

Anaconda

8 March 2000

Mr Robert Pullella
Office of Gas Access Regulation
Level 6 Governor Stirling Tower
197 St Georges Terrace
PERTH WA 6000

Dear Mr Pullella

Re: Submission to the Western Australian Gas Regulator on the Proposed Access Arrangement for the Dampier to Bunbury Natural Gas Pipeline

Anaconda would like to make the following comments regarding the proposed Access Arrangement:

Reference Tariffs

a) Initial Capital Base

The most contentious point in the Epic Energy proposal is the value assigned to the initial capital base. Epic have assigned an excessive value of \$2.570 billion, their purchase price plus acquisition costs.

The code generally requires the initial capital base to ordinarily fall between the depreciated actual cost (DAC) and the depreciated optimal replacement cost (DORC). Epic have not defined values for these limits, ie. DAC and DORC. It is necessary to understand these values to ensure that the value used is reasonable. The Regulator must develop likely values for the two boundary conditions before making their assessment of the initial capital base. In fact the figures for DAC and DORC should be readily available from government.

It is understood provision is made in the Code to use other appropriate methods for valuation, including any recent purchase price for the asset. Care must be taken when using this approach to ensure that purchase premiums are not included in the price.

In addition a comparison must be made between the purchase price and replacement cost. Users must not be penalised for the competitive bidding process encouraged by the State Government. In the specific case of the Dampier to Bunbury Natural Gas Pipeline the price paid was well in excess of the optimal replacement cost.

Consideration should be given as to whether lower prices, with associated lower tariffs were actually offered, and the price that alternative bidders were prepared to pay.

A reduced value for the initial capital base would have a marked effect on the reference tariff structure for the pipeline.

b) Regulatory Rate of Return

Previous decisions by the ACCC and other State Regulators have arrived at values for the weighted average cost of capital of 7.5% to 7.75%. This value needs to be re-examined given the recent increases in interest rates, however Anaconda feel the value of 8.6% proposed by Epic Energy is too high. Particularly with the lack of risk associated with the pipeline, given the large quantity of upstream reserves and the significant, and growing, downstream market. When combined with an excessive initial capital base, an inflated tariff structure results.

c) Non-capital costs

The structure for the non-capital costs is clearly defined in the Access Arrangement. A major point of concern is the increase of operating costs over the life of the Access Arrangement. Previous decisions have recognised the need for pipeline operators to target cost reductions and continuous improvement over the life of an Access Arrangement. There is no evidence of this in the Epic proposal.

d) Determination of Reference Tariffs

The proposed tariff structure uses the philosophy that all costs for the pipeline are recovered in each of the defined supply zones, dependant on throughput. This approach appears reasonable but the Regulator must ensure that capital costs are allocated correctly to each zone. Otherwise the tariffs in some zones may be excessive and lead to over-recoveries by Epic Energy.

Benchmarking

Minimal benchmarking data is provided by Epic Energy for their pipeline. There are many measures used by pipeline owners throughout the world to measure the performance of their pipelines. Anaconda recommend that the Regulator ask Epic Energy to revisit this area of their submission and provide benchmark data.

One exercise which should be carried out is the comparison of the cost (c/GJkm) for gas in each defined supply zone in the pipeline. This would enable all users to see which zones were assuming a high proportion of the cost recovery. Users who were being subjected to excessive tariffs would be identified and appropriate action to remedy the situation could be taken.

All the above issues should be considered by the Regulator in assessing the suitability of the proposed Access Arrangement for the Dampier to Bunbury Gas Pipeline.

Yours sincerely

Simon Lill
Project Development