorly structured using a simple headcount methodology and that DBP had previously been under-charged. For example, one area that was poorly addressed by Alinta was the recovery of depreciation costs. WNES spent approximately $28M in transition and establishment costs for their IT operations centre and are entitled to recover a portion of those costs via the OSA.

5.18 It should also be noted that WNES provide a significantly more reliable (high availability) service than Alinta did and have achieved this through the deployment of virtualisation technology, redundancy and real time synchronisation of data at the Disaster Recovery facility. All of these are considered industry best practice and are quite superior to the availability and reliability previously provided by Alinta.

Separation of Ownership and License costs

5.19 Because of the separation of ownership holdings between DBP and its IT service provider (no longer a > 50% interest) DBP must now directly pay for all of its Software Licensing. Alinta was able to purchase its licences based on a user base of 5000+ seats. DBP have a minimum base on which to establish agreements with providers such as Microsoft. Although there has been a very small reduction in the pass through costs under the OSA our direct licensing costs have gone from [redacted]. Products such as Microsoft, Citrix, Adobe, ChemAlert and Google Earth Pro all fall in this category.

5.20 DBP has also improved its safety and work practices and this has led to increased costs for products such as Citrix (remote computing) and Google Earth Pro (VSSMS). There has also been a significant increase in the number of staff using Microsoft productivity tools such as Visio and Project and we paid approx [redacted] last year.

Business-wide Maximo deployment

5.21 In 2008, DBP completed the upgrade of its asset management software Maximo. The annual support contract for this approx [redacted] In 2009, DBP also undertook a major rollout program for using Maximo and this resulted in additional licence costs of [redacted] plus annual renewal/maintenance fees [redacted]. The business intends to further increase the Maximo user base and will probably have another [redacted] worth of Maximo licensing expense in 2011/12.

5.22 Also, DBP is indicating that it intends to continue outsourcing certain IT functions.

Further Justification of forecast IT expenditure

5.23 DBP has stated that it is inappropriate for the Regulator to establish a benchmark or baseline year that all future costs are based on. This is explained by the extensive changes described above. DBP has however suggested that its approach to setting costs have been built from the bottom up as part of its budgeting process.

5.24 DBP has forecast costs for IT expenses that are constant in real terms over the 2011 to 2015 access arrangement period at an amount of [redacted] ($2010 31 December).

5.25 DBP submits that this amount is made up of 3 specific elements consisting of the following:

(a) [redacted] Operational Usage Fee

(b) [redacted] Capital usage fee or “Shared Use Fee”

(c) Other direct DBP IT costs

5.26 DBP provides the following cost breakdown for each of the 3 cost elements:

[redacted] *Operational Usage Fee*

5.27 DBP provides attachment 1 (DBP IT Budget 2009-2010 A.xls) as further justification and detailed breakdown of costs borne under the [redacted] Operational Usage Fee.

5.28 Attachment 1 demonstrates a total costs attributable and its breakdown of the [redacted] Operational Usage Fee of [redacted] for the 2009/10 Financial year.

[redacted] *Capital usage Fee*

5.29 DBP provides attachment 2 (Discussion paper) as further justification and detailed breakdown of costs borne under the [redacted] Capital Usage Fee or "shared Use Fee".

5.30 Attachment 2 demonstrates a total costs attributable to the [redacted] Capital Fee (or Shared Use Fee) of [redacted] for the 2009/10 Financial year (see table 5).

5.31 Attachment 3 (DBP Shared IT Service Usage) also breaks down the costs that make up the [redacted] for the 2009/10 [redacted] Capital Usage Fee (or Shared Use Fee).

5.32 Additionally, DBP provides a [redacted] presentation further explaining the basis of the [redacted] Capital usage fee or 'Shared Use Fee' as attachment 4.

Other DBP IT Costs

5.33 Beyond the [redacted] Operational Usage Fee and the [redacted] Capital Usage Fee (or Shared Use Fee) DBP directly incurs the following IT costs for IT applications that it is directly responsible for:

(a) Microsoft Enterprise agreement	[redacted]
(b) MS EA true-up (Project, Visio, Windows Server)	
(c) Maximo Annual Licence	
(d) Annual support ChemAlert/Jasper/Citrix/Maximo	
(e) CRS support costs (Sydac)	
Total	***$871,648***

Further Justification Summary

5.34 DBP submits that the forecast annual IT expenditure for the period 2011 to 2015 is made up of 3 specific elements consisting of the following:

(a) [redacted] Operational Usage Fee of [redacted] for the 2009/10 financial year.

(b) [redacted] Capital usage fee or "Shared Use Fee" of [redacted] for the 2009/10

(c) Other DBP IT costs budget of [redacted]

5.35 The above points justify DBP's requirement for at least [redacted] ($2010 31 December) for IT expenses that are constant in real terms over the 2011 to 2015 access arrangement period.

6. INDEPENDENT AUDIT OF ACTUAL OPERATING EXPENDITURE

6.1 Paragraphs 779 of the Draft Decision introduces the requirements for DBP to provide independent audit reports operating expenditure before being included as an increment to total revenue under the incentive mechanism.

6.2 Regarding the requirement to provide independent audit reports, as the ERA is aware, this requirement comes as somewhat of a surprise to DBP given that, in the months leading up to the filing of DBP's Original AA Proposal in April 2010, the ERA dispensed with this requirement. This was previously outlined by DBP in correspondence with the ERA in early 2010.

6.3 Accordingly, DBP has only had since 14 March to:

(a) understand what the ERA meant by the requirement to provide independent audit reports; and

(b) have an independent auditor undertake the audits and have the audit reports finalised and issued for review by the ERA.

6.4 The ERA has indicated that an audit which follows the procedure outlined in section 5 of Submission 52 is likely to address the ERA's requirement that the expenditure be independently audited.

6.5 An audit has been undertaken by [redacted], an independent auditor.

6.6 As part of this audit process, DBP identified some errors in the amount of capital expenditure for the period 2005 to 2010 that was reported in the Amended AA Proposal. On or about the date of this submission, a corrected version of the Amended AA Proposal is being submitted that contains corrected historical operating expenditure figures.

6.7 The audit undertaken by [redacted] reconciles the operating expenditure included in DBP's annual and half yearly financial statements from 2005 to 31 December 2010 with the historical operating expenditure recorded in the corrected Amended AA Proposal for that same period, and the report is contained in attachment 5.

6.8 The reconciliation process was undertaken by the auditor in a number of steps. The following tables outline each step and following each table is a written explanation of each step.

Table 1:

Annual Statement of Financial Performance (as per 30 June XX Statutory Report)

	6 Months to 30-Jun-05 '000	12 Months to 30-Jun-06 '000	12 Months to 30-Jun-07 '000	12 Months to 30-Jun-08 '000	12 Months to 30-Jun-09 '000	12 Months to 30-Jun-10 '000
Revenue From Continuing Operations	136,067	221,195	249,834	302,745	352,287	394,684
Other Income		1,958	842	3,008	414	94
Employee Benefits Expense	-429	-89	-602	-975	-7,129	-25,395
Depreciation & Amortisation Expense	-10,843	-33,191	-40,134	-48,080	-58,132	-65,836
Operations & Maintenance Expense	-2,667	-10,764	-10,685	-10,257	-19,417	-33,900
Management Services Fee	-13,865	-29,037	-30,234	-33,798	-33,733	-135
Fuel Gas Expense	-12,947	-23,133	-25,185	-23,527	-16,068	-15,289
Other Expenses	-98	226	-139	-1,301	-274	-1,202
Impairment Assets Held for Sale		-3,468				
Reduction in Goodwill				-11,921	-23,331	
Finance Costs	-58,002	-118,640	-117,644	-128,073	-162,206	-210,576
Income Tax Expense	-6,908	-9,299	-35,302	-6,006	-195	2,869
	30,308	**-4,242**	**-9,249**	**41,815**	**32,216**	**45,314**

6.9 The first step was to obtain the operating costs contained in the annual and half yearly statements of financial performance for the DBNGP Trust for the period from 1 January 2005 to 30 June 2010, each of which had been audited by [redacted]. The above table summarises these amounts from the relevant audited statements.

6.10 The independent auditor in paragraph (xiii) of its Report of Factual Finding (Attachment 5) agreed this reconciliation (Table 1).

Table 2:

Half Year Statement of Financial Performance (as per 31 December XX DUET Repporting Pack)

	6 Months to 31-Dec-05	6 Months to 31-Dec-06	6 Months to 31-Dec-07	6 Months to 31-Dec-08	6 Months to 31-Dec-09	6 Months to 31-Dec-10
Revenue From Continuing Operations	110,238,333	112,071,966	146,446,067	168,344,506	194,997,945	214,894,180
Other Income				407,616	67,364	10,274,459
Employee Benefits Expense					-11,862,036	-14,482,991
Depreciation & Amortisation Expense	-16,313,658	-19,753,854	-21,735,077	-29,033,386	-31,889,060	-38,013,078
Operations & Maintenance Expense						
Management Services Fee	-20,536,181	-19,539,611	-22,277,638	-28,407,642	-23,872,748	-15,778,493
Fuel Gas Expense	-11,174,873	-9,477,082	-14,885,017	-6,505,368	-9,061,897	-6,324,857
Other Expenses	163,583	-402,763	1,894,584	-5,781		
Impairment Assets Held for Sale						
Reduction in Goodwill			-5,929,671	-9,104,762		
Finance Costs	-54,450,871	-56,096,166	-63,058,308	-81,300,005	-96,290,133	-112,998,363
Income Tax Expense	-10,999,360	-1,610,847	-1,492,134	396,685	651,800	-3,927,002
	-3,073,027	**5,191,643**	**18,962,806**	**14,791,863**	**22,741,235**	**33,643,855**

6.11 The second step was to obtain the operating costs contained in the half yearly statements of financial performance for the DBNGP Trust for the period from 1 July 2005 to 31 December 2010, each of which had been prepared for the purposes of DBP's main shareholders update to the Australian Stock Exchange and which had been reviewed by [redacted]. The above table summarises these amounts from the relevant statements.

6.12 The independent auditor in its Report of Factual Finding (Attachment 5) in paragraph (xv) agreed that these amounts in Table 2 reconciled with the amounts contained in the reviewed consolidated financial reporting pack of the Trust prepared for DUET.

Table 3:

Six Monthly Statement of Financial Performance

	6 Months to 30-Jun-05 '000	6 Months to 31-Dec-05 '000	6 Months to 30-Jun-06 '000	6 Months to 31-Dec-06 '000	6 Months to 30-Jun-07 '000	6 Months to 31-Dec-07 '000	6 Months to 30-Jun-08 '000	6 Months to 31-Dec-08 '000	6 Months to 30-Jun-09 '000	6 Months to 31-Dec-09 '000	6 Months to 30-Jun-10 '000	6 Months to 31-Dec-10 '000
Revenue From Continuing Operations	136,067	110,238	110,957	112,072	137,762	146,446	156,299	168,345	183,942	194,998	199,686	214,894
Other Income	0	0	1,958	0	842	0	3,008	408	6	67	27	10,274
Depreciation & Amortisation Expense	-10,843	-16,314	-16,877	-19,754	-20,380	-21,735	-26,345	-29,033	-29,099	-31,889	-33,947	-38,013
Operating Expense*	-17,059	-20,373	-19,291	-19,942	-21,718	-20,383	-25,948	-28,413	-32,140	-35,735	-24,897	-30,261
Fuel Gas Expense	-12,947	-11,175	-11,958	-9,477	-15,708	-14,885	-8,642	-6,505	-9,563	-9,062	-6,227	-6,325
Impairment Assets Held for Sale		0	-3,468	0	0	0	0	0	0	0	0	0
Reduction in Goodwill		0	0	0	0	-5,930	-5,991	-9,105	-14,226	0	0	0
Finance Costs	-58,002	-54,451	-64,189	-56,096	-61,548	-63,058	-65,015	-81,300	-80,906	-96,290	-114,286	-112,998
Income Tax Expense	-6,908	-10,999	1,700	-1,611	-33,691	-1,492	-4,514	397	-592	652	2,217	-3,927
	30,308	**-3,073**	**-1,169**	**5,192**	**-14,441**	**18,963**	**22,852**	**14,792**	**17,424**	**22,741**	**22,573**	**33,644**

* Includes - Employee Benefits Expense, Operations & Maintenance Expense, Management Services Fee and Other Expenses

6.13 The third step involved converting the expenditure information contained in the 2 sets of statements referred to in steps 1 and 2 into 6 monthly reports. Table 3 demonstrates the 6 monthly periods used to report on a calendar year. The auditor has confirmed that that these figures reconcile with the figures in the relevant financial statements.

Table 4:

Statement of Financial Performance - By Calendar Year

	12 Months to 31-Dec-05 '000	12 Months to 31-Dec-06 '000	12 Months to 31-Dec-07 '000	12 Months to 31-Dec-08 '000	12 Months to 31-Dec-09 '000	12 Months to 31-Dec-10 '000
Revenue From Continuing Operations	246,305	223,029	284,208	324,643	378,940	414,580
Other Income	0	1,958	842	3,416	74	10,301
Depreciation & Amortisation Expense	-27,157	-36,631	-42,115	-55,378	-60,988	-71,960
Operating Expense*	-37,432	-39,234	-42,101	-54,361	-67,874	-55,159
Fuel Gas Expense	-24,122	-21,435	-30,593	-15,147	-18,625	-12,552
Impairment Assets Held for Sale	0	-3,468	0	0	0	0
Reduction in Goodwill	0	0	-5,930	-15,096	-14,226	0
Finance Costs	-112,453	-120,285	-124,606	-146,315	-177,196	-227,284
Income Tax Expense	-17,907	90	-35,183	-4,117	60	-1,710
	27,235	**4,023**	**4,522**	**37,644**	**40,165**	**56,217**

* Includes - Employee Benefits Expense, Operations & Maintenance Expense, Management Services Fee and Other Expenses

6.14 Step 4 involved the conversion of the 6 monthly figures in table 3 into figures for calendar years 2005 to 2010. Table 4 presents the figures contained in the statements of financial performance on a calendar year basis.

6.15 This was accepted by the auditor.

Table 5:

Reconciliation of Adjusted Operating Expenditure

	12 Months to 31-Dec-05 'm	12 Months to 31-Dec-06 'm	12 Months to 31-Dec-07 'm	12 Months to 31-Dec-08 'm	12 Months to 31-Dec-09 'm	12 Months to 31-Dec-10 'm
Operating Expense*	-37.43	-39.23	-42.10	-54.36	-67.87	-55.16
Adjustments						
- Overhauls recognised in Opex		-0.29	-0.59	-2.36	-12.19	
	-37.43	**-39.53**	**-42.69**	**-56.72**	**-80.06**	**-55.16**
Fuel Gas	**-24.12**	**-21.44**	**-30.59**	**-15.15**	**-18.62**	**-12.55**
	-61.55	**-60.96**	**-73.28**	**-71.87**	**-98.69**	**-67.71**

6.16 The next step outlined the items that were included in DBP's corrected Amended AA Proposal as operating expenditure items but which were not included in the audited financial statements as operating expenditure, but rather were included in these statements as capital expenditure.

6.17 Table 5 demonstrates the reconciliation items used for regulatory purposes. There was effectively 1 item – expenditure for compressor and GEA overhauls which are treated as capital items in the financial statements but expensed for regulatory purposes in the corrected Amended AA Proposal.

6.18 DBP notes that the independent auditor in its Report of Factual Finding (Attachment 5) in paragraph (xvi) agreed amounts included for "Adjustments – Overhauls recognised in OPEX" to the corresponding amount on the reconciliation of actual capital expenditure.

7. PRUDENCE AND EFFICIENCY OF PROPOSED OPERATING EXPENDITURE IN THE 2011 TO 2015 ACCESS ARRANGMENT PERIOD

7.1 Paragraphs 823 to 917 of the Draft Decision contains the ERA's deliberations on its review of DBP's proposed forecast operating expenditure contained in the Original AA Proposal for the 2011 to 2015 access arrangement period.

7.2 The ERA has disallowed or partially disallowed costs in the following categories of forecast operating expenditure:

(a) Consultancy expenditure
(b) IT expenditure
(c) Entertainment
(d) Repairs and maintenance
(e) CPRS
(f) Self insurance
(g) Compressor overhauls
(h) Regulatory expenses; and
(i) Fuel gas

7.3 The graph below graphically summarises:

(a) the difference between the Original AA Proposal's total forecast operating expenditure and the total forecast operating expenditure allowed by the ERA in the Draft Decision

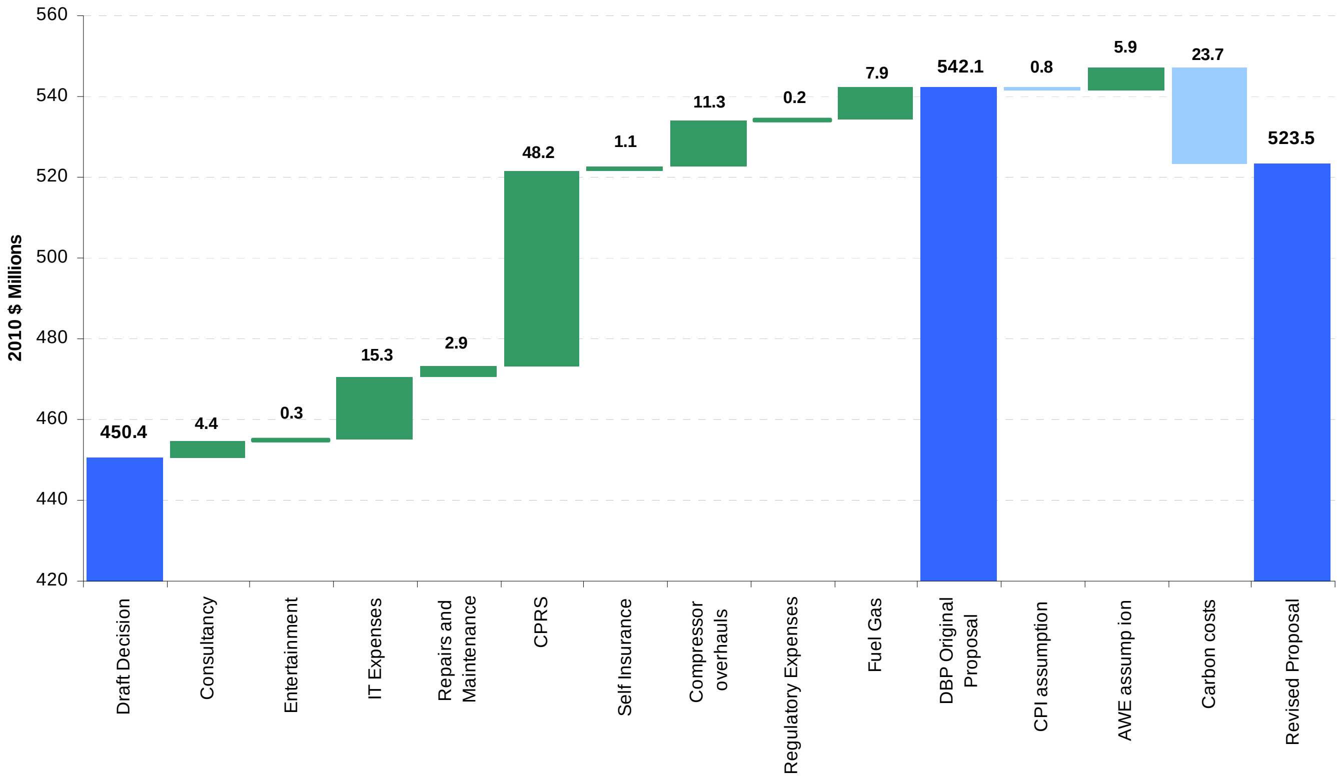
(b) the amounts of each category of operating expenditure that the ERA has disallowed; and

(c) the difference between the Original AA Proposal's total forecast operating expenditure and the total forecast operating expenditure DBP proposed in the corrected Amended AA Proposal (entitled Revised AA Proposal in the graph below).

7.4 DBP responds to the ERA's reasoning for disallowing each category of expenditure in turn.

7.5 DBP also filed a corrected Amended AA Proposal which contains figures for forecast operating expenditure which differ in value to the figures for forecast operating expenditure included in the Original AA Proposal and the Draft Decision. These differences are explained below.

7.6 Table 1: Differences in operating expenditure.



7.7 DBP addresses each item as they are raised in the ERA's Draft Decision

Consultancy Costs

7.8 DBP refers to submissions made in section 5 of this submission referring to consulting costs.

7.9 As a result, DBP has not made, in its corrected Amended AA Proposal, any change to the costs for consultants in the forecast operating expenditure total. It is the same as was included in the Original AA Proposal.

Exclusion of Entertainment Expenses

7.10 DBP submitted that entertainment expenses were [redacted] ($2009 real) in CY 2010.

7.11 The ERA's consultants point out that this is 0.2 percent of recurrent operating expenditure and conclude this is an immaterial amount of the annual operating budget and requires no further review. No conclusion is made that the expenses should be excluded from DBP's operating expenditure.

7.12 The ERA's Draft Decision draws a different conclusion suggesting that DBP's forecast for entertainment expenses increases by 46 per cent over actual costs in 2009.

7.13 DBP submits that its forecast is constant in real terms over actuals from CY 2010 and is a reasonable forecast considering expenses are inclusive of:

(a) Fringe Benefits Tax (FBT) - approximately [redacted] (FBT relates to expenditure relevant to mobiles, car parks, meals, motor vehicle use and home internet connections);

(b) Offsite planning days for each business unit and leadership teams and team building - approximately [redacted] and

(c) Christmas party, family day and other minor events – approximately [redacted]

7.14 The reasons for increase over actuals provided for CY 2009 are that for one third of the year, DBP's total number of staff was 10 and the asset manager recorded these costs in other cost items, but it is unclear just where.

IT Expenses

7.15 As stated earlier in this submission and in earlier submissions, Halcrow has incorrectly misinterpreted DBP's submissions. A number of significant events have led to increased IT opex.

Transition of OSA from Alinta to WestNet

7.16 When DBP's IT services under the OSA were transitioned from Alinta (in Melbourne) to WestNet in Perth there was a significant reduction in the size of the service provider which resulted in a reduction in economies of scale that caused an increases in:

(a) licensing costs

(b) data centre operating costs

(c) disaster recovery site costs (we now have a fully functioning DR site, this was never established under Alinta)

7.17 WNES are entitled to cost pass through only under the OSA. When WNES built their charge-back model it became clear that Alinta's charge-back model was quite inadequate and that DBP had previously been under-charged. For example, one are that was poorly addressed by Alinta was the recovery of depreciation costs. WNES spent approximately $[redacted] in transition and establishment costs for their operations centre on L5 and are entitled to recover a portion of those costs via the OSA.

7.18 It should also be noted that WNES provide a significantly more reliable service than Alinta did and have achieved this through the deployment of virtualisation technology, multiple redundant systems and real time synchronisation of data at the DR facility. All of these are consider industry best practice and are quite superior to the availability and reliability provided by Alinta.

Separation of Ownership and License costs

7.19 Because of the separation of ownership holdings between DBP and its IT service provider (no longer a 51% interest) DBP must now directly pay for all of its Software Licensing. Alinta was able to purchase its licences based on a user base of 5000+ seats. DBP have a minimum base on which to establish agreements with providers such as Microsoft. Although there has been a very small reduction in the pass through costs under the OSA our direct licensing costs have gone from [redacted]. Products such as Microsoft, Citrix, Adobe, ChemAlert and Google Earth Pro all fall in this category.

7.20 DBP has also improved its safety and work practices and this has led to increased costs for products such as Citrix (remote computing) and Google Earth Pro (VSSMS). There has also been a significant increase in the number of staff using Microsoft productivity tools such as Visio and Project and we paid approx [redacted] last year.

Business-wide Maximo deployment

7.21 In 2008, DBP completed the upgrade of its asset management software Maximo. The annual support contract for this approx [redacted]. In the last year we also undertook a major rollout program for using Maximo and this resulted in additional licence costs of [redacted] plus annual renewal/maintenance fees. The business intends to further increase the Maximo user base and will probably have another [redacted] worth of licensing expense in 2011/12.

7.22 Also, DBP is indicating that it intends to continue outsourcing IT service provision.

Repairs and Maintenance Costs

7.23 In Paragraph 861 of the Draft Decision the ERA states that DBP's actual costs for 2009 and forecast for 2010 to 2015 indicate a decline in costs from $7.156 m in 2009 to $5.615m in 2010 and then an increase in costs to $6.811 m in each of the years 2011 to 2015 ($2010). However, it goes on to conclude that the actual costs for 2009 include an adjustment to the value of inventories, indicating that the benchmark cost in 2009 would be better stated as $6.234 and the forecast costs for the 2011 to 2015 access arrangement period are 9.4 per cent greater than this benchmark.

7.24 In addition to the issue of the relevance of the historical costs being a benchmark for future operating expenditure (as discussed earlier in this submission), DBP submits that the baseline costs in 2009 do not reflect the baseline costs associated with the repairs and maintenance of the DBNGP moving forward into 2010 through to 2015.

7.25 This is due to a number of reasons. Firstly, the extensive expansion works conducted on the DBNGP and associated laterals during the construction of Stage 4, 5A, and 5B leading to increased maintenance costs.

7.26 DBP notes that a major component of the expansion was the installation of rotating equipment and valves. These are high maintenance items and have subsequent costs associated with them.

7.27 The second reason for the increase in costs since 2009 is that the asset management system has grown from 20,000 assets listed in 2008 to 33,000 assets and 38,000 locations. This means that with the expansion program the DBNGP maintainable assets has increased by approximately 65%.

7.28 Each expansion phase has occurred in series and Stage 5B is still being completed therefore to true baseline actual cost of maintaining the DBNGP and associated laterals will not be known until the 2011/2012 actual financial year has ended.

7.29 Given the significant number of assets entered into the asset management system (Maximo), there will be a significant number of work orders generated for general ongoing maintenance and necessarily, repairs.

Exclusion of CPRS costs

7.30 The ERA in paragraph 878 to 884 concludes that the prospect of a scheme to address carbon emissions is too uncertain for an estimate of costs to be included in the forecast of operating expenditure and therefore it has required the removal of DBP's forecast costs associated with the CPRS.

7.31 The ERA does however, allow the access arrangement to include provision for costs to be addressed by a reference tariff variation mechanism, although as will be outlined in another submission, the proposed mechanism that the ERA has allowed does not give DBP certainty that all of these costs will be able to be passed on to shippers.

7.32 At or around the time of the ERA's decision, the current Government has reaffirmed its stated policy is to introduce a price on carbon from July 2012.

7.33 Details of the carbon tax were announced on 24 February 2011 by the Federal Government. The two-stage plan for a carbon price mechanism will start with a fixed price period for 3 to 5 years before transitioning to an emissions trading scheme. The proposed start date of the carbon tax is 1 July 2010 subject to the legislation passing through both houses of parliament during the course of 2011.

7.34 The information that has been publicly released to date about the framework suggests that it will be very similar in substance to the CPRS Bill that was previously tabled in parliament.

7.35 The Government is expected to announce the initial fixed price for year one of the scheme but it is believed that it will be in the order of $20 to $30.

7.36 Given the current position of the Government, DBP has included in the corrected Amended AA Proposal, an amount for the carbon tax regime. In so doing, DBP has adopted conservative assumptions as to the price of the carbon tax and how long it will remain a fixed price tax - the tax will be set at $20 per tone and that the price will be fixed for the remainder of the access arrangement period.

7.37 DBP submits that it is therefore appropriate to include the costs of the imminent carbon tax in its forecast operating expenditure. DBP has provided its amended proposal on this basis.

Self Insurance

7.38 DBP refers to responses already provided to the ERA in regards to self Insurance costs. DBP's submissions relevant to self insurance are made in Submission 12 paragraph 6.32 to 6.34.

7.39 DBP does not agree with the decision made in the Draft Decision and has not made the corresponding amendment in its corrected Amended AA Proposal.

Compressor overhaul costs

7.40 Paragraphs 879 to 901 of the Draft Decision seek to reduce DBP's forecast operating expenditure for compressor overhaul costs. The ERA does this on the advice of its consultants that suggest forecasts costs should be based on observable costs incurred in 2009.

7.41 The ERA's consultant is incorrect to assume that by taking into account observed actual cost for one single year and for one single compressor overhaul, it has created an appropriate benchmark to apply to the quantum of the forecast operating expenditure.

7.42 The ERA must also understand that the DBNGP currently has 3 different makes of turbines that, over time, require overhaul and the one selected by its consultant is the least expensive of the 3 to overhaul. In DBP's experience the Nuovo Pignone is the more expensive to overhaul.

7.43 DBP also notes that acquisition of equipment is not the extent to the total cost. Additional work that is carried out to prepare for the major component overhaul is also added to this cost. A reasonable estimate for the total cost has in DBP experience been $2.86 m.

7.44 The costs of overhauls are based on the following:

(a) Overhauls are carried out every 30,000 hrs for Solar Taurus and Mars and 35,000 hrs for [redacted] machines. The Overhaul costs with Solar are based on the following:

(i) Number of operating run hours [normally 30,000 hrs]

(ii) Customer discount offered by Solar [3.61%]

(b) The fired hours are applied to the Gas Producer fired hours rate, the Power Turbine fired hours rate and the Accessory Gear Box fired hour's rate.

(c) These rates when applied resulted in the cost of an overhauled machine of [redacted]this will vary dependent on the US exchange rate – but this value is calculated at an exchange rate of parity].

(d) Compressor Seals are also replaced during overhauls as seals have a 4 year life before replacement. Seal materials costs [redacted]

(e) In addition to the cost of overhaul, the following costs are also applied as part of the exchanges of gas turbine:

Transport cost from US to WA and return [redacted] (turbine & seals)
Hire of crane
Exchange of lubricating oil at engine exchang
Replenishment of filters
Site works (turbine & seals)
Consumables
DBP labour for installation of equipment

7.45 Total budget for a typical Solar Mars Exchange and all associated auxiliaries included above [redacted]

7.46 For [redacted] Machine – the overhaul costs associated with CS6 and CS9 that took place in 2009/10 was $[redacted]

7.47 Accordingly, DBP has not changed its position from that contained in the Original AA Proposal

Regulatory expenses

7.48 In paragraph 908 of the Draft Decision the ERA seeks to reduce DBP's proposed forecast operating expenditure for regulatory matters from $1.21m to 0.913m ($2010).

7.49 The ERA's approach in determining this is to use expected costs in for the current revisions of the access arrangement as a benchmark.

7.50 This approach fails to take into account the circumstances surrounding the access arrangement revisions for the 2016 to 2020 period. Given the fact that DBP's actual revenue will be impacted by that process, DBP needs to make sure that all possible information is submitted to the ERA in a way that convinces the regulator that the access arrangement should be approved. In addition, there is likely to be a significant increase in interest from stakeholders in that process, thereby requiring DBP to spend more time reviewing and responding to submissions.

7.51 This approach also fails to recognise that DBP has already incurred more for this current access arrangement approvals process than it had foreshadowed in the Original AA Proposal.

7.52 Given this, DBP's forecast is reasonable as its will be required to direct more resources to the revisions of this access arrangement relative to the current revision process as it can reasonable be expected to have larger risks and commercial consequence for its business.

7.53 DBP maintains that its forecast is arrived on a reasonable basis.

Fuel gas

7.54 In paragraphs 909 to 916 the Draft Decision seeks to reduce forecast operating expenditure for fuel gas by $0.87 m per year ($2010) relying on the advice of its consultants.

7.55 The ERA has concluded that DBP's 10 per cent allowance for transient gases to not be prudent or efficient.

7.56 DBP has not amended its access arrangement proposal the reasons for the reasons explained in the following paragraphs.

Transient Fuel Curve

7.57 DBP utilizes a Steady State Fuel Curve captures the changes in compressor configurations driven by compressor availabilities and probability of occurrences. However, the actual compressor fuel usage under dynamic pipeline operating conditions can reasonably be expected to be higher than the calculated Steady State fuel.

7.58 [redacted]

- [redacted]
- [redacted]
- [redacted]

[redacted] [redacted]

[redacted] [redacted]

[redacted] [redacted]

[redacted]

7.60 [redacted]

[redacted]

[redacted]

7.62 [redacted]

[redacted]

[redacted], [redacted]

[redacted]						
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

[redacted]

[redacted]

7.66 [redacted]

[redacted]

[redacted]

7.68 [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

Summary

7.72 The process adopted in the determination of Stage 5B Fuel Usage and for the period 2011 – 2015 is consistent with all previous stages and in accordance with the normal processes.

7.73 So a 10% Transient Fuel Allowance is required for:

(a) Greater transient expected over the next period

(b) Lower utilisation will result in compressor operating as partly loaded level

(c) The Transient Fuel Allowance is also used to account for the lower gas HHV that will be expected over the next few years

Other - Utilities, Rates & Taxes

7.74 In paragraph 873 to 877 of the Draft Decision, the ERA comments on DBP's utilities rates and taxes in particular fees paid under the DBNGP Access Right.

7.75 DBP previously advised that it was currently negotiating with the Office of Energy on fees under the DBNGP Access Right however, it had submitted costs based on invoices received from the Lands Access Minister.

7.76 DBP wrote to the Office of Energy regarding the fees under the DBNGP Access Right requesting that the Government promptly make a decision as to the amount of the charges payable under the Access Request granted to DBP in connection with the access area it is entitled to use within the DBNGP Corridor.

7.77 DBP received a response from the Office of Energy on 28 April advising that the matter is currently with the Minister whose decision will not be available in time for DBP to meet the ERA's timing required for decision.

7.78 Given this, DBP has no more information before it which could reasonably require it to change its position from that in the Original AA Proposal in this regard.

8. VARIANCES IN PROPOSED OPERATING EXPENDITURE BETWEEN DBP'S ORIGINAL AA PROPOSAL AND REVISED AA PROPOSAL

8.1 There are a number of variances between DBP's forecast operating expenditure in the corrected Amended AA Proposal and the Original AA Proposal.

8.2 Variance items represented in the graph at the beginning of section include:

(a) CPI Assumptions

(b) Salary and Wages Assumptions

(c) Carbon costs

(d) CPI Assumptions

8.3 This variance from DBP's Original Proposal to its Revised Proposal is a mechanical adjustment for the CPI applied.

8.4 DBP refers to its submission 49 concerning the CPI factor applied to operating expenditure.

Salary and Wages Increase Assumptions

8.5 This variance from DBP's Original AA Proposal to its Revised AA Proposal is an upward adjustment for labour market pressures.

8.6 The ERA, in its Draft Decision (paragraph 831), stated it was satisfied that the DBP's forecast is consistent with the prudence and efficiently criteria of rule 91 on the basis that forecast rate of growth in total wages and salaries costs were less than recent rates of growth in WA average weekly earnings.

8.7 Since DBP's Original AA Proposal labour market pressures have had a direct result on retention rates across its business.

8.8 [redacted]

[redacted] [redacted]

[redacted] [redacted]

[redacted] [redacted]

8.10 DBP has therefore included a revised assumption for labour escalation in its Revised AA Proposal. DBP has used a labour information factor of 7% (4.43 above expected inflation of 2.57%).

8.11 Average Weekly Earnings (AWE) for WA is currently at 5.4% to December 2010.

8.12 DBP notes that its assumptions for labor inflation remain consistent with the ERA's rationale for considering DBP Original AA proposal prudent and efficient governed by rule 91.

Carbon Costs

8.13 This variance from DBP's Original Proposal to its Revised Proposal is an adjustment for the change in commencement date for the current stated intention of the Federal Government to have a price on carbon start at 1 July 2012.

8.14 DBP refers to submissions made in Section 7 of this submission to justify this change.

9. CONFIDENTIALITY

[redacted]

Attachments

Attachment 1 – DBP IT Budget 2009-2010 spreadsheet
Attachment 2 - Discussion paper
Attachment 3 - DBP Shared IT Service Usage Fee spreadsheet
Attachment 4 - DBP Shared IT Service Usage Fee presentation
Attachment 5 – [redacted] Independent Audit report on operating expenditure reconciliation