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Electorate includes Goldfields, Murchison, Gascoyne, Pilbara, Kimberley and Central Desert Areas

SUBMISSION TO THE GAS ACCESS REGULATOR ON THE ACCESS ARRANGEMENT PROPOSAL FOR THE GOLDFIELDS GAS PIPELINE

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Independent Member for Mining and Pastoral Region

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A number of issues should receive close scrutiny in the proposed Access Undertaking.

1. *Capital Base*

The “actual cost” of the Goldfields Gas Pipeline was $456 million, well below the purchase price of $624 million. Although the purchase price is not used to calculate the Initial Capital Base, it should not include any other assets such as the WMC power stations.

The Depreciated Actual Cost (DAC) should be depreciated over 3.5 years since the pipeline was completed. If the whole asset is depreciated over 65 years, the amount of depreciation over 3.5 years would be about $24.5m. Therefore the DAC would be about $431.5m.

The Gas Access Regulator should look at the relevance under the Gas Code of the use of infrastructure bonds for financing and see whether the DAC was actually below $431.5m, as a $50 million “profit” on the infrastructure bonds was booked by the initial Joint Ventures.

The Capital Base uses a value based upon the actual capital cost ($456 million) which has been adjusted upwards and then depreciated. In the calculation of the Optimised Pipeline Replacement Cost, the starting point is the construction cost of $456m. To this is added the upward adjustment of $50.7m comprised of three factors “claimed” to have increased the optimised replacement cost of the pipeline. They are the US dollar - Australian dollar exchange rate, interest rates and escalation in the CPI. The resulting ORC is $506.7m. These three factors deserve close scrutiny and should be rejected. The DORC is a replacement cost valuation and it seems totally inconsistent to add these three amounts to the construction cost. This whole calculation also ignores is that the <u>real</u> cost of pipeline construction has been dropping at 8% a year in recent years. It would be surprising if the GGT assets could not be replaced on an optimised basis at less than the actual construction cost of the Goldfields Gas Pipeline.

The Initial Capital Base could lie between the "DAC" ($431.5m) or a lower figure if the use of infrastructure bonds had been taken into account and a Depreciated Optimised Replacement Cost (DORC) of less that $456m.

2. Weighted Average Cost of Capital (WACC)

The Goldfields Gas Pipeline probably has a risk associated with it in terms of the continuity of customers because of the volatility of the mining industry and the potential for competition from a pipeline from Geraldton to the North Eastern Goldfields equal to or marginally higher than the Parmelia Pipeline. But this region has proved remarkably resilient over the last 35 years and contains major mines and mineral resources. A WAAC equal to or marginally higher than the Parm elia Pipeline WAAC (8.3%) should be considered. A WAAC of 8.3 –8.5% seems reasonable.

In reference to the betas used, it seems wrong to average the main customers' betas and then conclude that figure represents the beta for the Goldfields Gas Pipeline. Diversification of customers would reduce the risk below average based on the covariance of the various companies' risk to that of the market and each other.

3. Long Term Contracts

The issue of "long term contracts" is canvassed. One third of the capacity currently contracted expires in 5 years and all the contracts expire in 16 years.

Gas contracts overseas have shortened significantly over the last decade. In the USA a contract of 2 years is now considered a long term contract.

It is improbable that demand in the Goldfields will drop significantly in either 5 years or 16 years while advancing technology is able to discover and exploit lower grade and concealed mineral deposits. This pipeline services and traverses the Hamersley Province (iron ore), the Bangemall Basin (gold) and the Eastern Goldfields Greenstone Belts (gold and nickel sulphides and laterite's)

4. General

Since the construction of the Goldfields Gas Pipeline three and a half years ago, high delivered gas prices have been in place because of poor legislation and poor oversight of the project through the existing Agreement Act.

If this pipeline had been regulated in the past, as have other monopoly pipelines, the tariffs for gas transmission to Kalgoorlie-Boulder would be about $2.00/GJ to Kalgoorlie.

The task of the regulator is made difficult given the history of "regulating" this monopoly pipeline.

The Regulator should reduce the WAAC from 12.2 to 8.3–8.5% and the Capital Base calculation should be examined to ascertain the effect of infrastructure bonds on the DAC or actual capital cost of the pipeline and reject the three factors/amounts used to adjust up the Capital Base.

End of Submission.