



GOLDFIELDS  
G A S  
TRANSMISSION

# GOLDFIELDS GAS TRANSMISSION PTY LTD

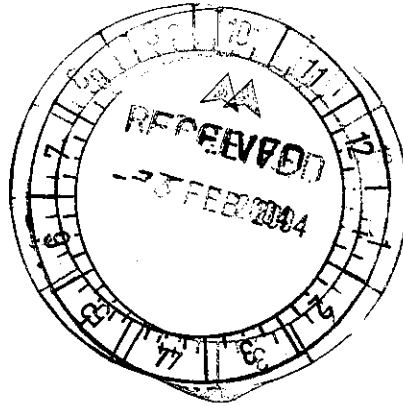
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Ref: DAK.ST.NL-0022

30 January 2004



Dr Ken Michael AM  
Alternate Chairman  
Economic Regulatory Authority  
Gas Division  
Level 6, 197 St. George's Terrace  
PERTH WA 6000

Dear Dr Michael

## **Review of Rate of Return Methodologies and Practices**

Goldfields Gas Transmission (GGT) understands that you are seeking public comment upon the report "Review of Rate of Return Methodologies and Practices" (the Report) dated September 2003 and released by your office on the 31 December 2003. GGT wishes to make the following comments, which it presumes will be made publicly available along with all other comment received on the Report by your office.

GGT understands that the closure date for public comment on the Report is 30 January 2004. Given the importance of the subject matter of the Report and the fact that it was issued during the traditional holiday period, this seems an unduly restrictive public comment period. Accordingly, GGT will confine its comments on the Report to matters of general principle. A more detailed review would require a considerable extension of time and, for reasons outlined below, an unwarranted and inefficient allocation of resources.

In general terms, GGT notes that the Report:

- has itself been "in production" for in excess of 12 months (based upon verbal communications with your office) and hence affording interested parties a highly restrictive period for public comment does not seem commensurate with the weight and impact due the subject matter,

- was compiled by the joint effort of a working group comprising of staff from your own office, the Office of the Rail Access Regulator, Curtin University of Technology and Economics Consulting Services, and hence the Report cannot be considered to represent an independent assessment, rendering it of dubious value,
- purports to "*consider evolving best practice in the determination of allowed rates of return in utility regulation*" with a "*special focus...on the treatment of diversifiable and non-diversifiable risk*". However the Report in fact merely seeks to provide a justification for existing practice and ignores or otherwise dismisses out of hand the existing problems with regulatory rate of return methodologies and the detrimental real world impacts identified in a growing body of publicly available commentary and evidence,
- is untimely in its release, which follows the release of the Draft Report of the Productivity Commission in its Review of the Gas Access Regime, which indicates that regulatory best practice is in fact currently evolving. According to the Productivity Commission, evolving best practice requires a recognition of the shortfalls of the theoretical CAPM rate of return methodology and the need to provide for specific recognition of so-called diversifiable (or non-systematic) investment specific risks,
- merely restates old arguments and represents a static and seemingly outdated view of regulatory rate of return practice and hence appears to be of little or no value other than by way of reinforcing the need for regulatory change. The Productivity Commission commented upon such studies in its Draft Report (Draft Finding 7.1) thus;


*"Since the Productivity Commission's review of the national access regime, there has been further research on the scope to use benchmarking techniques to regulate infrastructure industries. This research has not provided a convincing case that benchmarking techniques can remove the problems with the building block approach currently used for the Gas Access Regime. At this stage, the Commission sees little merit in more research on benchmarking, but seeks further comment from participants [regarding what specific non-financial information regulators should require – refer Information requests, page L]."*

Further, GGT would note that as the operator of the only pipeline with a regulatory decision concerning its access arrangement pending, the Report is arguably almost exclusively relevant only to the current regulatory process affecting GGT. In such circumstances, it needs to be noted that treatment of investment specific risk (ie. so called "diversifiable risks") in the Report is completely inadequate. GGT would reiterate that it is only concerned with the Goldfields Gas Pipeline and holds no other vertically or horizontally integrated assets by which it might be construed to have the ability to diversify its exposure to risks associated with the pipeline. Whether or not the owners of GGT hold other assets does not affect the risk exposure of GGT. And even if GGT's owners hold other pipeline investments, assuming these are significant enough to be subject to regulation, then no compensation for risk diversification will exist, as all pipeline assets will face a similarly limiting regulatory rate of return methodology.

It must be concluded that the treatment of risk diversification and the omission of asset specific risk advocated in the Report is flawed in concept and in particular in application to GGT.

In consequence of the preceding comments, GGT is of the view that the Report adds no value to its own regulatory access arrangement approval process and accordingly, wishes to advise of its objection to incurring any pass through of costs associated with the Report, from your office.

Yours sincerely



**David A King**  
**General Manager**